INTERIM JOINT COMMITTEE ON LOCAL GOVERNMENT

Minutes of the 6th Meeting
of the 2021 Interim

October 19, 2021

Call to Order and Roll Call

The 6th meeting of the Interim Joint Committee on Local Government was held on Tuesday, October 19, 2021, at 10:00 AM, in Room 154 of the Capitol Annex. Representative Michael Meredith, Chair, called the meeting to order, and the secretary called the roll.

Present were:

Members: Senator Robby Mills, Co-Chair; Representative Michael Meredith, Co-Chair; Senators Ralph Alvarado, Denise Harper Angel, Christian McDaniel, Morgan McGarvey, Michael J. Nemes, Wil Schroder, Adrienne Southworth, Brandon J. Storm, Damon Thayer, and Phillip Wheeler; Representatives Danny Bentley, Josh Bray, George Brown Jr., Jonathan Dixon, Jeffery Donohue, Ken Fleming, Deanna Frazier, Regina Huff, Mary Beth Imes, DJ Johnson, Adam Koenig, Matt Lockett, Mary Lou Marzian, Reginald Meeks, Jerry T. Miller, Brandon Reed, Rachel Roberts, and Walker Thomas.

Guests: J.D. Chaney and Bryanna Carroll, Kentucky League of Cities; Mayor Brian Traugott, City of Versailles; Mayor Jim Hamberg, City of Southgate; Tammy Vernon and Bill Pauley, Department for Local Government; Bruce Roberts and Chuck Bonta, Kentucky Fire Commission; Jim Henderson and Shelley Hampton, Kentucky Association of Counties; Carter Hendricks, South Western Kentucky Economic Development Council; Andi Johnson, Commerce Lexington; and Shelby Williams Somervell, Greater Louisville Inc.

LRC Staff: Mark Mitchell, Christopher Jacovitch, and Cheryl Walters.

Upon the motion of Senator Wheeler, seconded by Senator Nemes, the minutes from the September 22, 2021, meeting were approved.

Kentucky League of Cities' Legislative Platform for the Upcoming 2022 Session of the General Assembly

Mr. J.D. Chaney, Executive Director and CEO of the Kentucky League of Cities (KLC), told the Committee that some of KLC's issues are continued from last year. He then introduced City of Versailles Mayor Brian Traugott, KLC President, and Southgate Mayor Jim Hamberg, KLC First Vice President, to discuss the League's priorities for 2022.

Mayor Traugott stated that KLC has three principles of advocacy which are home rule; adequate, stable, and flexible resources; and economic prosperity. Kentucky cities are growing. The 2020 U.S. Census showed city residents account for 56 percent of Kentucky's total population. Kentucky cities, collectively, increased their population by 7.1 percent from 2010 to 2020. Cities added over 167,000 people—slightly more than the number of new residents, meaning current Kentuckians also moved into a city.

The League's top priority for 2022 is revenue diversification. Revenue-limited cities must have the ability to generate the funds needed to pay for the services people expect if Kentucky wants to continue to grow and prosper. To do this, Kentucky must modernize its antiquated funding options, equalize revenue tools currently only available to some cities, and amend section 181 of the constitution. This section impedes the legislature's ability to comprehensively reform local government tax policies. Revising it would bring local government revenue collection in line with the 21st century. Cities are currently forced to heavily rely upon revenue largely generated from productivity.

The restaurant tax is only available to former cities of the fourth and fifth class, does not increase taxes on businesses, and is paid by tourists, so entire financial burden is not solely on residents. KLC would like to expand this to all cities but with limits and concessions. Other revenue issues of KLC include local sales tax, protecting crediting provisions of occupational license taxes, and opposing centralized collection of local revenue.

Road funding is another KLC priority for 2022. Kentucky has not updated its gas tax since 2015, and is last among neighboring states for motor fuels revenue. Forty-eight percent of the amount collected is allocated to city, state, and rural roads and is divided using a system known as the "formula of fifths," which the legislature established in 1948 and which favored rural areas without accounting for increasing municipal road miles.

The current road funding modernization proposal includes updating the antiquated funding formulas. Funds over the 2014 high mark of $825 million would be evenly split between the municipal and county road aid programs at 13 percent each. Cities maintain more than 10,000 miles of public streets. Since 2009, Kentucky cities spent 62 percent more on city streets, while state and federal funding declined more than four percent. Cities spend more than $340 million a year to maintain and build streets. City streets are currently operating on a 40-year replacement cycle which more than doubles the industry standard.

The American Rescue Plan Act (ARPA) is not the answer. ARPA funds are limited in use and are restricted to COVID recovery. ARPA funds generally cannot be used for transportation funding shortfalls and supporting city services and revenue needs.

Another 2022 priority of the League is economic development. Kentucky cities drive the state's economy. Cumbersome and outdated restrictions can cause roadblocks.

The only tax increment financing provision of 2021 SB 162 creates unnecessary expenses and delays for local governments. The League appreciates legislators' efforts toward ameliorating those expenses and delays.

Law enforcement training is an issue of concern. Police cadets can wait several months for training at the Kentucky Department of Criminal Training delaying the time that a new hiree can begin patrolling up to almost a year.

Regarding the issue of paramedic training and certificate of need, current delays are being caused by a statewide paramedic shortage and a lengthy process to obtain an emergency certificate of need.

Mayor Hamberg told the Committee that KLC supports legislation that addresses the criminal aspects of substance abuse and measures that take a proactive stance on treatment, rehabilitation, training, and workforce reentry. The current COVID-19 pandemic resulted in an increase of up to nearly 50 percent in 2020 of overdose deaths.

Publication requirements costs city taxpayers around $1.4 million a year. Publicly owned city websites are available free of charge and allow documents to be available longer. 2020 House Bill 195 allows cities in counties that have a population of 80,000 or more to publish documents and advertisements on a website in lieu of publishing in a local newspaper, which is only 145 cities in nine counties. KLC would like to expand this availability to more cities.

Cities are looking to work with PVAs and others to ensure property ownership information is received in a timely manner. KLC would like to streamline the process used for proposing a tax rate when that tax rate would generate more than four percent more revenue than the compensating rate.

Cities are responsible for public safety and employ around 57 percent of Kentucky's full-time law enforcement officers. Cities handle 74 percent of the state's reported violent crime and spend more than $500 million a year in wages and benefits for police services. KLC would like to address the limitations on number of former officers and firefighters a city may employ, limitations on work schedules and policies, and the unique aspects of jobs within a fire and police department. 2019 House Bill 191 and 2021 SB 80, strengthened Kentucky's police decertification law. The Kentucky Law Enforcement Council needs to be able to terminate officers whose behavior is of concern without a bill of rights hearing if the officer has been decertified.

Regarding the Open Meetings Act, closed sessions of the locally-elected legislative body are sometimes required to protect proprietary information and taxpayer resources. Mandatory public hearings on municipal road aid and Local Government Assistance program funds are often inconvenient for citizens and unattended. KLC seeks to provide city employees and proprietary information the same privacy protections afforded to the state for similar purposes.

Regarding alcohol licensure, 2019 SB 29 allowed cities with a population of less than 20,000 to impose a regulatory license fee to help offset the cost of extra policing and regulation. KLC wants all municipalities to be able to recover those costs.

Untrained constables threaten the safety of citizens and trained law enforcement. KLC advocates eliminating constables' peace officer powers while maintaining their other powers and uses.

Municipal audit requirements are often cumbersome and costly for cities with no long-term debt and small budgets. KLC seeks to increase the audit exemption amount and lengthen the time to perform the audit before penalties are incurred.

Nonoperative homeowner associations and planned-unit developments can create unfavorable living conditions and lead to concern about maintenance of common areas. KLC seeks solutions to provide these service gaps when homeowner's associations or planned-unit development governing bodies cease operations or the fees derived therefrom are insufficient.

Energy-efficient lighting can save taxpayer resources while ensuring safety. KLC wishes cities to either be able to assume control of streetlights not owned by the city, or otherwise to be able to require electric utilities to install more efficient lights.

KLC seeks the ability of a municipal utility to escrow, rather than lose, funds from a rate increase if the rate increase is appealed to the Public Service Commission.

KLC advocates for adding penalties for private utilities that violate franchise agreements, as there are no present penalties for violating those agreements.

Government offices are subject to natural disasters, such as a floods or fires. Replacing damaged records is often complicated and expensive. KLC supports allowing an affidavit process to stand in lieu of lost or damaged documents to the Department for Local Government can help ensure assets are not frozen.

KLC seeks additional representation on tourism boards. Cities covered by a regional tourism commission need representation from at least the largest city in each county. Cities served by a consolidated local government tourism commission seek representation.

Paramedic and EMS services are vital but costly. Cities often are responsible for covering costs. KLC supports a user fee, like current 911 fees, which could help ensure funding to maintain these life-saving services.

KLC seeks to ensure that cities providing waste collection do not encounter lengthy publication requirements before extending a service agreement to neighboring areas.

KLC supports a legislative change to allow cities that do not collect funds or have elected officials to be dissolved through an administrative process instead of through the court system.

In response to a question from Senator Wheeler, Mr. Chaney stated revenue sharing between counties has been talked about for some time. Section 181 of the Constitution restricts the General Assembly's authority to allow counties to share revenue.

In response to another question from Senator Wheeler, Mr. Chaney said adjusting Section 181 of Kentucky's constitution could help negate competition between cities and counties for revenue options because the legislature would have more latitude to give local governments more revenue producing options. Regarding revenue issues relative to jails and the origin site of the violation, cities support the state increasing its financial assistance to counties regarding jail costs.

Representative Fleming commented that tax reform efforts need to be increased.

In response to a question from Representative Fleming, Mayor Traugott stated that cities need fiscal flexibility to offer incentives such as amenities to attract people from other states.

In response to a question from Senator Mills, Mr. Chaney said the formula for road funding has to be modernized as the tax is adjusted to account for any state changes accounting for the corporate move away from gasoline. Cities and counties will have to share funding. Senator Mills commented that there needs to be forward thinking in the future.

In response to a question from Representative Johnson, Mayor Traugott replied that it is not so much about adding new taxes, but diversifying the sources of revenue. It is not so much about tax increases, but rather a shift away from the burden on productivity. Representative Johnson commented that money is still being taken away from private citizens. Care needs to be taken to not place additional burdens on the citizens, especially at this time.

Special Purpose Governmental Entity Reports

Ms. Tammy Vernon, Cities and Special Districts (CSD) Branch Manager with the Department for Local Department (DLG), said that SPGEs are independent political subdivisions of the state which are government entities that exercise less than statewide jurisdiction and are organized for the purpose of performing specific services within limited boundaries.

DLG's statutory responsibility is to create and maintain an online central registry, reporting portal, and public access portal, and to monitor compliance by tracking status changes when notified, preparing statutorily required reports, and activating noncompliance procedures.

Ms. Vernon explained the timeline of the SPGE system consisting of the following phases: Phase I SPGE User Dashboard, Cycle 1: January - December, with a "go live" date of November 19, 2021; Cycle 2: April - March, with a "go live" date of February 15, 2021; Cycle 3: July - June, with a "go live" date of May 15, 2021; and Cycle 4: October - September, with a "go live" date of August 15, 2021. SPGE system features include users being able to assist SPGEs, oversight agencies, and CPAs in submitting requirements under KRS Chapter 65A. SPGE requirement checklists, maintaining account information, maintaining board meeting dates and board members, a message/alert center, specialty forms, data export, registration, budgets, and audits are all included as dashboard administration features. The Phase II SPGE Public Portal first meeting with Commonwealth Office of Technology (COT) was October 13, 2021, in which building process maps and storyboards were discussed with COT business analysts. The estimated "go live date" to be at the end 2022.

As of September 24, 2021, the SPGE Compliance Report showed 3.26 percent out of compliance, and 96.74 percent in compliance with additional compliance expected. The data included fire districts reporting to DLG.

Senator Thayer commented that it was more effective to testify before a legislative committee in person rather than by Zoom.

Mr. Bruce Roberts, Deputy Director, and Mr. Chuck Bonta, Training Records and Compliance Specialist, Kentucky Fire Commission, discussed fire department compliance reporting. In Fiscal Year (FY) 18, 458 of 460 (99 percent) fire departments complied with reporting; 492 of 499 (98 percent) in FY 19, 470 of 487 (97 percent) in FY 20; and 381 of 487 complied with reporting as of October 13, 2021.

At the time of the submitted report on October 13, 2021, there were 106 of 487 fire departments non-compliant (22 percent) for FY 21 year end actuals. Letters were sent to all non-compliant departments. At reporting time in 2020, non-compliance was at 22 percent. Reasons for high non-compliance numbers included COVID-19 causing delays and meeting cancellations, high loss of volunteer firefighters/administrative changes, and confusion over reporting requirements.

There are 33 Chapter 75 fire departments that report to the Fire Commission. 442 Chapter 273 fire departments report to the Fire Commission. There are 12 Chapter 75 Fire Tax Districts that are money raising districts and who contract out for their firefighter service coverage for a total of 487 reporting FY 21 to the Fire Commission. There are 775 total fire departments in the state, compared to 780 in the last reporting period.

Two percent of total fire departments reported over $500,000 in revenues, 14 percent reported over $100,000 but less than $500,000 in revenues, and 84 percent reported less than $100,000 in revenues.

Changes within the Fire Commission organizational structure to meet the needs of the fire departments in improving compliance in several areas include the addition of a fire commission compliance specialist to staff, and identifying the need to increase communication with agencies. With the addition of a compliance specialist, the Fire Commission will conduct an in-person financial review of departments every 12 to 18 months rather than every four years, as is the present span.

Constitutional Amendment relating to Local Taxation

Representative Meredith told the committee that the issue of local taxation is not a new topic. This effort is necessary to be competitive regionally and nationally, and to have a growing revenue stream for local governments. The effort to amend the Constitution stems from 2019. KLC and KACo have been core partners in the effort and the work has involved other stakeholders and research.

There are 416 cities in Kentucky. Those derive 59.1 percent of their revenues from local occupational and business taxes, 49 percent from payroll deductions, 5.5 percent from net profits, and 1.1 percent from gross receipts. From the 120 counties in Kentucky, 42.6 percent of their revenues come from business and payroll taxes, 39.1 percent come from payroll deductions, and 3.5 percent from net profits taxes. Louisville derives 57.4 percent of its revenues from business and payroll taxes. Lexington derives 66 percent of its revenue from business and payroll taxes.

Thirty-eight states allow for a local sales tax. Only 17 states allow a local income tax. Kentucky is in the top five regarding local government dependence on income and productivity-based taxes.

There has been a half decade's worth of effort at trying to get the state away from productivity based taxes, but to proceed on a local level, Section 181 of Kentucky's constitution needs to be amended to get the flexibility to help local governments transition away from those types of taxes.

Mr. Jim Henderson, Executive Director of the Kentucky Association of Counties (KACo), told the committee taxation has been the subject of discussion for the duration of his career in local government. Amending Section 181 is crucial to actually implementing substantial tax policy changes. The usage of a consumption-based tax in 38 states shows that it is more competitive, advantageous, and sustainable than non-consumption-based taxes. Tennessee's economy has grown even with its relatively high sales tax.

Mr. Chaney stated that Section 181 of the Constitution prohibits the General Assembly from giving local elected officials the ability to make many revenue decisions. The amendment to Section 181 will allow the General Assembly to have the discussions to enact legislation to allow the implementation of tax policy on the local level.

Representative Meredith reminded the committee that it takes a supermajority of the General Assembly to put the measure on the ballot to then be voted on by the public. If the public approves the proposal, then thoughtful discussions on tax policy would begin. The process is lengthy and will not happen immediately.

Mr. Carter Hendricks, Executive Director of the South Western Kentucky Economic Development Council, pointed out that in 1970, Hopkinsville and its neighbor Clarksville, Tennessee, were essentially the same size at roughly 25,000 people. Fifty years later, Hopkinsville's population is around 32,000 people while Clarksville's has grown to over 160,000. From 1980-2020, Tennessee more than doubled Kentucky's population growth during that same time, as did Indiana. Indiana and Tennessee currently are beating Kentucky in population growth with both states approaching seven million while Kentucky has 4.5 million people.

It has become clear that most of Kentucky's 400 plus cities and counties are struggling with the same issues and challenges that prevent population and sustained economic growth. Kentucky's cities and counties are not growing or not growing fast enough to keep up with the necessary improvements and infrastructure needed to create communities that attract new residents and new businesses. Local governments do not have access to revenue measures that allow them to properly invest in themselves, their infrastructure, or economic development initiatives. Additionally, the state's reliance on the income tax system place southern border counties at a distinct disadvantage as neighboring cities in Tennessee are able to boast no income tax and attract large populations as a result.

Kentucky has a great opportunity to reform its tax system which will lead to a positive and lasting impact. If the General Assembly can have the power through the amendment to the Constitution to create a better tax system, local governments and Kentucky can build on their assets and can grow significantly.

Ms. Andi Johnson, Chief Policy Officer for Commerce Lexington, told the committee that her group is working on a strategic action plan and that the Lexington region continues to be at a competitive disadvantage when it comes to local and state taxation.

Lexington's lack of flexibility in local taxing policies impedes competitiveness. A constitutional amendment is a necessity for continued debate about overall modernization of Kentucky's state and local tax systems. Kentucky's constitution imposes a lack of flexibility in establishing tax policy at the local level. These limitations keep local communities from addressing their unique economic and revenue needs.

As the legislature continues its efforts to reform Kentucky's tax system, local governments need to be given the opportunity to make their own choices about taxation that are in the best interest of their community and economic growth. A crucial step to comprehensive tax modernization is removing the constitutional constraints that stop local governments from working collaboratively with state government and the business community to respond to a rapidly changing economy.

Ms. Shelby Williams Somervell, Vice President of Government Affairs and Communications at Greater Louisville Inc. (GLI), stated that its members strongly support a constitutional amendment and appreciates Representative Meredith for his continued leadership on the critical issue.

The outdated tax structure keeps Kentucky cities and counties at a competitive disadvantage with their peer cities because their hands are tied when it comes to new streams of revenue. Kentucky needs to build a more competitive local tax structure to support economic growth, promote business development, and attract and retain talent. Taking this first step in passing a constitutional amendment will give the General Assembly the opportunity to rethink and recreate local taxation in the Commonwealth.

GLI urges the General Assembly to take this first step in giving cities and counties the ability to thrive in today's economy. The business community stands ready to support the next session and looks forward to the robust discussion in sessions to come regarding what that local tax structure looks like.

In response to a question from Senator Wheeler, Representative Meredith replied that there will be no tax on groceries—the local taxes would be the same taxes as collected on the state level to comply with the streamlined sales tax agreement.

Representative Koenig commented that this effort is good policy. There are collection problems with many taxes, but less so with a sales tax. Amending the Constitution would promote flexibility and options for local governments.

In response to a question from Senator Southworth, Representative Meredith said he didn't have an answer as to why Section 181 of the Constitution was written that way, but it was probably a result of the economy of the day.

In response to another question from Senator Southworth, Representative Meredith said changing the Constitution first will remove tax discussions from a hypothetical phase into a practical phase. Nothing in the constitution caps rates—this is done by statute presently. There could be discussions about caps, floors, and triggers that affect existing taxes. Reports are available for other states' tax profiles.

In response to a question from Representative Fleming, Representative Meredith stated that there can be discussions, but the constitutional amendment is necessary to actually make a significant change for local governments.

Senator Mills announced that the last meeting of the interim would be November 22, 2021.

There being no further business, the meeting was adjourned at 12:00 p.m.