Legislative Fiscal Bureau
One East Main, Suite 301 • Madison, WI 53703 • (608) 266-3847 • Fax: (608) 267-6873

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PECFA -- Revenue Obligation Authority (Commerce)

[LFB 2003-05 Budget Summary: Page 104, #17]

CURRENT LAW

The petroleum environmental cleanup fund award (PECFA) program reimburses owners for a portion of the cleanup costs of discharges from petroleum product storage tank systems and home heating oil tank systems. The program is funded from the segregated petroleum inspection fund. Revenue to the fund is generated from the 3¢ per gallon petroleum inspection fee assessed on all petroleum products that enter the state, including gasoline, diesel and heating oil. The program is authorized $342,000,000 in revenue obligation authority, including $270,000,000 in 1999 Act 9 and $72,000,000 in 2001 Act 16. The Building Commission has issued the entire $342 million in revenue obligations (typically long-term bonds or short-term notes), to fund the payment of claims under the PECFA program. The first use of petroleum inspection fees is payment of revenue obligation debt service, and the remainder of petroleum inspection fees are used for PECFA awards and administration, Commerce petroleum inspection programs, and other brownfields, clean air and environmental programs. The PECFA program is appropriated $68,000,000 petroleum inspection fund SEG each year in a biennial appropriation for PECFA awards.

GOVERNOR

Provide $115,000,000 in revenue obligation authority for the PECFA program, to increase revenue obligation authority under the program from $342 million to $457 million.

DISCUSSION POINTS

1. The backlog of PECFA claims that had been received and had not been paid

exceeded $200 million during the months of June, 1997, through February, 2000. Prior to the 1999 Act 9 authorization of revenue obligations, Commerce used an appropriation of $94,131,700 annually for payment of PECFA claims. Issuance of revenue obligations under the 1999 Act 9 authorization allowed Commerce to pay the backlog of PECFA claims. In 2001 Act 16, an additional $72 million in revenue obligations were authorized, for total authorization of $342 million, and the PECFA claims appropriation was decreased to $68,000,000 annually, to adjust for revenues needed to pay revenue obligation debt service. The additional revenue obligations were issued in the fall of 2001 and in 2002, and all proceeds have been used to pay PECFA claims. A cumulative total of $200 million in long-term revenue obligations have been issued with a weighted average interest cost of 5.33%. The remaining $142 million in issued obligations consists of short-term commercial paper, with a current weighted average interest rate of 1.6%.

2. Since the first claims were paid with revenue obligation proceeds in 2000, the claim backlog has been significantly reduced. Currently, claims are generally being reviewed and paid within two to four months of receipt. As of April 1, 2003, Commerce had received 516 PECFA award applications totaling $31.7 million that had not been paid. The backlog consists of two components, claims where review had not been completed and claims that have been reviewed and are awaiting payment. The first component consists of 172 claims for $12.3 million that were being reviewed by staff. The second component of the backlog consists of 344 claims for $19.4 million that had been reviewed and would be paid within approximately two to four months.

3. As of April 1, 2003, a total of over $1.27 billion in PECFA payments have been made for partial or full cleanup at 10,623 sites. Of the total payments, $917.7 million (72%) has paid for completion of cleanup at 8,766 closed sites (82.5%). The remaining $356.8 million (28%) has paid for partial cleanup at 1,857 open sites (17.5%). Almost 5,400 sites have been closed since April, 1999.

4. The amount of PECFA claims received exceeded $160 million annually in each of 1995-96, 1996-97 and 1997-98. The amount of claims received (net of ineligible costs) decreased to $70 million in 1998-99 and $95 million in 1999-00. Claims began to increase in 2000-01, to almost $110 million. This may have been partly due to more capital being made available at PECFA sites after the claim backlog was paid in 1999-00 with revenue obligation proceeds. The amount of claims received increased to $150 million in 2001-02, of which approximately $25 to $50 million may have been submitted in response to two 2001 Act 16 provisions that specified, as of September 1, 2001, that: (a) if an applicant submits a final claim more than 120 days after receiving notification from DNR or Commerce that no further action is necessary at the site, interest costs incurred more than 60 days after receiving the notice are not eligible for reimbursement; and (b) an owner or operator may submit a claim annually if the applicant has incurred $50,000 in unreimbursed eligible PECFA costs and at least one year has elapsed since submission of the last claim.

5. The large amount of claims received in the late 1990s was due, in part, to the December 22, 1998, federally-established deadline whereby owners with petroleum storage tanks subject to federal regulations were required to replace or upgrade the tanks to meet current leak

prevention and leak detection standards, or to stop using the tanks. This deadline applied to the large majority of PECFA-eligible sites, including commercial underground petroleum product storage tanks larger than 110 gallons and underground farm and residential vehicle fuel tanks larger than 1,100 gallons. If the owner or operator closed the tank instead of upgrading it, they were required to properly close and remove the tank within the following year (by December 22, 1999). Often, the point in time at which contamination was discovered was during the process of upgrading or removing the tank to comply with the 1998 deadline. Some tank owners regulated under state regulations rather than federal regulations (farm and residential tanks of 1,100 gallons or less, heating oil tanks over 4,000 gallons and aboveground storage tanks over 5,000 gallons) were required to upgrade, or to stop using, the tanks by May 1, 2001.

6. In 2002-03, the program received $80 million in claims as of April 1, 2003, and will likely receive a total of approximately $107 million in claims in 2002-03. Of this amount, approximately 4-5% of costs will be determined ineligible, for a net total of approximately $102 million in eligible claim costs received this year, or approximately $8.5 million per month. The June 30, 2003, backlog of submitted claims waiting to be paid will be approximately $43 million.

7. Commerce calculated that during the 12 months ending February, 2003, PECFA claims have been received at a rate of approximately $9.5 million per month, before deducting ineligible costs during claims processing. During the past six months, Commerce received an average of $8.8 million each month, before deducting ineligible costs. Commerce officials estimate that during the 2003-05 biennium, claims will continue to be received at a rate of approximately $9.5 million per month, resulting in demand of approximately $228 million during the 2003-05 biennium. Commerce does not make any adjustment in the estimate for ineligible costs or for a potential decrease in monthly incoming claims from past or future implementation of cost controls enacted in recent years.

8. Under the bill, there would be up to $251 million available for PECFA awards during the 2003-05 biennium, including $136 million SEG appropriated from the PECFA awards appropriation and $115 million in revenue obligation proceeds authorized in the bill. This amount would be sufficient to fund Commerce's estimate of $228 million in incoming claims during the biennium. The June 30, 2005, claim backlog would be approximately $20 million, or approximately two months of claims that would normally be in process at any given time.

9. Several cost control measures were enacted in 1999 Act 9 and 2001 Act 16. Some have been implemented, while others are still in the discussion stage. Since 1998, Commerce has directed over 250 sites through a competitive bid process for remediation costs, and estimates that between $30 and $45 million in cost savings were obtained in the past four years. The provisions for a $50,000 annual progress payment and elimination of eligibility of interest costs if the claim for a closed site is not submitted within 120 days after closure have resulted in claims being submitted sooner than if the provisions had not been enacted, reducing interest costs paid by the program.

10. In early 1999, Commerce and DNR promulgated emergency administrative rules COMM 46 and NR 746 at the direction of the Joint Committee for Review of Administrative Rules

to codify the procedures for classification of contaminated sites, definition of environmental risk and establishment of a risk protocol for evaluating sites. Permanent rules COMM 46 and NR 746, promulgated in early 2001, codified the 1999 Act 9 requirement that the agencies promulgate a rule for determining the risk to public health, safety and welfare and to the environment posed by petroleum discharges. Since then, many sites that did not have various environmental factors (such as free product or contamination in a drinking water well) have been closed with use of natural attenuation as the remediation method. Many sites have been closed with groundwater contamination that exceeds the groundwater enforcement standard exceedence when certain conditions were met, and, currently 1,865 PECFA and non-PECFA sites are listed on the DNR geographic information system registry. Further, 27 sites are listed that were closed with soil contamination that exceeds residual contaminant levels and 61 sites have both groundwater and soil contamination. In addition, there are 323 closed sites that are in the process of being placed on the GIS registry.

11. Between 2000 and August, 2002, Commerce held discussions with DNR and an administrative rule advisory group about how to implement additional cost control changes required by 1999 Act 9. Commerce has not submitted proposed administrative rule changes to the Legislature since Commerce and DNR promulgated COMM 46 and NR 746. The Department is evaluating the benefits of implementing the 1999 Act 9 requirement that Commerce promulgate a rule to identify ineligible costs to which a penalty would apply. The Department was required to establish usual and customary cost schedules for eligible costs, and has discussed possible wording of an administrative rule but has not promulgated a rule.

12. Commerce and DNR implemented the 1999 Act 9 bidding requirements by requiring all sites that had not committed to completing the site investigation and remediation for $60,000 or less to be bid, unless the site meets the requirements for bidding to be waived. The agencies anticipate that the use of the bidding process will replace the Act 9 requirement that the agencies use a joint decision-making process for setting remediation targets.

13. 1997 Act 27 authorized Commerce to promulgate administrative rules under which the Department would select service providers to provide investigation or remedial action services in specified areas. Commerce and DNR have discussed possible methods of implementing this provision and a joint agency committee is developing a pilot study that might use the process. However, no rules have been developed to date.

14. In the fall of 2000, Commerce began collecting information from lenders about past costs. As of January, 2003, Commerce believes it has received accurate data from over 90% of PECFA lenders that shows approximately $110 million in outstanding PECFA loans for incurred costs that have not been submitted. Commerce is also aware of approximately $10 million in costs incurred but not submitted by the bigger oil companies that do not take out PECFA loans. Under 1999 Act 9, Commerce is required to collect information from consultants that annually estimates the additional costs that must be incurred to complete the remedial action activities in compliance with the groundwater standards. In the fall of 2002, Commerce began collecting information from consultants and received data about approximately 2,500 sites, with no data reported for an

estimated 1,600 additional sites. Commerce estimates that the total costs yet to be incurred from reporting sites is $98.5 million, and that perhaps up to $50 million will be incurred for sites for which no data was reported. Thus, Commerce has recently calculated that at least $120 million in PECFA costs have been incurred but not submitted, and up to an additional $150 million will be incurred at sites the Department is aware of. There is an unknown amount of costs that have been incurred but that Commerce does not have information about, and an unknown number of sites with owners that have not notified Commerce that they will submit PECFA claims.

15. 1999 Act 9 required Commerce to conduct an annual review for medium- and low-risk sites, and Commerce and DNR to jointly conduct an annual review for high-risk sites and make a determination of the least costly method of completing the remedial action activities and complying with groundwater enforcement standards, to determine if natural attenuation will accomplish that, and to notify the owner or operator that reimbursement for remedial action is limited to the amount necessary to implement that method. Commerce officials recently indicated that they will use information gathered from consultants in the fall of 2002 to determine a process for annual review of sites.

16. Commerce officials have recently indicated that they are reluctant to promulgate further administrative rule changes to implement 1999 Act 9 provisions because they are discussing possible statutory changes to the program. The Department has not reconvened the advisory group that last met in August, 2002, and has not submitted any proposed statutory changes to the Legislature.

17. Debt service on the current $342 million in revenue obligations is anticipated to equal approximately $27.5 million in each of 2003-04 and 2004-05. Under the existing bond retirement schedule, debt service payments would increase to approximately $28.9 million in 2005-06, $42.5 million in 2006-07 and $41.3 million in 2007-08. Commerce estimates that the $115 million under the bill will be issued during the 2003-05 biennium, with $85 million of it issued in 2003-04 and $30 million in 2004-05. Debt service would increase by approximately $4.2 million in 2003-04, $8.2 million in 2004-05 and approximately $9.2 million annually beginning in 2005-06. The amount of debt service may vary, depending on the structure and timing of the issuance, and the amount of short-term versus long-term debt.

18. The following table shows the estimated condition of the petroleum inspection fund under the bill. During the 2003-05 biennium, $11.3 million annually would be appropriated for: (a) Commerce petroleum tank and inspection programs; (b) Department of Revenue collection of the petroleum inspection fee; (c) petroleum inspection fee refunds to eligible airlines; and (d) brownfields, clean air and environmental programs in the Departments of Commerce, Natural Resources, Transportation, Agriculture, Trade & Consumer Protection, and Military Affairs. Further, under the bill, beginning in 2004-05, the Department of Transportation motor vehicle emissions inspection maintenance program in southeastern Wisconsin would be shifted from the transportation fund to the petroleum inspection fund. The remaining funds would be used for PECFA awards, PECFA revenue obligation debt service and Commerce and DNR PECFA administration.

Petroleum Inspection Fund Estimated Condition
($ In Millions)

	2001-02 Actual	2002-03 Estimated	2003-04 Estimated	2004-05 Estimated
Opening Balance -- July 1	$18.4	$18.0	$20.1	$19.3
Revenues				
Petroleum Inspection Fee	$113.1	$113.7	$114.6	$118.8
Revenue Obligation Proceeds	30.0	62.2	85.0	30.0
Revenue Obligation Debt Service & Issuance	-22.5	-27.2	-31.7	-35.7
Interest Income and Other	0.6	0.4	0.3	0.4
Petroleum Bulk Tank Fees	0.9	0.9	0.2	0.2
Total Revenue	$122.0	$150.0	$168.4	$113.7
Total Revenue Available	$140.4	$168.0	$188.5	$133.0
Expenditures and Reserves				
PECFA Awards and Administration	$78.4	$71.2	$71.1	$71.0
PECFA Awards from Revenue Obligations	30.0	62.3	85.0	30.0
Other Existing Programs	12.7	12.4	11.3	11.3
DOT Motor Vehicle Inspection Program	0.0	0.0	0.0	6.3
Reserves, Lapses and Encumbrances	0.1	0.0	0.1	0.1
Total Expenditures	$121.2	$145.9	$167.5	$118.7
Less Transfers to the General Fund	-$1.2	-$2.0	-$1.7	-$1.7
Closing Balance -- June 30	$18.0	$20.1	$19.3	$12.6

19. The estimated annualized debt service costs of $38.1 million, beginning in 2005-06, would represent a debt service coverage ratio of approximately 3.1:1. That is, there would be approximately $3.10 of petroleum inspection fee revenue for every $1 of debt service to ensure sufficient revenues to pay debt service. A debt service coverage ratio of 3:1 or higher generally makes the obligations more attractive in the bond market. A lower debt service ratio, for example as low as 2:1, might be acceptable to the bond market if a higher interest rate is offered by the state when the obligations are sold. It is possible that obligations could be authorized in excess of the cumulative total of $457 million under the bill if needed in the future, while maintaining a debt service ratio of between 2:1 to 3:1.

20. As shown in the table of the estimated petroleum inspection fund condition, the fund is expected to have a June 30, 2005, closing balance of $12.6 million. The Committee could choose to appropriate this balance for PECFA claims. For example, if the PECFA claims appropriation would be increased by $6 million in each year, from $68 million to $74 million, the June 30, 2005, expected balance would be approximately $0.6 million.

21. If incoming claims are received at a rate closer to the six month average of $8.8 million, than the 12 month average of $9.5 million projected by Commerce during the 2003-05 biennium, and if approximately 4% of costs are deducted as ineligible, the net $8.5 million per month of incoming claims would total $204 million during the biennium ($247 million with the June 30, 2003, backlog of $43 million), instead of Commerce's estimate of $228 million ($271 million with the opening backlog). If the PECFA claims appropriation would be increased from $68 to $74 million annually , $82 million in revenue obligation authority would be sufficient to fund anticipated claim demand during the biennium, with a $17 million backlog on June 30, 2005. This represents approximately two months of claims that would normally be in process at any given time.

22. Given the cost controls that have been implemented, other cost controls previously enacted that are in the process of being implemented, and the federal deadline for most PECFA-eligible commercial underground tanks was December 22, 1998, it may be reasonable to expect claim levels to begin to decline during the biennium. If so, the need for revenue obligation authority would also decrease. For example, if the monthly average of incoming claims declines approximately 4% each January and June (to $8.6 million per month in July, 2003, $8.3 million in January, 2004, $8.0 million in July, 2004, and $7.6 million in January, 2005), claims would total approximately $195 million during the biennium ($238 million with the opening backlog). Further, if the PECFA claims appropriation would be increased by $6 million in each year, $75 million in revenue obligation authority would be sufficient to fund anticipated claim demand during the biennium, with a $15 million backlog on June 30, 2005 (two months of normal processing time).

23. If claim demand after June, 2005, decreases to equal to or less than the amount available from the claims appropriation after 2004-05, it is possible that revenue obligations provided in 2003-05 would be sufficient to fund long-term needs of the program. If demand stays above $6 million per month after June, 2005, it is possible that there would be a need for additional revenue obligations, or to review overall funding for the program.

24. If the Committee chooses to approve a level of revenue obligation authority sufficient for PECFA needs during the 2003-05 biennium, it could authorize $82 million or $75 million instead of $115 million in revenue obligations, provide an additional $6 million in each year for the PECFA claims appropriation, and review the need for revenue obligation authority during 2005-07 biennial budget deliberations, if necessary. However, it is possible that if the remaining $33 to $40 million of requested authority is not needed during the 2003-05 biennium, it would be utilized in 2005-06. If authorized at this time, it could be issued for PECFA payments as needed by Commerce.

25. Some would argue that no additional PECFA revenue obligations should be authorized until a thorough study is completed by the Legislature, state agencies, owners, consultants and other affected persons to determine how to reduce future PECFA costs to less than available revenue. After a study and any statutory or administrative rule changes would be made, a structure for future funding could be established.

26. Others would argue that $115 million or the alternatives of $82 million or $75

million of revenue obligations should be authorized to fund known PECFA costs of at least $120 million that have been incurred, but have not yet been submitted, and some portion of approximately $150 million in PECFA costs that are expected to be incurred in the future for known active sites.

27. An alternative to increasing the PECFA awards appropriation by $6 million in each year would be to transfer $6 million from the petroleum inspection fund to the general fund in each year of the biennium. An additional $12 million in revenue bonds would be required to meet anticipated claims demand.

28. If no additional revenue obligation authority is approved for the PECFA program by June 30, 2005, there would be an expected backlog of approximately $102 to $111 million in claims. PECFA site owners who submit a claim in June, 2005, would wait about 13 months for reimbursement under the program. Generally, claims would continue to accrue interest during this period.

ALTERNATIVES

1. Approve the Governor's recommendation to provide $115,000,000 in additional revenue obligation authority for the PECFA program, for total PECFA revenue obligation authority of $457,000,000.

2. Approve $82,000,000 in additional revenue obligation authority for the PECFA program. In addition, provide an additional $6,000,000 SEG in each year to increase the PECFA awards appropriation from $68,000,000 to $74,000,000 annually.

Alternative 2	BR	SEG
2003-05 FUNDING (Change to Bill)	- $33,000,000	$12,000,000

3. Approve $75,000,000 in additional revenue obligation authority for the PECFA program. In addition, provide an additional $6,000,000 SEG in each year to increase the PECFA awards appropriation from $68,000,000 to $74,000,000 annually.

Alternative 3	BR	SEG
2003-05 FUNDING (Change to Bill)	- $40,000,000	$12,000,000

4. Approve $94,000,000 in additional revenue obligation authority for the PECFA program. In addition, transfer $6,000,000 in each of 2003-04 and 2004-05 from the petroleum inspection fund to the general fund.

Alternative 4	BR	GPR
2003-05 REVENUE (Change to Bill)	$0	$12,000,000
2003-05 FUNDING (Change to Bill)	**-** $21,000,000	$0

5. Provide $87,000,000 in additional revenue obligation authority for the PECFA program. In addition, transfer $6,000,000 in each of 2003-04 and 2004-05 from the petroleum inspection fund to the general fund.

Alternative 5	BR	GPR
2003-05 REVENUE (Change to Bill)	$0	$12,000,000
2003-05 FUNDING (Change to Bill)	**-** $28,000,000	$0

6. Delete provision.

Alternative 6	BR
2003-05 FUNDING (Change to Bill)	**-** $115,000,000

Prepared by: Kendra Bonderud