INTERIM JOINT COMMITTEE ON APPROPRIATIONS AND REVENUE

Minutes of the 2nd Meeting
of the 2022 Interim

July 6, 2022

Call to Order and Roll Call

The 2nd meeting of the Interim Joint Committee on Appropriations and Revenue was held on Wednesday, July 6, 2022, at 1:00 PM, in Room 149 of the Capitol Annex. Representative Jason Petrie, Chair, called the meeting to order, and the secretary called the roll.

Present were:

Members: Senator Christian McDaniel, Co-Chair; Representative Jason Petrie, Co-Chair; Senators Danny Carroll, Donald Douglas, David P. Givens, Alice Forgy Kerr, Morgan McGarvey, Stephen Meredith, Michael J. Nemes, and Stephen West; Representatives Lynn Bechler, Danny Bentley, Randy Bridges, Joseph M. Fischer, Ken Fleming, Chris Fugate, Al Gentry, David Hale, Mark Hart, Bobby McCool, Jason Nemes, Ruth Ann Palumbo, Josie Raymond, Brandon Reed, Steve Riley, James Tipton, and Lisa Willner.

Guests: Perry Nut, Staff Economist, Legislative Economic Analysis, Legislative Research Commission; Jon Roenker, Chief Economist, Legislative Economic Analysis, Legislative Research Commission; Jim Gray, Secretary, Kentucky Transportation Cabinet; Jim Henderson, Executive Director/CEO, Kentucky Association of Counties; Jennifer Kirchner, Executive Director, Kentuckians for Better Transportation; John Hicks, State Budget Director, Office of the State Budget Director; Sandy Williams, Executive Director, Kentucky Infrastructure Authority (KIA); Perry Newcom, Judge Executive, Crittenden County; Brad Snyder, Judge Executive, Henderson County; and Jeff Hohn, President/CEO, Kenergy.

LRC Staff: Cynthia Brown, Sarah Watts, Hope Rowlett, and Ashton Thompson.

Approval of Minutes

A motion was made and seconded to approve the minutes of the July 6, 2022, meeting of the Interim Joint Committee on Appropriations and Revenue. The motion passed by voice vote.

Motor Fuels – Average Wholesale Price

Perry Nut, Staff Economist, Legislative Economic Analysis, Legislative Research Commission; Jon Roenker, Chief Economist, Legislative Economic Analysis, Legislative

Research Commission; Jim Gray, Secretary, Kentucky Transportation Cabinet; Jim Henderson, Executive Director/CEO, Kentucky Association of Counties; and Jennifer Kirchner, Executive Director, Kentuckians for Better Transportation, testified concerning the average wholesale price (AWP) of motor fuels in Kentucky.

Mr. Nutt explained that the motor fuels tax in Kentucky has three parts: the excise tax, the supplemental highway user tax, and the petroleum storage tank environmental assurance fee. The excise tax is nine percent multiplied by the AWP. The AWP is determined through a survey of fuel dealers conducted in the first month of each quarter (July, October, January, and April) and the average of the four quarterly survey values from the previous fiscal year is used to set the excise tax. By statute, the annual change in the AWP is limited to plus or minus 10 percent and cannot be below the statutory minimum of $2.177 per gallon. The supplemental tax is fixed at five cents per gallon for gasoline and two cents per gallon for diesel. These two parts of the overall tax are deposited into the Road Fund. The petroleum storage tank environmental assurance fee is fixed at 1.4 cents per gallon and is deposited into that specific fund.

The most recent change to Kentucky's motor fuels tax occurred during the 2015 Regular Session with the passage of House Bill (HB) 299. Prior to HB 299, the motor fuels tax was adjusted on a quarterly basis and the motor fuels tax was expected to decline by 10 cents per gallon during the 2015 fiscal year (FY). HB 299 set the minimum AWP used to calculate the excise tax at $2.177 for the fourth quarter of FY 2015 and every quarter in FY 2016. With this action by the General Assembly, the minimum excise tax rate was increased from 16.1 cents per gallon to 19.6 cents per gallon. Since 2016, the AWP from the annual survey has been below the statutory minimum with the passage of HB 299. Therefore, the motor fuels tax on gasoline has remained the same at 26 cents per gallon.

In response to questions from Representative Petrie, Mr. Nutt said that Tennessee's motor fuels tax on gasoline is 27.4 cents per gallon. Missouri's motor fuel tax is 22.4 cents per gallon and is the only surrounding state that has a lower tax than Kentucky. The primary reason Illinois, Indiana, Virginia, and West Virginia have a higher motor fuels tax is because those states apply a wholesale sales tax to motor fuels sales.

Prior to 2004, there was no change in the motor fuels tax rate because the AWP was below the statutory minimum of $1.11 per gallon. After 2004, the AWP and motor fuels tax increased by approximately 10 percent annually. The motor fuels tax peaked in the first quarter of 2015 at 32.5 cents per gallon but fell quickly throughout the fiscal year as the AWP declined.

Motor fuels tax receipts are a function of the motor fuels tax rate and taxable gallons. Taxable gallons are relatively stable and aren't significantly affected by fuel prices. There are 2.1 billion gallons of gasoline and one billion gallons of diesel fuel subject to the tax and yield on average $31.6 million for each one cent of tax imposed. A constant motor fuels tax rate since 2016 and low variability of taxable gallons sold have produced only modest growth in motor fuels tax revenues since 2106.

The road fund is largely dependent on the motor fuels tax and the motor vehicle usage tax. As the AWP of gasoline increased from 1996 to 2014, the motor fuels excise tax and road fund receipts both increased. However, during the recession, the road fund experienced a two year decline as Kentucky motor vehicle sales fell sharply. Motor fuels tax receipts have been relatively stable since 2016 due to a constant motor fuels tax rate and limited variation in taxable gallons.

In response to a question from Representative Petrie, Mr. Nutt said that based on 11 months of collections and current observations, expected revenues to the road fund will be close to the expected Road Fund revenues.

Motor fuels tax revenue is shared by allocating 1.4 cents per gallon to the Underground Storage Tank Fund and 2.1 cents per gallon to the road fund. After these deductions, 51.8 percent of motor fuels tax receipts stay in the road fund and the remaining receipts are shared with local government entities.

The AWP of gasoline determines the motor fuels tax rate unless it exceeds the statutory maximum AWP. In FY 2022, the AWP per gallon was $2.512 but the maximum AWP is $2.395 per gallon. Therefore, the maximum AWP is used to determine the excise tax rate for FY 2023. In FY 2023, the motor fuels tax rate would have been statutorily set at 28 cents per gallon of gasoline, including the excise tax of 21.6 cents; the supplemental tax of 5 cents; and the petroleum storage tank environmental assurance fee of 1.4 cents. However, an emergency regulation was filed by the Executive Branch on June 2, 2022, to keep the motor fuels tax at its current level of 26 cents per gallon. It is estimated that this will result in a loss of $16.4 million to the road fund and $15.2 million in motor fuels tax revenue sharing for one half of the current fiscal year. Savings to commercial purchasers are estimated to be $7.5 million for one half of the fiscal year.

In response to a question from Representative Petrie, Mr. Nutt said that the general fund and road fund estimates are determined by the Consensus Forecasting Group and may be modified by the General Assembly. In December 2021, the Consensus Forecasting Group incorporated an increase in motor fuels tax of 1.6 cents per gallon for FY 2023.

In response to a question from Representative Gentry, Mr. Nutt said that there is no data yet to explain why there was an increase in motor vehicle usage tax receipts FY 2021 but it could be attributed to an increase in the value of motor vehicles.

In response to a question from Representative Bentley, Mr. Nutt said that based on national data from the Energy Information Administration, commercial fuels is defined as Class 3 trucks (14,000 gross vehicle weight rating and above). In response to another question from Representative Bentley, Mr. Nutt said that jet fuel is not taxed under the motor fuels tax statute. Instead, it is subject to the sales tax.

Secretary Gray said that Governor Beshear has taken a number of steps to help Kentuckians who are struggling in this volatile economy. These steps include suspending a scheduled two cents per gallon increase in motor fuel taxes.

The motor fuels tax is 24.6 cents per gallon and has not increased since April 1, 2015. The governor consulted the Kentucky Transportation Cabinet prior to issuing the emergency regulation and the cabinet assured the governor that suspending the two cent increase would have no material impact on the cabinet's budget. According to the Office of the State Budget Director, the estimated impact to the road fund is $28.2 million through mid-January. This equates to 1.6 percent of the enacted road fund revenue estimate for FY 2023. Like Kentucky families and businesses, the Kentucky Transportation Cabinet will adapt and adjust to get through the suspension period.

Even with suspension of the two cent increase, it is estimated that local governments will receive about $17 million dollars more in revenue. This represents an increase of $8 million for the rural secondary road program, $6.7 million for county road aid, and $2.8 million for municipal road aid. Local governments will also receive revenue sharing funds on schedule, with the first payment issued at the beginning of August.

Governor Beshear will propose to the next General Assembly that funds from the general fund surplus be used to restore revenue sharing to the level included in the budget for FY 2023.

Secretary Gray spoke to effects of inflation on the cabinet's operations. The Kentucky Transportation Cabinet and Ohio Department of Transportation recently hosted an industry forum in Covington for bidders who were interested in the Brent Spence Bridge project. Contractors present at the forum were concerned that suppliers would not guarantee prices for more than 30 days.

The Cabinet's Construction Procurement division sets a fair and reasonable engineer's estimate for individual projects. Overall, project costs have been rising. A bid was submitted for a U.S. 127 relocation project over the Wolfe Creek Dam, but the bid was rejected by the awards committee because it was 17 percent over the engineer's estimate. The engineer's estimates were adjusted to reflect inflation, and bidding was reopened, but the bids still exceeded the new estimates.

Due to a shortage in supplies, the cabinet has temporarily modified paint specifications to allow a broader spectrum of colors. A shortage of cement and extended lead times for electrical components have also contributed to some project delays. However, the cabinet is adapting to these shortages to manage projects effectively.

In response to a question from Representative McCool, Secretary Gray confirmed that all budgeted road fund projects will be implemented this year. While different project phases may adjust the letting calendar, there is no plan to adjust anything at present.

In response to a question from Representative Nemes, Secretary Gray said that he advocated for raising the motor fuels tax in 2021, but those economic conditions differ from today's conditions. A little help is better than no help at all. Responding to comments made by Representative Nemes, Secretary Gray said that the Bipartisan Infrastructure Law (Infrastructure Investment and Jobs Act) will provide $210 million each year for five years to fund projects for bridges and highways.

In response to a question from Senator Kerr, Secretary Gray said he did not know how many women are employed by the Kentucky Transportation Cabinet making $50,000 or more a year, but would provide that information in the future.

Mr. Henderson discussed the impact of the gas tax freeze on counties. Fiscal courts within counties own and maintain half of the road miles and over a third of the bridges in the state. In many rural counties, closer to two-thirds of road miles are maintained by the fiscal courts within counties. Cities and counties maintain 50,000 road miles.

The motor fuels revenue sharing model allocates 18.3 cents for county road aid, 7.7 cents for municipal road aid, and 22.2 cents for rural secondary state roads. This formula makes the motor fuels tax particularly important to the counties and cities, more than the state as a whole. No portion of the motor vehicle usage tax on cars is returned to either a county or a city. While the state relies heavily on the motor vehicle usage tax, this portion of the Road Fund is not available to local jurisdictions.

Reporting just the facts, in the past ten years, the asphalt costs for road maintenance has doubled, from $50 per ton to more than $99 per ton. At the same time, the freeze in the gas tax represents approximately $5 million in reduced funding to local jurisdictions.

Jennifer Kirchner, representing Kentuckians for Better Transportation, testified that the effects of a gas tax freeze will only save $1 per month for the average Kentuckian and the Road Fund is projected to lose $35 million by January. If the freeze is extended through fiscal year 2022-2023, the loss would be approximately $60 million. The lost funds were included in the biennial transportation budget. The freeze cripples the funding mechanism and renders the current motor fuel tax system irrelevant. In the last eight years, little to no growth in the Road Fund has been realized. The Road Fund has not kept pace with rising costs and increased needs. The freeze contributes to chronic underfunding of transportation infrastructure.

Broadband Deployment

John Hicks and Sandy Williams indicated that the federal government has stepped up with funding, $300 million appropriated by the General Assembly, split $117.2 million funded by the American Rescue Plan Act (ARPA), Coronavirus State Fiscal Recovery Fund, and $182.8 million funded by the ARPA, Capital Projects Fund. Forty-seven awards were recently announced for $89.6 million in grant funding. This round of awards was capped at $5 million for each award. These will result in $204 million in total investment and more than 34,000 households and businesses will be covered in 36 different counties.

The next steps for broadband deployment include the creation of the Office of Broadband Development, application development for the next round of grant funding incorporating HB 315 and the Infrastructure, Investment and Jobs Act requirements, and finally developing the program for pole replacement subsidies. Currently, the Office is searching for an Executive Director, establishment of duties and responsibilities, including the federal requirements with state-wide mapping to location specificity.

The Broadband, Equity, Access, and Deployment (BEAD) program at the federal level provides $42.45 billion nationwide. An estimate of Kentucky’s allocation is approximately $700 million. This process will take a while to implement in calendar year 2023, with a five-year action plan, to engage the entire strategic plan for the Commonwealth.

The Digital Equity Act includes three spectrums: broadband, devices, and skills. All three spectrums must be present to have users most successfully work on the internet. A separate plan will be needed to access approximately $20 million over five years, with an implementation plan which aligns with the BEAD action plan. The ultimate outcome is not only to provide broadband to all but make it useable for all.

HB 315 also included $20 million for pole replacement subsidies from the Rural Infrastructure Improvement Program. This program is set up to be a reimbursement of expenses for the removal or replacement of existing utility poles that are necessary for broadband deployment. Applications will be available by September 1, 2022.

Jeff Hohn testified that as a PSC-regulated utility, Kenergy is now ready to proceed following the passage of HB 315. Some pre-engineering on the Kenergy project has been done, and the business is proceeding to the “make ready stage” in preparation for construction. Kenergy serves approximately 59,000 meters in their service areas, with 35,000 being considered unserved or underserved, or 60 percent of their membership. Kenergy is looking at 3 to 5 year buildout with approximately 150 to 200 miles per year.

Brad Snyder testified it has been a slow roll out for the PSC-counties. For a person looking to relocate, the first question in determining location is inquiring about internet viability and speed. Beyond that question, others are about cost and school districts. His message for rural counties is urgency.

Perry Newcom testified that he represents even more rural counties than Judge Snyder and he appreciates the creation the Office of Broadband Deployment as a central point of contact. We all want the same outcome, to provide broadband service to all Kentucky without regard to where you live. Not a day goes by without the office receiving a call inquiring which area of the county can receive a reliable, affordable, and high speed internet service. In most cases, the answer is that it is just not available. Two examples of struggles in Crittenden County include: (1) a software engineer for a nation-wide company was able to work individually with a big-box provider to turn on business fiber to meet his needs, but he is paying over $600 each month for 50/50 service; and (2) artists for Bone Fish Grill are paying over $700 each month for a 25/25 service. This is an extreme hardship.

Federal Funds for Water and Wastewater Projects

John Hicks testified that $250 million was appropriated in the 2021 Regular Session out of the American Rescue Plan Act and another $250 million in 2022 Regular Session, plus a set of other project specific funding was appropriated in addition to the second $250 million. Of the first $250 million, $200 million has been committed and approved. A portion of the remaining $50 million will be reserved for cost escalations, which has become the norm for most projects. This was a very successful roll out of the first round of grant program funding. The next round will begin with a call for project starting in July, based on local consensus. A list of funding available by counties is on the KIA website: www.kia.ky.gov

In response to a question from Representative Petrie, Mr. Hicks said that a total of approximately $540 million will be delivered to the local jurisdictions for drinking water and wastewater projects and Ms. Williams testified that applications were about three times the amount of money provided. There will always be a need.

In response to a question from Senator Carroll, Ms. Williams stated that regionalization of services is always considered and we would hope that the utilities would give consideration to that when they participate in their water management councils. Mr. Hicks stated that the Division of Water and our Emergency Management Operations have been working with local officials within the City of Marion to determine the best next step and what is a permanent step to provide water. They are currently engineering that first step for the City of Marion. Part of that effort may lead to a need for state funding to deal with that emergency, but we have not gotten to that point yet.

A comment from Senator McCool included information on an area in Martin County where people must purchase a token and take that token to a central place to receive drinking water and then take that water back to their homes. Service could be provided from Johnson County if a pump was installed. The point is that people need drinking water.

Representative Petrie announced that a packet of information was provided to each member from the Personnel Cabinet. This information was presented earlier in the morning during a Budget Review Subcommittee meeting involving personnel. This information will be used during a meeting with the Cabinet within the next 14 days with the Co-Chairs and other selected committee members to understand how to move forward with personnel compensation issues.

With there being no further business, the meeting was adjourned at 2:49 p.m.