HOUSE RESEARCH ORGANIZATION bill analysis | 5/2/2005 | HB 3460 Baxter (CSHB 3460 by Crabb)

SUBJECT: Changing the calculation of the rate of interest paid on utility deposits

COMMITTEE: Regulated Industries — committee substitute recommended

VOTE: 5 ayes — P. King, Hunter, R. Cook, Crabb, Hartnett

0 nays

2 absent — Baxter, Turner

WITNESSES: For — John Fainter, Association of Electric Companies of Texas, Inc.; Michael Jewell, Direct Energy, CPL Energy, and WTU Retail Energy; (*Registered, but did not testify*: Jose Camacho, Valor Telecom; Brad Denton, Texas Telephone Association; Mike Williams, Texas Electric Cooperatives)

Against — None

BACKGROUND: Utilities Code, ch. 183 governs utility deposits made by customers of water, electric, gas, or telephone utilities. Sec. 183.003 requires on December 1 of every year that the Public Utilities Commission (PUC) set the annual interest rate on deposits at an amount greater than the lesser of:

- 85 percent of the average rate paid over the previous 12-month period on U.S. Treasury bills (T-bills) with a 12-month maturity date; or
- 12 percent.

The rate must be at least 6 percent.

DIGEST: CSHB 3460 would require that the PUC set the annual interest rate on utility deposits at the average rate paid over the previous 12-month period on T- bills with a 26-week maturity date. It would repeal the 6-percent minimum and 12-percent maximum limits on interest rates on deposits

The bill would take effect September 1, 2005.

SUPPORTERS SAY:

By mandating that utilities pay an interest rate set at the rate for a six-month T-bill, CSHB 3460 would implement a recommendation from the PUC's 2005 Scope of Competition report and ensure that interest rates on deposits reflected market rates. Currently, utilities must pay a rate of between 6 percent and 12 percent on deposits. While this rate may have been reasonable while interests rates were higher, current rates on short-term investments are well below 6 percent, requiring utilities to pay dividends on deposits that likely are higher than they could receive through investing those funds. CSHB 3460 reasonably would tie rates to the rate paid on a six-month T-bill, providing a fair return on funds that consumers paid in the form of a deposit.

The current rate for a six-month treasury bill is about 3 percent. Although 6 percent may have seemed like a reasonable rate in the mid-1990s, this rate is far above what most financial institutions currently are willing to pay on deposits. Utility deposits even could be viewed as attractive investment opportunities in the current market, potentially leading customers to overpay on deposits that they know would guarantee them a favorable rate of return. In order to normalize the rate that deposits yield, the Legislature should remove the arbitrary 6-percent floor and 12-percent ceiling on these funds.

Because the U.S. Treasury no longer sells 12 month T-bills, it is important that this part of statute be amended and that rates be based on the full rate of the 26-week T-bill. In addition, because deposits are likely to be held only over the short term, the interest rate associated with the six-month T-bill would be appropriate. Utilities are not in the banking business, and it is important that there be a transparent and fair rate on utility customer deposits.

OPPONENTS SAY:

CSHB 3460 would decrease the yield consumers received on the deposits they made for utility service. Consumers often have no choice but to make these deposits, and they deserve to earn a reasonable rate of return on these funds. Utilities that receive these deposits are free to invest them in assets other than T-bills and easily could receive a higher rate of return than the modest level they would be required to pay out. Utilities could see their profits increase while families who had met their credit obligations to utilities would receive less money when their deposits were returned.

CSHB 3460 could have the unintended consequence of encouraging utilities to demand larger deposits from their customers. If a utility projected that it could receive a higher rate of interest on a deposit than it would have to pay back to the customer, it would be in the utility's economic interest to draw more money from its customers. The Legislature in the past has encouraged utilities to collect only the minimum deposit that is necessary, and this bill would run counter to that policy goal.

NOTES: The committee substitute added an effective date and made other non-substantive changes.

The companion bill, SB 1747 by Fraser, passed the Senate on the Local and Uncontested Calendar on April 21.