

INTERIM JOINT COMMITTEE ON APPROPRIATIONS AND REVENUE

Minutes of the 4th Meeting of the 2022 Interim

September 21, 2022

Call to Order and Roll Call

The 4th meeting of the Interim Joint Committee on Appropriations and Revenue was held on Wednesday, September 21, 2022, at 1:00 PM, in Room 149 of the Capitol Annex. Representative Jason Petrie, Chair, called the meeting to order, and the secretary called the roll.

Present were:

Members: Senator Christian McDaniel, Co-Chair; Representative Jason Petrie, Co-Chair; Senators Danny Carroll, Donald Douglas, David P. Givens, Stephen Meredith, Michael J. Nemes, and Stephen West; Representatives Lynn Bechler, Danny Bentley, John Blanton, Randy Bridges, Ken Fleming, Chris Fugate, Al Gentry, David Hale, Angie Hatton, Bobby McCool, Ruth Ann Palumbo, Melinda Gibbons Prunty, Josie Raymond, Brandon Reed, Steve Riley, Sal Santoro, James Tipton, and Lisa Willner.

Guests: Eric Kennedy, Director of Advocacy, Kentucky School Boards Association; Nick Clark, President, Kentucky Association of School Business Officials; Charles Aull, Executive Director, KY Chamber, Center for Policy & Research; and Katherine Loughhead, Senior Policy Analyst, Tax Foundation.

LRC Staff: Jennifer Hays, Sarah Watts, Hunter Branham, and Lexi Bensberg.

Approval of Minutes

Upon motion and second, the minutes from the August 17, 2022, meeting were approved without objection.

K-12 Funding – School Board Employee Raises

Eric Kennedy, Director of Advocacy, Kentucky School Board Association (KSBA) and Nick Clark, President, Kentucky Association of School Business Officials, testified on the impact that 2022 RS HB 1 has had on school districts across the state.

Mr. Kennedy testified that 2022 RS HB 1 included increases in funding that the KSBA has advocated for in previous budget cycles. Among these increases were the Support Education Excellence in Kentucky (SEEK) base per pupil amount, transportation reimbursement, and the per-child rate for Family Resource and Youth Service Centers (FRYSCs).

To further explain the SEEK formula, and how HB 1 has benefitted school districts, Mr. Kennedy provided Todd County's final calculation sheet from last year and its most recent calculation sheet for the current school year. This county was chosen because it can be considered average, as the funding received by a district is dependent on the county's local property assessment. It would be a misrepresentation to provide a calculation sheet for a county that is 'property poor' or 'property rich'. Other factors considered in the SEEK formula include attendance, number of children, and the number of children considered to be 'at-risk' in a district.

Mr. Kennedy also provided the calculations for Livingston County to provide an explanation for 'hold-harmless districts.' These are districts that, when assessing the typical variables in the SEEK formula, would receive less SEEK funding in the current school year than they received in the 1991-92 school year. Budget bills enacted by the General Assembly provide a guaranteed per pupil amount, which prevents school districts from receiving less SEEK funding than what they received in the 1991-92 school year.

In the 2022 Session, the General Assembly encouraged local school boards to adopt employee raises. The KSBA conducted a survey in July to ascertain local school board approved employee raises. All 171 districts responded to the survey, and responses were provided in legislators' folders for the meeting. 162 districts responded that their school board approved an across-the-board employee raise for the 2022-23 school year, though the school boards of 105 of these districts approved salary increases that were more nuanced and involved a consideration of staff classification.

In response to a question from Chair Petrie, Mr. Clark testified that the budget passed in 2022 was the most favorable for education in recent history.

In response to a question from Senator McDaniel, Mr. Kennedy testified that it would be beneficial to continue looking at the SEEK formula and consider changes that would make its resulting funding more equitable between districts. It is possible that with increasing property values, more counties could fall into the 'hold-harmless' category.

In response to a question from Senator Nemes, Mr. Clark clarified that the more a district receives in local property tax, the less it will receive in SEEK funding. Mr. Kennedy testified that when considering this, it is important to evaluate all the variables in the formula.

In response to a question from Senator Carroll, Mr. Kennedy testified he is not aware of requirements in statute that ensure that SEEK money provided for specific variables is spent on said variables. However, there are mandates in state and federal law that require schools to provide services to specific classifications of students regardless of the funding they receive from the state.

In response to a question from Representative Willner, Mr. Kennedy said that school boards would be able to provide more to students if they were provided more funding.

In response to a question from Representative Tipton, Mr. Kennedy testified that there are large disparities in pay across school districts within the state.

Tax Modernization Issues

Charles Aull, Executive Director, KY Chamber, Center for Policy & Research and Katherine Loughead, Senior Policy Analyst, Tax Foundation, testified on Kentucky's opportunity for growth in terms of tax modernization.

Mr. Aull testified that tax policy reforms that occurred in 2018 and 2019 have had a positive impact, and will continue to grow. These reforms included eliminating income tax brackets and reducing Kentucky's individual and corporate tax rates from 6 percent to 5 percent. He predicts that HB 8 will have a similar positive impact by the reducing the individual income tax rate.

In order to consider attracting more population into the state, the legislature must understand that there is ample competition from other states in terms of tax modernization. This competition is further intensified when considering that the number of interstate migrants continues to trend downwards. There are a multitude of factors that people consider when looking to move states. There is research that suggests a connection between state taxation and geographic mobility.

Mr. Aull testified that improvements could be made through transparency of the amount in the state's budget reserve trust fund, improvement of cost recovery, changing the inventory tax, and multiple other avenues.

Ms. Loughead testified that there are reforms that can be made to the Kentucky tax code that would be conducive to the state's economic growth while minimizing economic harms to taxpayers. Including Kentucky, 24 states have recently enacted income tax cuts. There is also a trend away from graduated tax structures, Kentucky enacted a flat tax rate in 2019. By the end of 2026, there will be at least 14 states that have enacted a flat tax rate. These reforms create a competitive landscape that ideally attracts more constituents.

After discussing areas for potential reform in Kentucky's tax code with state legislators and constituents, the Kentucky Chamber and the Tax Foundation published a report in November 2021. This report provides recommendations resulting from these discussions. In addition to the recommendations mentioned by Mr. Aull, Ms. Loughead testified in favor of improving the tax treatment of business investment expenses, shifting away from local occupational and net profit taxes, repealing the inventory tax, and reducing the reliance on tangible property taxes.

In response to a question from Senator Carroll, Ms. Loughhead testified that these suggestions would be best applied to the tax code incrementally.

Chair Petrie clarified that raising the sales tax to recoup lost revenue from the implementation of these suggestions would be a last resort.

In response to a question from Representative Raymond, Mr. Aull stated that increasing the sales tax is not the only way to recoup revenue that would be lost if these reforms were adopted. Mr. Loughhead testified that it would be likely to see the sales tax base increase before the sales tax rate would increase.

In response to a question from Senator Carroll, Mr. Aull testified that the transition from occupational licensing taxes to a sales based tax structure would be very difficult. It would be beneficial to avoid adopting tax code reforms that approach it as 'one-size-fits-all,' as it would be more difficult to apply in rural areas of the state. Regardless, the occupational licensing tax is something that employers find odd, so it would benefit economic growth to consider phasing out this tax. Mr. Aull added that the Kentucky Chamber is actively researching ways to increase economic development in rural areas experiencing trends of depopulation.

Chair Petrie made the committee aware of the additional materials provided in their folders, including the Interim Budget Allotment Adjustments for FY 2023, the Interim Emergency Appropriation Increases for FY 2023, and reports received by the Appropriations and Revenue Committee since the August meeting.

With there being no further business, the meeting was adjourned at 3:03 p.m.