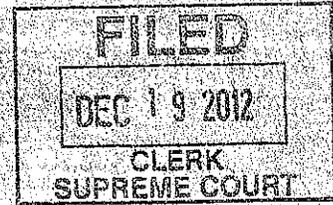


COMMONWEALTH OF KENTUCKY
SUPREME COURT
NO. 2012-SC-000071-D



ERVIN KLEIN, THOMAS C. RECHTIN,
EDDIE NOEL and DAVID MILES

APPELLANTS

vs.

JONATHAN MILLER
In his official capacity as the Secretary of the
Finance and Administration Cabinet

MARY LASSITER
In her official capacity as State Budget Director

and

RICHARD MOLONEY
In his official capacity as Commissioner of the
Department of Housing, Buildings and Construction

APPELLEES

APPEAL FROM COURT OF APPEALS
NO. 2010-CA-000750

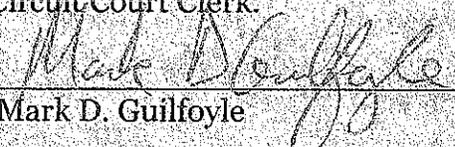
APPELLANTS' BRIEF

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CERTIFICATE OF SERVICE

I hereby certify that a true and accurate copy of Appellants' Brief was served via ordinary mail this 17th day of December, 2012, upon Hon. M. Stephen Pitt and Hon. Christopher W. Brooker, Wyatt, Tarrant & Combs, 500 West Jefferson Street, Suite 2800, Louisville, KY 40202; and Hon. Thomas Wingate, Franklin Circuit Court, 669 Chamberlin Ave., Frankfort, KY 40601. Appellants did not withdraw the record from the Franklin Circuit Court Clerk.


Mark D. Guilfoyle

INTRODUCTION

This is a case in which four (4) licensed building contractors appeal from a summary judgment dismissing their claim that license and permit fees collected by the Department of Housing, Buildings and Construction (“HBC”) to fund enforcement of the state’s building code are not subject to transfer into the General Fund by the legislature in a budget bill. The Court of Appeals affirmed the grant of summary judgment in Appellees’ favor.

Based on a long line of cases after *City of Henderson v. Lockett*, 163 S.W. 199 (Ky. 1914), HBC fees are assessed pursuant to the state’s police power and may not be used to supplement the general tax needs of state government. Separately, Appellants’ claim is supported by *Beshear v. Haydon Bridge*, 304 S.W.3d 682 (Ky. 2010), which holds that the legislature has “simply no authority to transfer private agency funds.” (*Id.* at 705) Finally, the legislature’s transfer of HBC funds violates Sections 2, 15, 51, 180 and 242 of the Kentucky Constitution, as well as the Equal Protection Clause.

STATEMENT CONCERNING ORAL ARGUMENT

Appellants respectfully request oral argument, which may assist the Court in discerning the application of its precedents -- in two distinct line of cases -- to this cause. As well, this appeal implicates several sections of Kentucky's Constitution, and oral argument may help to explicate their application to this cause.

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May It Please The Court:

I. STATEMENT OF THE CASE

This action was commenced in the Franklin Circuit Court on June 25, 2008. In the 2008–2010 biennial budget bill, the General Assembly directed transfers of fees from the Department of Housing, Buildings and Construction (“HBC”) to the General Fund “notwithstanding the statutes or requirements of the Restricted Funds enumerated.” (2008 Ky. Acts, c. 127 at 419 (item 29), 422, 425) The budget bill ratified Governor Beshear’s Executive Order 2008-011, which transferred \$6,495,200 from the HBC’s current accounts to the General Fund. (TR 45) Additionally, the budget bill ordered that \$3,700,000 be taken from fees to be collected in the future by HBC during 2008-2010. All these transfers totaling \$10,195,200 would come from license, permit and inspection fees assessed and collected by HBC and its related agencies to enforce the State Building Code for “life safety from hazards of fire, explosion and other disasters.” (KRS 198B.050(2)) Appellants allege that converting these non-tax fees to General Fund taxes violates statutory and constitutional proscriptions.

Ten different categories of Building Code fees are fixed in differing amounts by five statutory boards and the HBC Commissioner.¹ Activities financed by license and permit fees collected by HBC are paid from trust or revolving fund accounts.² Each category of HBC fees is a “restricted fund.” (KRS

¹KRS 198B.090(10); KRS 198B.490; KRS 198B.615; KRS 198B.676(1); KRS 198B.710(1) and (2); KRS 227.620(5); KRS 227A.050(1); KRS 236.130(1) and (2); KRS 227.487(2); KRS 318.136.

² KRS 198B.095; KRS 198B.615; KRS 198B.676(2); KRS 198B.710(2); KRS 227.620(5); KRS 227A.050(1); KRS 236.130(3); KRS 318.136.

48.010(13)(f)) These accounts are distinguished from the General Fund, which is “all monies, ***not otherwise restricted***, available for the operation of State government.” (KRS 48.010(13)(a)) (Emphasis added)

On January 19, 2010, the trial court entered summary judgment sanctioning the transfers (“Summary Judgment”). In doing so, the trial court made two very significant observations. First, the trial court found that “HBC accounts are funded by regulatory fees charged pursuant to the State’s police power.” (Summary Judgment at 3, fn. 5) That obvious observation necessarily compels examining the 100-year-old line of cases holding police power fees cannot be used to produce revenue for purposes not related to regulation or enforcement. That line of cases supports summary judgment ***in Appellants’ favor***.

Second, the trial court declared that “HBC fees are not a tax.” (*Id.* at 7) The trial court and all parties to this appeal agree that taxes are “public funds” and, as such, may be transferred to the General Fund in a budget bill. In concluding that HBC funds are “public funds,” however, the trial court improperly looked to the “purpose” of HBC and its fees rather than to the “source” of the fees. The trial court said:

In summary, the various aspects of HBC indicate that its purpose, and the purpose of the fees that it collects, are public. The fees that it collects are paid in the interest of regulating housing, buildings, and construction in the Commonwealth and spent in the interest of regulating housing, buildings, and construction in the Commonwealth -- a quintessentially public purpose.³

³January 19, 2010 Opinion and Order at 9.

As will be seen, the proper focus should be on the **source** of the fees. Such a focus compels the conclusion that HBC fees are “private funds” not subject to transfer to the General Fund.

On January 28, 2010, Appellants filed a CR 59.05 Motion to Alter, Amend or Vacate, asking the trial court to apply *Beshear v. Haydon Bridge*, 304 S.W.3d 682 (Ky. 2010), to this case. By Order entered March 26, 2010 (the “CR 59.05 Order”),⁴ the trial court denied Appellants’ motion and reasserted that HBC fees are “public funds”:

Plaintiff’s contentions merit consideration in light of the recent *Haydon Bridge* ruling; ultimately, however, the distinctions between *Haydon Bridge* and the instant case, which we noted in our original Order, are still relevant and demonstrate that our ruling is, in fact, consistent with *Haydon Bridge*.

The trial court’s rationale distinguishing *Haydon Bridge* rested largely on characterizing assessments as private funds, while designating police power fees as public funds.

Appellants timely filed an appeal; and, on January 6, 2011, the Court of Appeals issued an “Opinion Affirming.” In doing so, the Court of Appeals twice noted the HBC’s “policing power” (*Id.* at 4, 7), but then proceeded largely to ignore the 100-year-old line of cases that bars the use of regulatory fees imposed through the police power for general revenue purposes. In addition, like the trial court, the Court of Appeals refused to consider the **source** of HBC fees, opting instead to distinguish *Armstrong* and *Haydon Bridge* only on the obvious and

⁴ CR 59.05 Order at 2.

immaterial fact that HBC accounts are not commingled with private and public funds. (*Id.* at 18)

By Order entered on October 17, 2012, this Court granted discretionary review.

II. FACTUAL BACKGROUND

HBC was established by Executive Order of Governor Julian Carroll⁵ after the tragic Beverly Hills fire in 1977 “to create a standard uniform building code and protecting the consumer in health and safety matters.”⁶ Ratifying legislation was enacted by the 1978 General Assembly.⁷ HBC monitors all construction to ensure building code compliance, conducts safety inspections during construction, and continues inspections after a project has been completed, according to the testimony of Commissioner Richard Moloney.⁸ The agency issues over 40,000 permits per year and conducts over 120,000 inspections per year. HBC issued 88,442 licenses and permits during 2008.⁹ HBC is organized in four divisions: Building Code Enforcement, HVAC, Plumbing, and Minimum Safety Standards (also called Office of State Fire Marshall).¹⁰

⁵ TR at 22-26.

⁶ Hank Hancock depo. at 7. There are five depositions in the record, but they are not paginated as part of the trial record.

⁷ 1978 Ky. c. 117, c. 155 ¶¶ 124-126.

⁸ Moloney depo. at 8-9.

⁹ TR 134-135.

¹⁰ Moloney depo. at 13.

The HBC statutory scheme includes structural and mechanical standards.¹¹ These standards are adopted by the HBC Board in the Uniform State Building Code. (KRS 198B.050) The HBC Board's twenty members include (one each) a home builder, architect, structural engineer, mechanical engineer, electrical engineer, general contractor, plumbing or HVAC contractor, mechanical contractor, electrical contractor, and labor/building trade member. Commissioners of HBC, Public Health and Ky. Housing Corp., Attorney General or designee and a local fire chief also serve. (KRS 198B.020)

Appellants are four licensed contractors located in Bellevue, Louisville, Richmond, and Springfield. (Complaint ¶¶ 2-5 and TR 133) Thomas C. Rehtin has served on both the HBC Board and the HVAC Board. (Rehtin depo. at 4, 29) Ervin Klein, a member of the Kentucky Association of Plumbing, Heating and Cooling Contractors, has endorsed fee increases to "hire the inspectors that are needed" at HBC. (Klein depo. at 5, 22) Appellees are Finance Secretary Jonathan Miller, Budget Director Mary E. Lassiter, and HBC Commissioner Richard Moloney (now Ambrose Wilson IV).

Appropriations in the 2008-2010 biennial budget for HBC operations were:

	<u>2008-09</u>	<u>2009-10</u>
General Fund	\$ 2,321,000.00	\$ 2,432,000.00
Restricted Fund	\$15,826,400.00	\$17,292,500.00
TOTAL	\$18,147,400.00	\$19,613,500.00

¹¹ These standards are designed to prevent industrial boiler explosions (KRS 236.010 and 236.080), electrical fires and shock (KRS 227.487), passenger elevator collapse (KRS 198B.480, and plumbing failure (KRS 318.010-990). HBC laws also cover fire protection sprinklers (KRS 198B.712), HVAC contractors (KRS 198B.65B), and mobile home and recreational vehicles (KRS 198B.090).

(2008 Ky. Acts c. 127, p. 372)

General Funds are appropriated only to the Office of State Fire Marshall. All other HBC activities are paid from restricted funds collected by five different statutory boards and the HBC Commissioner.¹² The Commissioner alone sets the rate for nearly \$2 million of fees collected annually. Moloney testified that “we tried to be as close as possible” in setting the fees “to make sure that we will be able to pay this office and not go over the amount” needed for revenue neutral balances.¹³ Current types, authority and range of fees are:

TYPE	AUTHORITY FOR SETTING FEES	RANGE OF FEES
Boiler and Pressure Vessels	Commissioner, KRS 236.130	\$175-\$250 licenses \$15-\$1200 inspections
Electrical Inspectors	Commissioner, KRS 227.487	\$100
Master Electrician,	KRS 227A.060, maximum \$100	\$100
Journeyman Electrician	KRS 227A.060, maximum \$50	\$50
Electrical Contractor	KRS 227A.060, maximum \$200	\$200
Elevators	Commissioner, KRS 198B.490	\$75-\$130 +
Fire Protection Sprinkler Contractors	Commissioner, KRS 198B.555	\$50-\$250
Building Inspectors	HBC Board, KRS 198B.090	\$100
Home Inspectors	Kentucky Board of Home Inspectors, KRS 198B.706	\$250
HVAC	Board of Heating, Ventilation & Air Conditioning, KRS 198B.622	\$10-\$250
Manufactured Housing And RV's	Manufactured Home Certification & Licensure Board, KRS 227.620	\$25-\$500
Plumbing	HBC Board, KRS 318.050 and 318.134	\$50-\$250 licenses \$5-\$35 permits

¹² Moloney depo. at 10-13.

¹³ Moloney depo. at 16-20.

Increases and decreases in fees have occurred over the years. Some fees were increased in 1993 and some were decreased in 1995. Extensive across-the-board fee increases were enacted by HBC committees in 2001. Citizen members of the plumbing and HVAC Boards approved increases of 150% to 500%, depending on the license type. Significant increases were also made in boilers, elevator inspections, elevators, hazardous materials, and sprinkler programs.¹⁴

Then-commissioner Dennis Langford orchestrated the 2001 increases by scheduling an HBC Board meeting at Lake Cumberland State Park. Documents presented by the department showed that expenses in 2001 exceeded revenue by \$2.4 million. HBC staff presented a package showing proposed income and expenses for the current year. Staff expressed the view that if the members of the construction industry want to continue the license and permit programs at the same quality as in the past, "they need to increase those fees."¹⁵ The meeting at Lake Cumberland was described as "quite a show" to convince contractors to support the fee increases. All expenses were paid by the State for the 50-75 people who attended. Langford "brought in all the right people. He was very convincing."¹⁶

Year-end surpluses began to build up after the 2001 fee increases. Instead of spending the increased fees on Building Code enforcement, \$4,936,800 was taken from HBC "to help balance the state budget" in 2004. (Hancock depo. at

¹⁴ Hancock depo. at 11-16 and Exhibits 1 and 2.

¹⁵ Hancock depo. at 13 and Exhibit 1.

¹⁶ Rehtin depo. at 14, 15, 32.

23 and Hancock Exhibit 2) At the end of fiscal year 2007, HBC fee accounts totaled nearly \$10 million. (Answer to Interrogatory 6)¹⁷ Due to the large year-end surpluses, discussions were initiated in early 2004 by the Plumbing Code Committee asking that Van Cook, then Executive Director of HBC, reduce permit and license fees. Cook responded by letter dated June 7, 2004, asking that the Committee “not consider reducing permit and license fees” because “such action is not feasible at this time.”¹⁸ Klein testified that promises made by HBC staff to get the 2001 fee increases had not been kept. Commissioner Langford and others induced contractors’ support by promising to hire more inspectors and provide technical equipment. Klein said “we were sold a bill of goods.” He continued:

So, in 2004, we asked that the fees be reduced to the 2001 level because – what’s going to happen with all this money that’s being built up? We knew what was going to happen, because we had already been told. It’s going to be moved over to the General Funds.¹⁹

Appellant David Miles agreed, testifying that “the money is not being used as we intended.” (Miles depo. at 12) Appellant Eddie Noel testified about delays in getting electrical and plumbing inspections due to a shortage of inspectors. (Noel depo. at 8-10)²⁰ Private contractors support thorough inspections to protect the health and welfare of the public. (Klein depo. at 22)

To the extent that HBC exercises control over its fees and funds, it is police power authority statutorily delegated by the General Assembly. The budget,

¹⁷TR 136.

¹⁸ Hancock depo. at 17 and Exhibit 3.

¹⁹ Klein depo. at 45, 46.

²⁰ TR 141

“which provides the revenue for the Commonwealth and which determines how that revenue shall be spent, is fundamentally a legislative matter.”²¹ The legislature’s power over the Commonwealth’s purse strings is plenary. Police power authority is limited. The Kentucky Constitution empowers the General Assembly to make appropriations (Section 230), to contract debts (Sections 49-50), to provide for annual taxes (Section 171), and to provide for payment of license fees and excise taxes (Section 181). The legislature determines, by statute, which funds are restricted and which funds lapse to the General Fund to the extent that they are in excess of appropriations or expenditures.

III. KEY ISSUES TO BE ADDRESSED²²

Appellants contend that the right of a regulatory agency to assess fees in exercise of police power is limited to “amounts sufficient only to meet the expense of issuing the license and supervising any necessary regulatory measures.”²³ “Anything in addition to this amounts to a tax for revenue, and cannot be upheld as a valid exercise of the police power.”²⁴ These longstanding principles governing police power fees are incorporated into the statutory structure requiring that HBC fees be fixed only in amounts needed to operate its

²¹ *Legislative Research Commission v. Brown*, 664 S.W.2d 907,925 (Ky. 1984).

²² These issues were properly preserved for review in Appellants/Plaintiffs’ Memorandum in Support of Motion for Declaration of Rights and Injunctive Relief (TR 131-153); Reply Memorandum (TR 169-174); Response to Defendants’ Memorandum in Support of Cross-Motion for Summary Judgment (TR 226-250); CR 59.05 Motion and Memorandum (TR 281-287); and Reply in Support of CR 59.05 Motion (TR 300-306).

²³ *Roe v. Commonwealth* 405 S.W.2d 25, 28 (Ky. 1966), citing *City of Henderson v. Lockett*, 163 S.W. 199 (Ky. 1914).

²⁴ *Reeves v. Adam Hat Stores*, 198 S.W.2d 789, 791 (Ky. 1946).

program.²⁵ Appellees candidly agree that HBC operates on a revenue neutral basis in setting license and inspection fees.²⁶ Commissioner Moloney's undisputed testimony is that the fees are set "to make sure we will be able to pay this office and not go over the amount" needed annually for HBC programs.²⁷ The Court of Appeals' Opinion Affirming overturns these long-established judicial precedents limiting use of police power fees and assessments to particular purposes and obliterates the constitutional distinction between police power fees and taxes assessed as license fees under Constitution Section 181.

In addition, none of the fees paid by contractors for building code enforcement are fixed by the General Assembly. All HBC license, permit and inspection fees are set by regulatory boards²⁸ or the Commissioner.²⁹ A few fees are subject to statutory maximums.³⁰ The *source* of the fees are private contractors who pay them for the privilege of being regulated and, hence, of

²⁵ KRS 198B.090(10); KRS 198B.490; KRS 198B.615; KRS 198B.676(1); KRS 198B.710(1) and (2); KRS 227.620(5); KRS 227A.050(1); KRS 236.130(1) and (2); KRS 227.487(2); KRS 318.136.

²⁶ Moloney depo. at 19-20.

²⁷ Moloney depo. at 17-19.

²⁸ Building Inspectors KRS 198B.090; HVAC KRS 198B.622; Home Inspectors KRS 198B.706(6); Mfg. Housing KRS 227.620; Plumbing KRS 318.050 and 318.134.

²⁹ Boiler and Pressure Vessels KRS 236.130; Elevators KRS 198B.490; Fire Protection Sprinkler Contractors KRS 198B.555, Electrical Inspectors KRS 227.487.

³⁰ Electrical Contractor fee not to exceed \$200; master electrician fee not to exceed \$100, KRS 227A.060; Home Inspectors fees not to exceed \$250, KRS 198B.706(6); Mobile Home Manufacturer \$500 maximum and Retailer \$250 minimum per KRS 227.620(4).

doing business.³¹ Consequently, HBC fees are “private funds” under the teaching of *Thompson v. KRA* and *Haydon Bridge*. They may not be transferred to the General Fund.

Next, the trial court relied on a hybrid formulation of finance accounts called “excess funds” as the basis for ruling that the transfers were valid.³² The Court of Appeals similarly found that “year-end balances” in HBC accounts can be transferred to the General Fund.³³ These constructs, however, provide no authority to transfer the fees at issue.

Finally, the transfers at issue violate several constitutional provisions. The budget bill at issue improperly amends KRS Chapter 198B in violation of Sections 15 and 51. Next, assuming the legislature has indeed converted HBC fees to taxes, it has improperly changed the purpose for which the fees were levied in violation of Section 180. The transfers also constitute an improper taking of private property in violation of Sections 2 and 242. And, the General Assembly’s actions violate Section 2 and the equal protection clause, as various classes of contractors were treated arbitrarily based on “cash flows.”

ARGUMENT

I. HBC FUNDS ARE NOT AVAILABLE FOR TRANSFER TO THE GENERAL FUND TO OPERATE STATE GOVERNMENT.

Two foundational precepts require reversal of the Opinion Affirming. First, the General Assembly may not utilize regulatory fees imposed pursuant to

³¹ As noted, the State Fire Marshall receives funding from the General Fund.

³² Summary Judgment Order at 2; CR 59.05 Order at 4.

³³ Opinion Affirming at 18.

the police power to fund the general operations of state government. Second, HBC fees are “private funds” not subject to expropriation by the General Assembly. These precepts operate independently, and they are circumscribed by two distinct lines of authorities set down by this Court.

A. HBC fees are levied pursuant to police power and may not be used to fund the operations of state government.

“Business taxes may be imposed under the police power for purposes of regulation or under the taxing power for purposes of revenue.”³⁴ HBC is a “governmental unit whose principle duties require exercise of a broad police power in order to safeguard the public health . . . It is an administrative agency created to perform one specific function. The scope of its authority is necessarily limited.”³⁵ The trial court correctly characterized this case as involving fees enacted pursuant to the police power:

HBC fees are collected pursuant to the Commonwealth’s police power for the purpose of regulating housing, buildings, and construction, in order to protect public health, welfare, and safety.

* * *

The nature of the HBC funds is regulatory - the fees are enacted pursuant to the state’s police power.³⁶

As regulatory fees, however, HBC fees may only be levied subject to an important constitutional constraint -- a constraint that bars the transfers at issue.

³⁴ *Renfro Valley Folks, Inc. v. City of Mt. Vernon*, 872 S.W.2d 472, 474 (Ky. App. 1993).

³⁵ *Henry v. Parrish*, 211 S.W.2d 418, 422 (Ky. 1948).

³⁶ CR 59.05 Order at 4.

Since its decision in *Henderson v. Lockett* in 1914, this Court has invoked a bright line rule that regulatory fees cannot be used to supplement the tax needs of general government:

Where a license fee is exacted as a revenue measure, under statutory authority based upon section 181 of the Constitution, the courts will not interfere with the exercise of that power unless the action is arbitrary and oppressive. But, where a license fee is imposed under the police power, the fee exacted must not be so large as to charge the ordinance with the imputation of a revenue-producing purpose. The fee that may be imposed under the police power is one that is sufficient only to compensate the municipality for issuing the license and for exercising a supervision regulation over the subjects thereof. ***Anything in addition to this amounts to a tax for revenue, and cannot be upheld as a valid exercise of the police power.***³⁷

This rock solid rule of law has been invoked consistently and repeatedly by this Court.³⁸

In *Reeves v. Adam Hat Stores*, 198 S.W.2d 789 (Ky. 1947), the Court considered the nature of a law that imposed a license fee on retail merchants graduated according to the number of stores operated in Kentucky. The Court found the law to be “a revenue measure rather than a police measure because the revenue it raises is so greatly in excess of the cost to the State of issuing the license and of enforcing the statute.” (*Id.* at 791.) The Court referred to the then-developing line of authorities as follows:

³⁷ *City of Henderson v. Lockett*, 163 S.W. 199, 201 (Ky. 1914) (emphasis added).

³⁸ See, e.g., *The City of Mayfield v. Carter Hardware*, 230 S.W. 298, 300 (Ky. 1921); *Daily v. Owensboro*, 77 S.W.2d 939, 941 (Ky. 1934); *Martin v. City of Greenville*, 227 S.W.2d 435, 437 (Ky. 1950); *Reeves v. Adam Hat Stores*, 198 S.W.2d 789 (Ky. 1947); *Roe v. Comm. Of Ky.*, 405 S.W.2d 25, 28 (Ky. 1966).

The *Lockett* case has been followed in an unbroken line of decisions down to *Daily v. City of Owensboro*, 257 Ky. 281, 77 S.W.2d 939. It must not be forgotten that in a police act the amount of license fees charged should in some measure correspond to the cost of issuing the license and of enforcing the supervisions or regulations provided in the act.

(*Id.* at 791-92)³⁹

The trial court completely ignored this line of authorities -- in both its Summary Judgment and its CR 59.05 Order. The Court of Appeals at least acknowledged one of the cases -- *Adam Hat Stores* -- by quoting from that case and stating that "one might be persuaded" by the clear import of *Adam Hat Stores*.⁴⁰ Yet, the Court of Appeals utterly ignored the holding in *Adam Hat Stores* -- with no explanation as to why it was **not** persuaded!

Instead of conforming to the well established rule limiting the use of police power fees, the Court of Appeals stated that "we find *Commonwealth v. Louisville Atlantis Community/Adapt, Inc.*, 971 S.W.2d 810, 815 (Ky. App. 1997), to be dispositive."⁴¹ But, *Louisville Atlantis* dealt with whether the fee imposed on charitable gaming violated Section 170's exemption of charities from taxation. The Court distinguished the fee as a constitutional regulatory fee and not a tax, citing *Gray v. Methodist Episcopal Church*, 114 S.W.2d 1141 (Ky. 1938). The *Gray* Court held that while charities are exempt from taxation, they are not exempt from regulatory fees. The Court of Appeals in this case merely stated the

³⁹ Most recently, license fees for raising revenue were distinguished from regulatory fees in *Renfro Valley Folks v. Mt. Vernon*, 872 S.W.2d 472, 474 (Ky. 1994), also citing *Lockett*.

⁴⁰ Opinion Affirming at 17.

⁴¹ Opinion Affirming at 17.

general rule that the auto registration fee in *Gray* is not a tax and therefore must be paid by a charitable organization, “even if it produces revenue for the public.” (*Id.* at 1144)

That stray comment, of course, is mere dicta. And, the *Gray* Court explained that, while the amount of a registration fee⁴² may be more than necessary for strictly “police” purposes, using the fee “to repair damage to the highways, occasioned by the use of this new vehicle, constituted a valid exercise of the police power.” (*Id.*) That is because the “primary purpose” of the law “was to regulate and supervise the privilege of using a vehicle on the highway.” (*Id.*) There is an obvious connection between the auto registration fee and road repair that is completely missing in this case.⁴³ There is no connection between HBC regulatory fees and General Fund taxes. *Gray* is completely inapposite.

At any rate, *Gray* cannot be construed as condoning, or even remotely dealing with, taking police power fees from a regulatory agency and using them as General Fund taxes. And *Gray* most certainly does not conflict with or overrule the *Lockett-Adam Hat Stores* line of authority.⁴⁴

⁴² An annual auto registration of \$11.50 is paid to the county clerk. (KRS 186.020 and 186.050(1))

⁴³ Indeed, registration fee balances are dedicated to the state road fund. KRS 186.240(4).

⁴⁴ The ruling in this case turns the *Gray* decision on its head and exposes charitable gaming fees, in addition to HBC fees, to General Fund transfers. In fact, a parallel case pending in this Court challenges the transfer of \$700,000.00 in charitable gaming fees to the General Fund in the same 2008–2010 biennial budget where the funds at issue were transferred. The circuit court ruling in that case declared the transfers invalid, but the Court of Appeals reversed the trial court. *Beshear v. Louisville Soccer Alliance, Inc.* (Supreme Court Case No. 2012-SC-197).

Finally, the trial court's Summary Judgment declared "there are no implicit restrictions that would prevent the General Assembly from suspending the statutory restrictions on HBC funds" under *Armstrong*.⁴⁵ Even if it were true that *Armstrong* contains "no implicit restrictions," the ruling in *Lockett* and its progeny of nearly 100 years ***explicitly forbids*** police power fees being extracted from licensees and diverted to "a tax for revenue." Under the ruling of the trial court, the "implicit restrictions" lacking in *Armstrong* would overrule the ***explicit prohibitions*** in *Lockett* and its progeny.⁴⁶

B. HBC fees are "private funds" that may not be expropriated by the General Assembly.

The Court of Appeals upheld the trial court's ruling that *Armstrong v. Collins*, 709 S.W.2d 437 (Ky. 1986), provides authority for the legislature "to lift statutory restrictions on HBC funds by temporarily suspending the relevant statute [sic] in the budget bill."⁴⁷ As just demonstrated, applying *Armstrong* to the facts of this case creates a direct conflict with a long line of Kentucky cases holding that the right to assess fees in exercise of police power prohibits any of the fee money from being used as a tax for general government purposes. In addition, the Court of Appeals failed to consider that *Armstrong* declared that neither Section 51 nor KRS 48.315 may be invoked as authority to transfer private funds to the General Fund. (*Id.* at 446) This doctrine was reinforced by *Haydon*

⁴⁵ Summary Judgment at 6.

⁴⁶ Long established constitutional limits on the use of police power fees were not modified, or even addressed, in *Armstrong*.

⁴⁷ Opinion Affirming at 6.

Bridge's holding that “[t]here is simply no authority to transfer private agency funds.” (304 S.W.3d at 705)

In *Haydon Bridge*, this Court held that workers’ compensation assessments paid to the Benefit Reserve Fund are “private funds” that may not be transferred into the General Fund by the legislature in a budget bill. (*Id.* at 704-05) The Court defined “assessments” as charges “which are specially beneficial to particular individuals or property . . . imposed in proportion to the particular benefits.” (*Id.* at 698) “Taxes” on the other hand are “public burdens imposed generally upon the inhabitants of the whole state . . . for governmental purposes, without reference to peculiar benefits to particular individuals or property.” (*Id.* at 697-98)

Applying these foundational definitions to this case, HBC fees equate with assessments. The definition of “fees” mirrors the *Haydon Bridge* definition of “assessments.” A fee is:

A charge for a particular service . . . for the purpose of fulfilling the statutory mandates (that) cannot be equated with taxes The validity of special assessments and user fees depends on an analysis of the charge and the benefit . . .⁴⁸

Assessments and fees are interchangeable terms. The trial court breezed by these facts to find that fees are not analogous to assessments and that “HBC Fees Generate Public Revenue.” (CR 59.05 Order at 2) The trial court concluded that fees paid under the police power generate revenue “in the public interest” and, therefore, “the legislature may lawfully transfer excess HBC funds to the General

⁴⁸ *Ky. River Authority v. City of Danville*, 932 S.W.2d 374, 376-377 (Ky. App. 1996), *cert. denied*, 520 U.S. 1186, 137 LEd 682 (1997).

Fund.” (*Id.* at 4) “Public interest,” however, is simply not part of the *Haydon Bridge* formulation. Both HBC fees and workers’ compensation assessments are specially beneficial to particular individuals and property.

Moreover, HBC fees are “imposed in proportion to the particular benefits.” Appellees freely admit that the goal is revenue neutrality, “to make sure we will be able to pay this office and not go over the amount” of money needed to fund HBC. (Moloney depo. at 19-20) Similarly, employer assessments amortize workers’ compensation liabilities actuarially in amounts needed. (*Haydon Bridge* at 687).

Finally, HBC fees are not “imposed generally upon the inhabitants of the whole state, for governmental purposes” Although all parties agree HBC fees are not taxes, the trial court went further: “[T]he fact that HBC fees are not taxes does not automatically make them assessments.” (CR 59.05 Order at 4) Even if it does not follow automatically, it is indisputable that *Haydon Bridge* did not recognize a hybrid category of non-assessment, non-tax revenue measures.⁴⁹ The trial court failed to address the line of cases that -- consistent with *Haydon Bridge* -- effectively and expressly equates “fees” with “assessments.” *Ky. River Authority* at 376, uses “fees” and “assessments” interchangeably:

Assessments and fees charged without a relationship to a benefit received by the payor are arbitrary and capricious

⁴⁹ The Court stated that “both taxes and assessments are appropriately referred to as revenue measures,” but further noted that “there is a difference between taxes and assessments.” *Haydon Bridge* at 697, 698. There is no third category.

Similarly, the Court of Appeals has distinguished fees from taxes just as the *Haydon Bridge* court distinguished assessments from taxes:

A tax is universally defined as an enforced contribution to provide for the support of government, whereas a fee is a charge for a particular service.⁵⁰

Appellants repeatedly cited these authorities, but the lower courts' rulings do not seriously contend with them.

The trial court also made much of the fact that “[i]n contrast to *Haydon Bridge*, the HBC accounts at issue in the instant case do not involve commingled funds -- the funds come solely from regulatory fees imposed by the HBC.” (CR 59.05 Order at 3) This distinction glosses over the **source** of HBC funds. In *Thompson v. Ky. Reinsurance Assoc.*, 710 S.W.2d 854 (Ky. 1986), this Court held that the General Assembly may not transfer assessments collected by the Kentucky Reinsurance Association (“KRA”), stating that “to arrive at this conclusion it is only necessary to identify the nature and purpose of the KRA and to identify its **sole** source of funding.” (*Id.* at 857) (emphasis in original). Of course, HBC fees come **solely** from licenses and permits paid for by private contractors.⁵¹ Under *Thompson*, HBC fees are private funds.

The trial court dodged the ruling in *Haydon Bridge* and *Thompson* by declaring that police power fees collected to protect public health, welfare, and

⁵⁰ *Longrun Baptist Assoc., Inc. v. Louisville and Jefferson Co. Metropolitan Sewer Dist.*, 775 S.W.2d 520, 522 (Ky. App. 1989)

⁵¹ Like the KRA, HBC was “created for one purpose and its funding is achieved without tax dollars, without public money.” *Haydon Bridge* at 698, citing *Thompson*.

safety are public funds, like taxes, because “HBC fees are public in nature.”⁵² That plays far too loose with the word “public.” HBC is “self-sufficient based upon the fees that are paid and permits that are taken.”⁵³ Private contributions discussed in *Armstrong* are used for public purposes too, *viz.*, retirement systems and workers compensation programs. The private contributions in *Armstrong*, just like HBC fees paid to monitor the private activities of building contractors, are dedicated exclusively to public purposes. That fact alone does not convert the funds to public funds.

II. KRS 48.315 PROVIDES NO BASIS FOR TRANSFERRING HBC FUNDS.

The trial court declared that the General Assembly has authority to transfer in a budget bill “all or part of the agency funds, special funds, or other funds” established under the provisions of certain statutes enumerated in KRS 48.315(1).⁵⁴ That enumeration is as follows:

The General Assembly may provide in a budget bill for the transfer to the General Fund for the purpose of the General Fund all or part of the agency funds, special funds, or other funds established under the provisions of KRS 15.430; 21.347; 21.540; 21.560; 42.500; 47.010; **48.010(13)(g)**; 56.100; 61.470; 64.345; 64.350; 64.355; 95A.220; 136.392; 138.510; 161.420; 161.430; 164A.020; 164A.110; 164A.800; 164A.810; 216A.110; 230.218; 230.400; 230.770; 248.540; 248.550; 278.130; 278.150; 286.1-485; 304.35-030; 311.450; 311.610; 312.019; 313.350; 314.161; 315.195; 316.210; 317.530; 317A.080; 319.131; 320.360; 321.320; 322.290; 322.330; 322.420; 323.080; 323.190; 323.210; 323A.060; 323A.190; 323A.210;

⁵² CR 59.05 Order at 4.

⁵³ Klein depo. at 70, 71.

⁵⁴ Summary Judgment at 4.

324.286; 324.410; 325.250; 326.120; 327.080;
330.050; 334.160; 334A.120; 335.140; 342.122;
342.480, etc.

(Emphasis added) For its part, the Court of Appeals declared that the use of “etc.” at the end of KRS 48.315(1) constitutes “relevant language which is unambiguous in nature.”⁵⁵ To the contrary, the essence of the phrase “et cetera” is loaded with ambiguity. The historic weight of authority built on the *Lockett* doctrine simply cannot be toppled by the flimsy thread found in the term “etc.” Nor can *Haydon Bridge’s* clear cut proscription against transferring private funds to the General Fund be undone by a vague Latin phrase.

Consider first that the list does not include **any** of the HBC statutes. The *Haydon Bridge* Court distinguished the general language of KRS 48.310(2) and 48.316 from “the [noted] provisions” of KRS 48.315.⁵⁶ The lower courts’ interpretation makes “the [noted] provisions” of KRS 48.315 an endless list, rendering superfluous the enumeration that precedes “etc.”

Second, while KRS 48.315 pointedly allows budget transfers relating to the road fund (KRS 48.010(13)(g)), it excludes transfers of restricted funds (KRS 48.010(13)(f)). The legislature is thus deemed to have **intended** to exclude restricted funds not listed.⁵⁷ This general rule is applied when the relevant

⁵⁵ Opinion Affirming at 16.

⁵⁶ “KRS 48.315 appears to have been set out separately from KRS 48.316 in recognition that the funds affected were ‘agency funds, special funds, or other funds established under the [noted] provisions.’” *Haydon Bridge* at 703.

⁵⁷ *Smith v. Wedding*, 303 S.W.2d 322, 323 (Ky. 1957) (“it is a primary rule of statutory construction that the enumeration of particular things excludes the idea of something else not mentioned.”) *Louisville Water Co. v. Wells*, 614 S.W.2d 525, 527 (Ky. App. 1984).

language is ambiguous and as an aid in arriving at legislative intent.⁵⁸ Since HBC statutes are *not* listed, there is no unambiguous authority for transferring HBC funds.

Third, every amendment of KRS 48.315 has included “etc.” since its enactment in 1984.⁵⁹ Over time, the legislature subtracted from, but never added to the list. These subtractions would be futile if “etc.” were construed to include “all others not listed.” The legislature must therefore have intended to exclude unlisted statutes. (*Smith v. Wedding, supra*) The lower courts’ reliance on “etc.” leads to an absurd result. Why enumerate any statutes? If a limitless list were intended, the General Assembly would have simply said so.

Fourth, “etc.” is preceded by a comma not a semicolon. All the listed statutes are separated by a semicolon. Arguably, the legislature must have intended “etc.” to relate only to the last statute in the series, *viz.*, KRS 342.480. To say the least, use of the term “etc.” at the end of the list is confusing and uncertain. Had it intended to relate to unenumerated statutes, the list would have ended “KRS 342.480; etc.”⁶⁰

⁵⁸ *Public Service Commission v. Com.*, 324 S.W.3d 373 (Ky. 2010).

⁵⁹ Acts 1984, ch. 410, § 6; Acts 1992, ch. 109, § 39; Acts 2003, ch. 169, § 4; Acts 2006, ch. 207, § 1; Acts 2009, ch. 78, § 4, and Acts 2010, ch. 85, § 18.

⁶⁰ “Semicolon’ is defined as ‘the punctuation mark (;) used to indicate a major division in a sentence where a more distinct separation is felt between clauses or items on a list than is indicated by a comma, as between the two clauses of a compound sentence.’ *People v. Beardsley*, 688 N.W.2d 304, 306 (Mich. Ct. App. 2004).

Fifth, portions of the KRS 48.315 list are unconstitutional under *Armstrong*⁶¹ and it includes statutes that have been repealed (e.g., KRS 342.480). The statute is so tangled as to be void for vagueness. (See *Board of Trustees of the Judicial Form Retirement System v. Attorney General of the Commonwealth of Kentucky*, 132 S.W.3d 770 (Ky. 2003)). In finding an amendment to the Judicial Retirement Act void for vagueness, the Court held that “while statutes affecting (the First Amendment, criminal law and civil penalties) should receive the most **rigorous** review and are most **commonly** held void for vagueness, non-punitive civil, regulatory, or spending statutes are also invalid if they are so unintelligible as to be incapable of judicial interpretation. In that circumstance, the statute often is declared void for ‘unintelligibility’ or ‘uncertainty’ as opposed to ‘vagueness.’” (*Id.* at 778) (emphasis in original). To be sure, KRS 48.315 is “uncertain” as to its reach either to restricted funds generally or to the unlisted HBC statutes specifically. It is void for vagueness.

Sixth, the transfer of certain trust and agency funds authorized by KRS 48.315 was approved in *Armstrong*. As noted, budget transfers of HBC fees are not authorized by KRS 48.315. Furthermore, budget transfers of private funds are not allowed under *Armstrong*. HBC was created and operates to prevent public disasters by monitoring the private activities of building contractors who pay for their own policing exclusively out of their private funds. Taxpayers are

⁶¹ Transfers from State Police Retirement (KRS 16.565); KERS (KRS 61.580); CERS (KRS 78.650)13; Teachers Retirement (KRS 161.420); and Workers’ Compensation (KRS 342.122 and KRS 342.480), 709 S.W.2d at 446, 447.

not charged for these services.⁶² HBC fees are no different than the private funds described in *Armstrong*, such as assessments paid by insurance companies for the financing of workers compensation programs.⁶³ Nor are they any different than the assessments at issue in *Thompson v. KRA*.

Finally, KRS 48.315 was originally enacted in 1984 and was amended in 1992, 2003, 2006, 2009 and 2010. The building code was first enacted in 1978. The portion of the building code relating to HVAC was enacted in 1994.⁶⁴ At any time when it amended KRS 48.315, the legislature could have added HBC statues to the list. As previously noted, however, the legislature subtracted from but never added to the list of statutes covered by KRS 48.315. The rulings of the trial court and the Court of Appeals attribute a legislative intent that conflicts with what the General Assembly actually did.

All of these arguments were made below. The trial court dismissed them all with one declarative sentence: "As an indication that the list of statutes is not exclusive, the statute ends the list with 'etc.'"⁶⁵ That's it. No more. The Court of Appeals made short shrift of these arguments, as well, resorting to Black's Law Dictionary's definition of "etc." and flawed logic.⁶⁶ Consider this untenable proposition:

⁶² Hancock depo. at 7-10.

⁶³ *Armstrong v. Collins* at 446-447.

⁶⁴ Ky. Acts 1994, ch. 59

⁶⁵ Summary Judgment at 4.

⁶⁶ Opinion Affirming at 16.

The use of “etc.” by the legislature expresses an obvious intent to include other additional unspecified statutes. Thus the HBC account funds are properly included.⁶⁷

It’s magic. Something that is unspecified somehow gets properly “included”?

The Court of Appeals also failed to explain how the list is illustrative:

Thus, the inclusion of “etc.” makes the enumerated list of statutes in KRS 48.315(1) illustrative rather than exhaustive. *See Fox v. Grayson*, 317 S.W.3d 1, 10 (Ky. 2010). Therefore, we disagree with Appellants’ argument that KRS 48.315 does not provide a basis for the transfer of the HBC account funds. . . .⁶⁸

The list is “illustrative” of what? The Court of Appeals never says; it just “disagrees” with Appellants’ analysis. No explication. “Illustrative” apparently means just what the Court of Appeals says it means.⁶⁹

Finally, the Court of Appeals posits that if it were to apply the maxim *expressio unius est exclusio alterius*, it would nonetheless not apply:

However, even if we were to apply the canon as argued by the Appellants, we believe “etc.” to be relevant language which is unambiguous in nature which, in and of itself, defeats the application of the maxim.⁷⁰

This is quite circular and really suspect. How can the legislature’s use of “etc.” after a listing of 63 specific statutes possibly be deemed to be “unambiguous in nature”? The Court of Appeals gives no good reason why the maxim should not

⁶⁷ Opinion Affirming at 16.

⁶⁸ Opinion Affirming at 16.

⁶⁹ “When I use a word,” Humpty Dumpty said, in a rather scornful tone, “it means just what I choose it to mean, neither more nor less.” (Through the Looking Glass, Ch.6)

⁷⁰ Opinion Affirming at 16.

apply here. In sum, KRS 48.315 provides no basis for transferring HBC fees to the General Fund.

III. SO-CALLED "EXCESS FUNDS" OR "YEAR-END BALANCES" ARE PROHIBITED FROM TRANSFER TO THE GENERAL FUND.

Appellees urged the trial court to endorse a hybrid form of finance accounts called "excess funds" which are subject to transfer to the General Fund. While bluntly acknowledging that a valid definition was at issue, the trial court declared that, since only "excess funds" were taken, the transfers were valid. (Summary Judgment at 11-12). The trial court freely admitted that the term "excess funds" was manufactured:

While the parties contest the validity of the term "excess funds," the Court finds that, to the extent that there are monetary resources in a fund above the spending appropriated by the General Assembly, it is reasonable to refer to such resources as "excess" or "surplus."

(Summary Judgment at 2, f.3) There is, of course, no statutory definition of "excess funds." It is a term of convenience contrived solely to fit this case.

Appellees also offered a second definition of "excess funds" as:

Monetary resources in excess of the spending appropriated by the General Assembly. They consist of any unexpended cash balance from the prior year's appropriation plus expected annual revenues and represent the amount of monetary resources greater than appropriated spending represent excess funds. In other words, fees in excess of those needed to satisfy the amount appropriated for a given year are excess. They may also include left-over funds from the prior fiscal year or years.

(John Hicks Affidavit, TR 202) Both definitions were made up by the budget office ***after this litigation was filed*** to fill the gap of authority where none exists.

The Court of Appeals focused on “year-end balances”:

While true that [*Haydon Bridge*] said *Armstrong* prohibited the transfer of year-end balances containing commingled funds, we do not believe that the Court intended to prevent the transfer of year-end balances that contained public funds that were not commingled with private funds.⁷¹

Governor Beshear’s Budget Reduction Order No. 08-01 issued on January 4, 2008, transferred \$6,495,200 from ten (10) HBC fee accounts. (TR 45) ***The Governor’s Order, in the middle of the fiscal year, makes no mention of “excess funds” nor does it explain how “year-end balances” can occur in January.*** The budget bill ordered \$3.7 million to be taken out of HBC fees collected ***in the future*** during the 2008-10 budget cycle due to “the financial condition of the state.” The budget bill itself undermines the budget office notion that these transfers are “excess funds” or “year-end balances.” Most of the transfers we made in mid-year, the rest from future collections. Yet, both the trial court and the Court of Appeals rotely assented to the budget office’s manufactured definitions.

Year-end balances “cannot be separated into categories called ‘public money’ and ‘private agency funds.’” *Haydon Bridge* at 705. The character of each fund on the last day of the year is the same as on the first day. Having a “year-end balance” does not magically transform an HBC account into a “public

⁷¹ Opinion Affirming at 18.

fund.” Hybrid accounts called “excess funds” cannot exist under the reasoning in *Haydon Bridge*. Fees are either fish or fowl. Fees collected under Ky. Const. Sec. 181 are taxes. Fees like HBC licenses and permits collected under the police powers are “private agency funds.” There is no third category. The Court of Appeals disagreed, declaring that year-end balances (and indeed all HBC funds) are public funds.⁷² ***Under the reasoning of the Court of Appeals, all license and permit fees collected by HBC are public funds that may be taken for general government operations -- not just year-end balances!***

The trial court cited *Ky. River Authority, supra*, to support the conclusion that protecting public safety is “in the public interest” and therefore HBC fees are public funds.⁷³ That ruling in no way characterized water user fees as public funds that are subject to transfer to the General Fund. In fact, the trial court’s ruling is inconsistent with *Ky. River Authority*. The *Ky. River Authority* court noted that the fees “are not used for the General Fund, but only for Kentucky River basin management.” (932 S.W.2d at 376) Nonetheless, water user fees will in the future be available to use as taxes in a budget bill if the lower courts’ rulings stand.⁷⁴

⁷² Court of Appeals’ Opinion Affirming at 18.

⁷³ CR 59.05 Order at 4.

⁷⁴ The Court of Appeals in this case distinguished HBC fees as “public funds,” while offering no explanation (except a footnote) for distinguishing the Kentucky river fees as “private contributions. (Opinion Affirming at 14, f. 19) Once again, the Court of Appeals offers up only a thin and conclusory analysis.

A cycle of fee increases, followed by transfers of fee account balances for use as General Fund taxes, followed by more fee increases to replenish the accounts, to be followed by more transfers from account balances for use as taxes, has been demonstrated in this case. In fact, Moloney admitted that the downturn of the economy and transfers totaling \$10 million has left his agency with no “excess funds” and needing to increase fees. (Moloney depo. at 31-32)

Transferring restricted funds began in 1984 leading to the decisions in *Armstrong* and *Thompson*. These transfers, whether or not characterized as “excess funds,” have become more expansive, in good times and bad times, during budget surpluses and shortfalls, in every biennial budget since 1984. Routine transfers of workers’ compensation assessments paid by employers, beginning in 2000, led to this Court’s recent ruling in *Haydon Bridge*, where, like this case, non-tax revenue has been used to supplement General Fund taxes.

The trial court in *Louisville Soccer Alliance v. Beshear* (now pending in this Court) accurately pointed out that this Court in *Armstrong* “was very explicit that its ruling applied only to ‘temporary, determinable suspensions of the statutes relating to the appropriations of public funds.’”⁷⁵ The Opinion Affirming would expand *Armstrong* to grant murky authority for taking any fee amounts called “year-end balances” even where as here, the taking occurs in mid-year (Gov. Beshear’s Order No. 08-01) and before the fees are even collected (2008-10 biennial budget bill). This practice would assure not even a pretense of difference between constitutional taxes and police power fees.

⁷⁵ Opinion and Order of Judge Philip Shepherd at 4.

IV. THE LEGISLATURE'S ACTIONS VIOLATE SECTIONS 15 AND 51 OF THE KENTUCKY CONSTITUTION.

Section 15 of the Kentucky Constitution provides that “[n]o power to suspend laws shall be exercised unless by the General Assembly or its authority.”

Section 51 of the Kentucky Constitution provides as follows:

No law enacted by the General Assembly shall relate to more than one subject, and that shall be expressed in the title, and no law shall be revised, amended, or the provisions thereof extended or conferred by reference to its title only, but so much thereof as is revised, amended, extended or conferred, shall be reenacted and published at length.

As *Haydon Bridge* makes clear, Section 51 prescribes three things. First, any Act of the legislature shall relate only to one subject (the one subject rule). Second, an Act’s subject shall be expressed in the title of the Act (the title or notice requirement). Finally, no existing law shall be revised, amended or its provisions conferred or extended by referring to its title only, but rather when such action is intended, the Act must be re-enacted and published at length (publication requirement). (304 S.W.3d at 690.)

Armstrong, of course, sets forth the sequence of considerations under Section 51. A reviewing court must determine whether the General Assembly has acted within its statutory powers, whether the budgetary actions comply with the title requirement and whether a contested modification actually constitutes a repeal or amendment or a true modification or suspension under the reenactment and publication. (*Id.* at 701) *Haydon Bridge* found certain budget transfers violative of Section 15 and 51, as follows:

The amounts, however, taken directly from the funds and transferred to Mines and Minerals on two

occasions, as well as the five million dollars (\$5,000,000) transferred back to the General Fund from the KWCFC and BRF funds in the 2002-2004 biennial budget were not authorized by KRS 48.310(2) or KRS 48.315, and were in violation of KRS 342.1227(2)-(3) and as such, were improper suspensions under Section 15, and as "amendments," rather than "suspensions," were subject to the "publication" requirement of Section 51 of the Kentucky Constitution. There having been no publication, the transfers were, and are, invalid.

(*Id.* at 705)

Similarly, in this case the transfers at issue are not authorized by KRS 48.315 and they are in violation of KRS 48.010(13)(f) (as "restricted funds"); in violation of KRS Chapter 198B.095, .490, .676(2) and .710(2); and in violation of KRS 227.620(5); KRS 227A.050(2); KRS 236.130(3) and KRS 318.136. Just like *Haydon Bridge*, the transfers in this case were improper suspensions under Section 15 and violative of the publication requirement of Section 51.

Specifically, budget transfers from HBC accounts were ordered "notwithstanding the statutes or requirements of the Restricted Funds enumerated." (2008 Ky. Acts, c. 127 at 419 (item 29), 422, 425) This language acknowledges the true nature of HBC fees as Restricted Funds and exposes the measure as an attempt to ordain tax revenue for the General Fund out of a pool of money collected under the police power. The biennial budget is a spending bill enacted by the General Assembly under Section 51. Using the "notwithstanding" clause, the effect of the budget bill is to convert fees for building code enforcement into taxes ordered to be paid to the General Fund. This technique combines taxing and spending in the same bill in violation of Section 51.

Both the trial court and the Court of Appeals glossed over these fundamental tenets. The trial court stated:

Even if the Budget Bill effectively converted non-tax fees into taxes, the title of the Bill provides more than a clue that it deals with the revenue and appropriations affecting government agencies. HB 406 does not violate Section 51.⁷⁶

That essentially articulates a **violation** of Section 51, and the trial court altogether ignored the Section 51 rubric outlined above.

The Court of Appeals gave a mere nod to the rubric but then made this rather odd conclusion:

There is nothing to indicate that the budget bill did anything other than transfer funds **then in existence**. It acted only as a temporary suspension of the statutes. There was no amendment to the statutes that would activate the publication requirement of Section 51 of the Kentucky Constitution, thus, we find no violation thereof.⁷⁷

Of course, the funds wrongly transferred in *Armstrong* and *Haydon Bridge* were “then in existence.” Such a fact has no bearing on the Section 51 analysis. Furthermore, \$3.1 million of the transfers were fees to be collected in the future during the biennium. (2008 Ky. Acts, c. 127, 425)

In *Haydon Bridge*, agency and trust funds “taken from the possession of the KWCFC or BRF and transferred to the General Fund and Mines and Minerals” were held to be invalid and unconstitutional:

Budgetary actions cannot be termed proper “suspension” per Section 15 of the Kentucky

⁷⁶ Summary Judgment at 10.

⁷⁷ Opinion Affirming at 19. (Emphasis added)

Constitution, unless authorized by other budgetary authority.

(*Id.* at 704) The transfers were held to be “amendments,” and therefore subject to “publication” under Section 51. “There having been no publication, the transfers were, and are invalid.” (*Id.* at 705) This case is identical.

No claim whatsoever was made in the lower courts that the first dollars collected each year could be “taken from the possession of” HBC for use as taxes. But the last dollars, based on “cash flows,” may be taken, according to the trial court. (Summary Judgment at 12) Budgetary suspensions to take the last dollars constitute amendments to the Uniform State Building Code⁷⁸ by suspending “the statutes or requirements of the Restricted Funds enumerated below.”⁷⁹

Haydon Bridge distinguished between funds “in the possession of” the BRF (*i.e.*, employer assessments) and “public funds” (*i.e.*, coal severance taxes transferred from the General Fund). The Court stated “the diversion of such public funds prior to their receipt by the KWCFC or BRF” is proper. (*Id.* at 704) The General Assembly may divert “public funds” by using its “suspension” power to “take back what it has already given by invading agency funds.” (*Id.* at 704) ***In this case, there are no funds to take back.*** HBC fees “in the possession of” five Boards and the Commissioner are not public funds (*i.e.*, taxes). Changing

⁷⁸ KRS Chapters 198B, 227, 236 and 318 are the working parts of the Uniform State Building Code “which shall establish standards for the construction of all buildings, as defined in KRS 198B.010 in this state.” KRS 198B.050(1).

⁷⁹ KRS 198B.010(10), KRS 198B.095(2), KRS 198B.615, KRS 198B.676(2), KRS 227.620(5), KRS 227A.050(2), KRS 236.130(3) and KRS 318.136.

the financing of the Building Code requires “amendments” under Section 51. (*Id.* at 705) In sum, both lower courts got it wrong on Section 15 and 51.

V. THE BUDGET BILL VIOLATES SECTION 180 OF THE CONSTITUTION BY CHANGING THE PURPOSE FOR WHICH HBC FEES WERE LEVIED.

Section 180 of the Constitution provides that “no tax levied and collected for one purpose shall ever be devoted to another purpose.” The lower courts evaded this mandate by simply declaring that “HBC fees are not a tax”⁸⁰ or that “HBC account funds . . . are regulatory fees and not taxes.”⁸¹ Of course, neither court disputed that the legislature *used* the fees as though they were taxes. The logic employed is akin to declaring that a hamburger is not food, but then proceeding to eat the hamburger. If one *uses* the hamburger as food why, then, it is food. If the legislature uses HBC fees as taxes why, then, they are taxes.

In *Haydon Bridge* this Court considered whether the legislature’s redirecting coal severance tax receipts from the Benefit Reserve Fund to the General Fund violated Section 180. There was no violation because the statute levying the tax made clear that excess coal severance taxes must be credited to the General Fund:

In this case, KRS 143.090(4) provides that, “[a]ll [coal severance] tax levied by KRS 143.020 collected in excess of the amount required to be deposited to the transportation fund (road fund) or transferred to the Office of Energy Policy shall be deposited by the Department of Revenue to the credit of the general fund.” Thus, KRS 143.090(4) does not, itself, dedicate coal severance tax revenue to the KWCF or BRF.

⁸⁰ Summary Judgment at 7.

⁸¹ Opinion Affirming at 16.

Therefore, the transfer of the nineteen million dollars (\$19,000,000) in annual credits diverted from the KWCF and the BRF to the General Fund was not in violation of Section 180 of the Kentucky Constitution.

(304 S.W.3d at 706). In the case at bar, such a mandate is wholly absent. There is not even a suggestion in any of the statutes that levy HBC fees that the fees may be credited to the General Fund (except Fire Protection Sprinklers under KRS 198B. 615).

All of which gets back the critical distinction between Section 181 fees and police power fees. Fees imposed under Section 181 by general laws on trades, occupations and professions are "public funds." The General Assembly could have elected to appropriate income taxes, sales taxes, license fees or other taxes imposed by general laws under Sections 171, 180 and 181. Instead, the political decision was made to delegate authority to the Commissioner and HBC boards to set rates, collect money and hire staff to prevent loss of life, explosions or other disasters, enforce standards, and establish programs to improve skills. Essentially, the legislature is using a proxy to levy taxes -- it escapes scrutiny and perhaps disapprobation when the Commissioner and HBC boards set or increase "fees" and then quietly swipes the fees as taxes in the budget bill when it sees fit. The legislature may not delegate the power to tax.

The Summary Judgment states that "the various aspects of HBC indicate that its purpose, and the purpose of the fees that it collects, are public." (*Id.* at 9) There is no dispute on that point, but that public purpose can be funded either by General Fund appropriations out of tax revenue paid by all Kentucky citizens, or by fees imposed under the State's police power on those engaged in the

construction industry. *Commissioners of the Sinking Fund v. Hopson*, 613 S.W.2d 621 (Ky. App. 1980). License fees are routinely imposed as taxes by local governments under Section 181, or just as routinely imposed by the Commonwealth in the exercise of police power. (*Id.* at 623) The trial court stated that redirecting “excess public revenue to the General Fund does not violate Section 180, especially in light of the substantial public policy interest in responding to the budgetary crisis facing this state.” (Summary Judgment at 11) ***But Section 180 makes no exception for a budgetary crisis!*** And, according to this analysis, as long as the money is deemed “excess,” it can be taken as a supplemental tax for General Fund purposes such as education, prisons, Medicaid, parks, *ad largum*. But the trial court categorically concluded that HBC fees are not taxes! Contractors and others professionals paid fees totaling \$14,800,000 in FY 2008 specifically and only for building code enforcement. (2006 Ky. Acts c. 252 at 870) On January 4, 2008, \$6,495,100 was converted to General Fund taxes by executive order. Since the money is not a tax, we are told that Sections 171, 180 and 181 do not apply. Money ***used as a tax*** must be ***enacted as a tax*** under Section 171⁸² and 180. And, what if the entire \$14.8 million were taken?

The trial court cited the legislature’s constitutional power of the purse strings to appropriate money (Section 230), to contract debts (Sections 49-50), to provide for annual taxes (Section 171), and “to provide for the payment of

⁸² Section 171 provides that the General Assembly shall levy “an annual tax . . . sufficient to defray the estimated expenses of the Commonwealth . . . for public purposes only . . . uniform upon on all property . . . by general laws.”

license fees and excise tax (Section 181).” (Summary Judgment at 3) (emphasis added) It is not clear whether the court equated *license fees* under Section 181 with HBC license fees under the police power. This is but one more example how the courts below blurred the bright line between Section 181 fees and police power fees.

Even if the transfers to the General Fund are taxes, as the trial court conceded they may be (Summary Judgment at 10), Section 180 would prohibit their use for a different purpose. Constitutional limits on the right of the General Assembly to act are determined by the courts based on the “existence or nonexistence of the facts authorizing legislative action.” The General Assembly cannot “lift itself by its own boot straps in violation of the Constitution” by acting upon authority which does not exist.⁸³ Non-tax fees collected administratively may not be “boot strapped” into General Fund taxes. In short, balancing the budget does not override other constitutional directives.

Year-end balances, even if regarded as “excess funds,” cannot be magically transformed into taxes in a biennial budget bill. Only the General Assembly may levy a tax under Section 180.⁸⁴ The enactment must specify the purpose of the levy and no tax collected for one purpose shall ever be devoted to another purpose. Even if HBC fees were somehow regarded as taxes, the purpose for which they are levied and collected is limited to building code enforcement, and would be prohibited from transfer to the General Fund under the constraints of

⁸³ *Ky. Sheriffs’ Assn. v. Fisher*, 986 S.W.2d 444, 447 (Ky. 1999).

⁸⁴ *St. Ledger v. Revenue Cabinet*, 942 S.W.2d 893, 898 (Ky. 1997).

Section 180. Determining the legitimacy of the challenged governmental practice is appropriate where a constitutional violation is alleged.⁸⁵

VI. TAKING FEES PAID FOR LICENSES AND PERMITS TO SUPPLEMENT THE GENERAL FUND VIOLATES CONSTITUTION SECTIONS 2 AND 242.

The trial court's ruling empowers the General Assembly to retroactively take any or all restricted funds for use as taxes to balance the budget because "the government has a legitimate state objective in utilizing public revenue to address the massive revenue shortfalls facing the Commonwealth." (Summary Judgment at 10) The court cited the legislature's plenary powers of the purse strings.⁸⁶ But the State's police powers are neither plenary nor unlimited.⁸⁷ The trial court agreed that HBC fees are not taxes and that the agency was created under the Commonwealth's police power. (Summary Judgment at 7-8)

Police powers are justified when exercised prospectively. Appellees admit that license and permit fees are assessed in anticipation of being revenue neutral only to fund the HBC office. (Moloney depo. at 19-20) Regulatory schemes "are presumed to be valid, but they must be consistent with the statutes authorizing them."⁸⁸ The Airport Commission expanded its jurisdiction beyond its statutory authority. This Court held that an authority may not retrospectively take

⁸⁵ *Coulthard v. Com.* 230 S.W.3d 572, 582 (Ky. 2009).

⁸⁶ Power to make appropriations (Section 230), to contract debts (Sections 49-50), to provide for annual taxes (Section 171), and to provide for payment of license fees and excise taxes (Section 181). (*Id.* at 3)

⁸⁷ *Ky. Central Life Ins. Co. v. Stephens*, 897 S.W.2d 583, 591 (Ky. 1995).

⁸⁸ *Ky. Airport Zoning Commission v. Ky. Power Co.*, 651 S.W.2d 121, 124 (Ky. App. 1983).

property for a “retrospective operation” in the exercise of police powers. Taking year-end balances from HBC accounts constitutes a retrospective use in violation of Section 242.

“In the proper exercise of police powers the right to use the property may be limited without compensation.”⁸⁹ The crux of that limitation is “that the action must bear a real and substantial relationship to the public health, safety, morality, or some other phase of the general welfare” regulated by the activity.⁹⁰ Taking year-end balances (or mid-year transfers) bears no relationship to HBC purposes. The action “is arbitrary and cannot stand as a valid exercise of the police power.” (*Id.* at 473)⁹¹

Arbitrariness is the hallmark of the HBC transfers. The amount of tax created out of each life safety account ranged from a nominal transfer of \$100 taken from fire protection sprinklers to \$2,750,100 raided from electricians and electrical inspectors. Plumbers were assessed \$900,000 and HVAC contractors were assessed \$700,000. The Executive Order specified transfer of \$6,495,200 from fees paid for certification, license, inspection, and permitting by persons engaged in the building and construction industry. However, the Executive Order was arbitrarily changed by the State Budget Director, who explained in Answer to Interrogatory 15 as follows:

⁸⁹ *Com. v. Stephens*, 539 S.W.2d 303, 306 (Ky. 1976).

⁹⁰ *Dept. for Natural Resources v. Stearns Coal*, 563 S.W.2d 471, 473 (Ky. 1978).

⁹¹ By contrast, this Court’s ruling *Gray v. Methodist Episcopal Church*, *supra*, upheld using auto registration fees for road repairs as a valid exercise of police powers.

Prior to executing the mandated fund transfers, the Office of State Budget Director, in coordination with staff of the Environmental and Public Protection Cabinet, reviews the sufficiency of the account balances and the cash-flow liquidity and appropriated spending needs for the subsequent fiscal year. That review determined that the Plumbing account and HVAC account receipts were significantly less in fiscal year 2008 than HBC has estimated. Due to the level of decline in receipts and the anticipated cash-flow needs of the agency to begin the new fiscal year, these two amounts, \$900,000 for Plumbing and \$7000,000 for HVAC, were not transferred.

In order to “sustain legislative interference with the business of the citizen, by virtue of the police power,” the court must be able to see “the preservation of the public health, morals, safety or welfare.” If it is manifest that a legislative act “under the guise of the police regulation, is an invasion of the property rights of the citizen, it is the duty of the court to declare it void.”⁹² Fees paid under the guise of protecting public health and safety may not be retroactively taken as General Fund taxes.

Cash flow needs of HBC were mysteriously determined by bureaucrats, not by the five boards and the Commissioner who assess and collect fees. Moloney testified he did not know how the amounts to be transferred were determined, but he was “part of the influence” in changing the amounts *after* the budget was enacted. (Moloney depo. at 25-26) Appellees offered no further explanation. Fair and unbiased procedures, free of arbitrary state action, whether legislative, judicial or administrative, are guaranteed by Constitution Section 2. (*Smith v.*

⁹² *McGuffy v. Hall*, 557 S.W.2d 401, 413 (Ky. 1997).

O'Dea, 939 S.W.2d 353, 357 (Ky. App. 1997)).⁹³ Vital programs like boiler inspection (\$300,000) and elevator inspection (\$400,000) had money taken based on "cash flow."⁹⁴ Fundamental fairness, unbiased procedures, and uniformity in financing HBC were by no means factors in the cash flow analysis of the budget office.

Apparently, the controlling standard for this tax assessed by Executive Order was to get the money from any available source without respect for uniformity. The General Assembly's ***power to collect*** is its taxing authority under Sections 171, 180 and 181. HBC Boards' and the Commissioner's ***power to collect*** is police power, not taxing power. The General Assembly may not delegate power to tax. Yet, the trial court has declared that the General Assembly's ***power to spend*** includes the power to retroactively use police power fees as taxes by declaring a budget dilemma. (Summary Judgment at 12) Arbitrary amounts were appropriated from ten HBC accounts ranging from a nominal \$100 taken from Fire Protection Sprinkler money to \$2,750,100 from electricians and electrical inspectors. (Moloney depo. at 25-26) There was no uniformity in amounts transferred.

⁹³ Uniformity required under Section 171 and the exercise of arbitrary power prohibited by Section 2, are closely related. *City of Lexington v. Motel Developers*, 465 S.W. 2d 253, 257 (Ky. 1971). If the lower courts characterized HBC fees as Section 181 fees, then uniform classification required by Section 171 is clearly lacking. If properly characterized as police power fees, the classifications are arbitrary under Section 2.

⁹⁴ Appellees acknowledged a backlog of 6,000 to 8,000 industrial boiler inspections as of September 15, 2008, due to staffing shortages. Moloney said HBC was trying to fix the understaffing because "you can have an explosion, you endanger somebody's life and that's what we're out there to do, to try to keep anybody from getting killed over an explosion." (Moloney depo. at 20-24)

Section 2 is particularly apt to invalidate a tax scheme that empowers bureaucrats with absolute discretion to convert dedicated, non-tax pools of money over to General Fund accounts. The budget provision improperly delegated to the Executive Branch authority to make selective transfers by absolutely arbitrary means.⁹⁵ That is the unmistakable import of this ruling by the trial court:

The broad scope of the 2008 Budget Bill was designed to redirect cash flows in the interest of balancing the Commonwealth's budget. HBC was far from the only agency subject to fund transfers. As to the specific amounts taken from individual HBC accounts, it is left to the executive branch to decide how best to effect a legislative mandate. Basing these decisions on cash flows is rationally related to the state's interest in balancing the budget. We do not find any Constitutional infirmities here.

(Summary Judgment at 12) The entire scheme is fraught with constitutional infirmities. The function of the Court is "to decide a test of regularity and legality of the board's actions by statutory law and by the constitutional protection against the exercise of arbitrary and official power."⁹⁶

Who decides how much tax gets assessed against each category? Is the degree of public risk a factor? How much increase in certificate and license fees will be needed? Will inspectors be fired because fees collected for life safety programs have been converted to General Fund taxes? Which comes first, enforcing the state building code or the biennial budget? The utter lack of answers to all these questions demonstrates that Section 2 forbids the

⁹⁵ *Diemer v. Trans. Cabinet*, 786 S.W.2d 861, 865 (Ky. 1990).

⁹⁶ *Ky. Milk Marketing v. Kroger Co.* 691 S.W.2d 893, 899 (Ky. 1985).

shenanigans devised in the budget provision at issue. Arbitrary and discriminatory features built into the budget transfers are breathtaking.

The 2008-10 biennial budget parlayed “excess funds” or “year-end balances” into a new tax supplementing state government finances. Such treatment constitutes a taking in violation of Section 242. Private property rights must yield to the public interest unless the exercise of constitutional police power exceeds the limits of “reasonability.”⁹⁷

VII. THE HBC TRANSFERS VIOLATE THE EQUAL PROTECTION CLAUSE.

The trial court found that the 2008 budget bill transfers “designed to redirect cash flows in the interest of balancing the Commonwealth’s budget” did not violate the equal protection clause. The court said that “(b)asing these decisions on cash flows is rationally related to the state’s interest in balancing the budget.” (Summary Judgment at 12) Equal protection of the *state’s interest* is not the issue. Equal protection for licensees and permit holders, who pay fees for regulatory and enforcement purposes, then see over \$10 million dollars of their money ripped away to finance the state’s deficit, is the stuff this appeal confronts. The trial court correctly noted that the measure of equal protection is whether “the law is rationally related to a legitimate governmental objective . . . or if it is founded upon any substantial distinction suggesting the necessity or propriety of

⁹⁷*Adams, Inc. v. Louisville Jefferson Co. Board of Health*, 439 S.W.2d 586, 589 (Ky. 1969), *Lexington Fayette Food v. Urban City Government*, 131 S.W.3d 745, 752 (Ky. 2004).

such legislation.”⁹⁸ In considering whether a legislative act “is rationally related to a state objective, we begin by reviewing the purpose of the provision.”⁹⁹ The HBC budget transfers bear no relationship, rational or otherwise, to the police power regulatory purposes for which the fees are paid. According to the trial court’s reasoning, the retirement fund transfers banned in *Armstrong* and the workers compensation transfers banned in *Haydon Bridge* are “rationally related to the state’s interest in balancing the budget” and therefore do not violate equal protection. The trial court measured equal protection based solely on the interest of the state, not the interest of the HBC regulatory program or its licensees and permit holders.

Similarly, the Court of Appeals noted that regulation of economic matters comports with equal protection “if it is rationally related to a legitimate state objective.”¹⁰⁰ The Court of Appeals opinion, however, contains no analysis of what “legitimate state objective” is served by taking HBC regulatory fees for unrelated budget purposes. The court simply concluded that the “person challenging a law upon equal protection grounds under the rational basis test has a very difficult task because the law must be upheld if there is any reasonably conceivable state of facts that could provide a rational basis for the

⁹⁸ Summary Judgment at 12, citing *Kentucky Harlan Coal Co. v. Holmes*, 872 S.W.2d 446, 455 (Ky. 1994).

⁹⁹ *Wynn v. Ibold Inc.* 969 S.W. 2d 695, 696 (Ky. 1998).

¹⁰⁰ Opinion Affirming at 21, citing *Wynn v. Ibold Inc.*, *Kentucky Harlan Coal Co. v. Holmes*, *supra* and others.

classification.”¹⁰¹ Presumably, the court agreed with the trial court that “the state’s interest in balancing the budget is the sole measure of equal protection in this case. Both the trial court and Court of Appeals ignored the fundamental considerations of purpose and public safety in the HBC regulatory fee program.

If the General Assembly wants to make HBC a tax collection agency like the Department of Revenue, the statutory scheme must be amended to conform with constitutional requirements. Balancing the budget does not supersede other provisions of the Constitution. Balancing the budget is a monumental challenge when revenues are projected to fall \$1 billion short of General Fund appropriations, but the General Assembly has the authority to increase income taxes or other taxes as it sees fit. It does not have the arbitrary power to increase taxes without uniform classification, or to arbitrarily convert fees for prevention of life safety hazards and other disasters into discriminatory taxes.

CONCLUSION

There seems little doubt that HBC fees are police power fees that may not be used to supplement general tax receipts for the operation of state government. The transfers at issue are barred by this Court’s decision in *City of Henderson v. Lockett* and its progeny. In addition, HBC fees are “private funds” as that term, has been defined in *Armstrong, Thompson and Haydon Bridge*. As such, the legislature may not transfer HBC fees into the General Fund. Finally, and just as fundamentally, the transfers at issue violate Sections 2, 15, 51, 180 and 242 of the

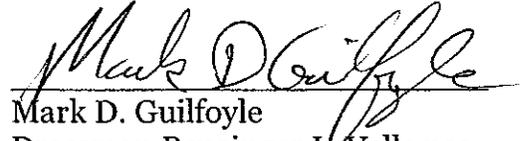
¹⁰¹ Opinion Affirming at 21, citing *Commonwealth ex rel. Stumbo v. Crutchfield*, 157 S.W. 3d 621, 624 (Ky. 2005), citing *United States Railroad Retirement Board v. Fritz*, 449 U.S. 166, 101 S. Ct. 453, 66L. Ed. 2d 368 (1980).

Kentucky Constitution, as well as the Equal Protection Clause. The grant of summary judgment in Appellees' favor should be reversed.

Respectfully submitted,



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Appendix

1. 1/19/10 Franklin Circuit Court Opinion and Order Granting Defendants' Cross Motion for Summary Judgment
2. 3/25/10 Franklin Circuit Court Opinion and Order Denying Plaintiffs' CR 59.05 Motion to Alter, Amend, or Vacate
3. 1/6/11 Court of Appeals Opinion Affirming