

TASK FORCE ON LOCAL GOVERNMENT ANNEXATION

Minutes of the 1st Meeting of the 2023 Interim

June 30, 2023

Call to Order and Roll Call

The 1st meeting of the Task Force on Local Government Annexation was held on Friday, June 30, 2023, at 1:00 PM, in Room 169 of the Capitol Annex. Representative Jonathan Dixon, Chair, called the meeting to order, and the secretary called the roll.

Present were:

Members: Senator Robby Mills, Co-Chair; Representative Jonathan Dixon, Co-Chair; Senators Michael J. Nemes, Robert Stivers, and Phillip Wheeler; Representatives Beverly Chester-Burton, Michael Meredith, and Michael Sarge Pollock.

Guests: Dawn Kelsey, Henderson City Attorney; Steve Gold, Henderson County Attorney; Jim Henderson, Shelley Hampton, and Rich Ornstein, Kentucky Association of Counties; Bryanna Carroll, Morgain Patterson, and Michele Hill, Kentucky League of Cities; and Mike Clark, University of Kentucky Gatton College of Business and Economics.

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

Representative Dixon stated that he wanted to reassure everyone that there are no predetermined outcomes when it comes to the task force, but there are a few goals that have been set: bring cities and counties together to discuss the important issue of annexation; allow members to gather information and get questions answered; and allow an unbiased approach to annexation so that cities and counties can work together for the progress of the people in Kentucky.

Discussion of Current Annexation Laws from the Prospective of Cities and Counties

Ms. Dawn Kelsey, Henderson City Attorney, told the members that the statutory requirements for proposed annexation are primarily found in KRS Chapter 81A.

The requirements for proposed annexation by a consolidated local government are somewhat different from other local governments and can be found in KRS 67C.111. Any proposed annexation by a city in that county shall first receive the approval of the legislative council of the consolidated local government prior to the city proceeding with

annexation. After July 15, 2024, a change in the law will allow a petition by 66 percent or more of the qualified voters, of the area proposed to be annexed, to allow annexation.

Generally, the territory proposed to be annexed must be adjacent or contiguous to the city limits. Kentucky courts have held that to meet the requirement the new area only needs to touch the boundary of the annexing city or could be annexed even if separated by some natural barrier such as a river or road. There is no requirement that the shape of an annexed territory be regular.

Corridor annexation is the annexation of “thin strips of land” such as highways, which is the only link between the territories. In general, these types of annexations are disfavored by courts, but they may be approved if there is a tangible “municipal purpose.” Municipal purpose cannot be just contiguity, but instead the corridor should serve a concrete and tangible municipal purpose existing at the time the annexation is sought. Ms. Kelsey discussed a recent Attorney General Opinion which found that the existence of watermains or other utility services along the corridor constituted a valid municipal purpose to support annexation.

If the corridor annexation is along a county road, then the road will become a city road, and the city will be responsible for its upkeep. Mr. Steven Gold, Henderson County Attorney, added that in some situations, cities will use corridor annexation along the shores of lakes or rivers, or along utility easements, and thus avoid annexing county roads, meaning the county would remain responsible for road maintenance. Ms. Kelsey stated that those types of annexations occurred rarely.

In continuation, Ms. Kelsey stated that the territory proposed to be annexed must be urban in character or suitable for urban development without unreasonable delay. Ms. Kelsey discussed a recent example in Henderson County where a farm parcel was consensually annexed by the City of Henderson and a papermill will soon open on that land that will provide a significant number of jobs. This example demonstrated that the property need not be urban at the time, but would be suitable for urban development. Ms. Kelsey stated that the criteria for determining suitability for urban development would include nearby population density, and the potential for commercial, industrial, institutional, or governmental use of the land.

Ms. Kelsey next discussed circumstances where a territory would not be suitable for annexation. The territory proposed to be annexed may not include lands that lie within the boundaries of another incorporated city. Additionally, any land within an agricultural district formed pursuant to KRS 262.850 (Agricultural District and Conservation Act) cannot be annexed. Generally, no part of the territory proposed to be annexed may lie in another county—a city located in one county may not annex territory in a different county—but a limited exception exists in KRS 81A.415 which provides an option for cities already located within two counties to annex territory located in a third county that contains

the city's utility infrastructure. The exception might apply to the City of Corbin which lies within two counties.

If the territory to be annexed meets the statutory requirements, then there are two pathways to annexation: consensual, which is the most common type of annexation—97 percent of all the annexation in the state for the last three years were consensual; and non-consensual, which is uncommon in Kentucky. Ms. Kelsey stated that in her 11-year tenure, and during the 21-year tenure of her predecessor, the City of Henderson had never undertaken a non-consensual annexation. The non-consensual annexation process requires more steps in order to protect the rights of property owners and residents in the area being annexed.

When conducting a consensual annexation, the city may immediately enact an ordinance annexing territory into the city if it obtains the written consent of each owner of real property within the territory proposed to be annexed. To conduct a consensual annexation, the consent must be in writing, and must be obtained from each property owner within the territory. Ms. Kelsey also stated that cities can also contract for consent to annexation when agreeing to provide municipal services in an area. Those contracts can bind future owners of the property, if they are properly recorded with the county clerk. Even where a city provides services to an area outside of its annexed territory, it may wait to annex that territory.

For a non-consensual annexation a city will begin with an “intent to annex” ordinance. The city must have a first reading of the ordinance; provide notice of a second reading of the ordinance to all real property owners within the territory proposed to be annexed within requisite statutory time limits, and conduct a second reading and passage of the ordinance. The city must also publish the “intent to annex” ordinance and publish notice of the right to petition to place the question of annexation on the ballot on two different occasions. If no objection or request for petition is received by the city within 60 days, the city may proceed with the non-consensual annexation via ordinance.

When a valid petition objecting to the annexation—signed by either 50 percent of resident voters within the proposed annexed territory, or 50 percent of the real property owners in the proposed annexed territory—has been received by the mayor, it is placed on the ballot for the next regular election by the county clerk. If 55 percent of those voting oppose annexation, then the annexation is defeated, and no portion of the proposed annexed property can be annexed for five years. Further, a city may not withdraw the proposal for annexation, in order to avoid having the issue placed on the ballot. If fewer than 55 percent of those voting oppose the annexation, then the city may move forward by passing an annexation ordinance.

For both consensual and non-consensual annexation the final steps for a city to annex the territory include: 1) sending notice of the annexation to the proper individuals

and entities; 2) delivering a copy of the annexation ordinance, map, and list of properties with name and address for each property owner to the county clerk within 60 days of the annexation; 3) sending the ordinance and a map prepared by the land surveyor to the Secretary of State's Office so that voter rolls can be updated; 4) sending a map with new boundaries to the Kentucky Revenue Cabinet; and 5) sending the map to all affected franchise taxpayers.

Ms. Kelsey next turned to some unusual types of annexations addressed in statute. First, industrial plants, which are not located in residential areas, may be non-consensually annexed pursuant to KRS 81A.510. The statute requires that the industrial plant being annexed to also be included in area that contains registered voters in numbers equal to or greater than 50 percent of the average number of employees of the industry in the preceding calendar year. This is a high standard and requires that when a non-consensual annexation of an industrial area occurs it must be of a significantly larger territory than just the plant itself.

KRS 81A.427 imposes additional notice requirements on a city annexing territory containing the utility infrastructure owned by another city. KRS 81A.490 provides that the rights of utilities in an area annexed by a city are expressly preserved. Annexations do not affect utility areas or the provision of utility services. Ms. Kelsey again discussed the paper mill in Henderson County, and explained that the electrical utility provider would not be changed due to the annexation of territory.

With regard to the temporary annexation procedures found in 2023 SB 141, beginning on March 1, 2023, cities will only be permitted to complete annexation that was started, but not completed, prior to March 29, 2023, and can only initiate new annexation if it meets the following criteria: 1) an opportunity for substantial economic development would be impeded if a parcel of land is not annexed; 2) an annexation of a parcel would directly facilitate the delivery of new or substantially improved city services that cannot be provided by the city in the absence of the annexation or the lack of annexation will result in the substantial loss of services; 3) if annexation was started on or after March 1, 2023, and a contract associated with the annexation led prior to March 29, 2023, would be voided by the provisions of SB 141; 4) the property owner has requested the annexation of property that is contiguous to the existing city boundary and the city provides written notice to the fiscal court at least 45 days prior to enacting the final ordinance annexing the property; 5) the fiscal court has concurred in the annexation; 6) the provision of SB 141 would void, alter, or otherwise impede the continuation of any provision of an interlocal agreement executed by the county and one or more cities within the county involving occupational license fees or insurance premium taxes; and 7) when annexation is required in order to maintain ongoing services provided by a city to a school, no city, prior to July 1, 2024, may initiate or complete an annexation of an area that includes any property owned by that school district unless requested by the school district and concurred with by the fiscal court of the county.

Standing to Challenge Annexations has been extended to permit those that are harmed to contest the legality of the annexation, including adjoining property owners to a territory proposed to be annexed where there are no residents within that territory. Further, SB 141 grants standing to counties opposed to an annexation within their territory from the date of enactment to July 1, 2024. Counties do not otherwise have a statutory right to challenge an annexation unless the county owns property within the territory. Mr. Gold noted that there are two different types of Standing to Challenge Annexations—standing to oppose the annexation when it is proposed and standing to challenge the annexation in court.

The city may wait to zone newly annexed territory using normal procedures provided in KRS Chapter 100 after the annexation is complete. But when a non-consensual annexation is proposed, the city may proceed to propose zoning of that territory between the passage of the “intent to annex” ordinance and the final annexation ordinance by following the procedure outlined in KRS 100.209.

After the annexation, the burden of taxation must be uniform throughout the city, which means the city must assume any liabilities attached to the annexed territory and the annexed territory must assume its fair share of the tax burden. City services, such as fire and EMT services, must be made available to residents in the newly annexed territory.

Mr. Gold explained that there are three main revenue options for cities and counties: 1) property taxes on real property, personal property, and motor vehicles; 2) occupational license taxes; and 3) insurance premium taxes. Occupational taxes and insurance premium taxes require crediting, meaning that if a city and county both levy those taxes, county revenue is decreased by the amount paid to a city, in order to avoid double taxation. Occupational license fee rates are capped at one percent for counties with populations of more than 30,000 by KRS 68.197.

Mr. Gold referred to several maps of Kentucky counties showing the imposition of different taxes by counties and cities. Occupational taxes are not uniform across the counties, and are subject to a variety of exceptions. Mr. Gold listed several counties that have been grandfathered in and do not have crediting requirements. Concerning insurance premium taxes, only three counties, pursuant to KRS 91A.080, are not required to credit those taxes when an insurance premium tax is levied by a city.

Other revenue options available to cities and counties include: bank franchise/local deposits; transient room tax; alcohol regulatory fees; 911 fees; and user fees for sanitation. These taxes do not represent a substantial source of revenue for local governments.

In response to a question from Senator Wheeler, Mr. Gold replied that occupational and insurance premium taxes are subject to separate crediting. If a county imposed an

insurance premium tax on a business that was then annexed into a city that levied an occupational tax, the business would be required to pay both in full.

In response to a series of questions from Senator Stivers, Mr. Gold stated that certain counties were not required to credit occupational taxes and thus those subject to the taxes within cities would have those taxes stacked. Mr. Gold described the occupational licensure taxation statutes as a morass due to the multitude of exemptions. In counties with a population less than 30,000, the county could impose an occupational license tax, and a city located within that county could impose its own occupational license tax, and those taxes would similarly not be subject to offsetting. Mr. Gold discussed the legislative history concerning the occupational licensure statutes. The statute was originally intended to grant an authority to those counties with a population of more than 30,000 to impose an occupational tax via referendum. In 1986, the referendum requirement was subsequently removed and the crediting requirement was added. Then in 1988, a court ruling held that counties with a population under 30,000 were permitted to impose occupational taxes pursuant to their home rule powers. Because of this unique history, those counties with populations of less than 30,000 were granted powers that the legislature had initially conceived of as only constituting a limited and restricted grant to larger counties, without any of the limitations or restrictions imposed on larger counties.

In response to another question from Senator Stivers, Ms. Kelsey stated that generally corridor annexations will be approved if the municipal purpose of annexing the territory is real at the time of the proposed annexation. The distance of the corridor is not a relevant factor, and usually the purpose relates to municipal services. The purpose may not be speculative. Ms. Kelsey discussed the benefits that those within the corridor may receive, and some benefits that the county may receive from her experience. Mr. Gold, stated that each county presents unique situations. Additionally, while courts indicate that they disfavor corridor annexations very few have been disallowed. Mr. Gold also raised a hypothetical example where the county engaged in bonding or other economic development in an area that was subsequently annexed which would lead to conflict, but in his experience with Ms. Kelsey, they were able to work out issues related to annexation on the front end.

In response to another question from Senator Stivers, Ms. Kelsey stated that an annexation would likely not be approved where there was no need for any municipal services or those services were adequately provided by some other entity.

In response to another question from Senator Wheeler, Ms. Kelsey stated that cities have the right to decide what lines will be drawn when annexing territory, and may avoid those parcels where they anticipate residents may object. The presenters again emphasized that the shape on an annexation do not matter.

Senator Mills commented that irregular shapes and holes in annexed territory causes problems with city services, as in his district, in knowing what is provided in the city and the county, and who is to respond in emergency situations. Ms. Kelsey replied that situation has improved due to GIS surveying and mapping. Mr. Gold stated that there are situations where gaps occur in provision of services even from house to house due to irregular annexations.

In response to Senator Wheeler's concern, Representative Meredith commented that he believed that when there are significant portions of agricultural land involved, it is not a direct consensual versus non-consensual discussion with the resident of the property, but the agricultural district can be created which then precludes the annexation. Ms. Kelsey said that Representative Meredith was correct and that agricultural and conservation districts are not subject to annexation. Mr. Gold noted that the creation of those districts can be burdensome.

Representative Dixon encouraged people that had related stories or issues, to let task force members know, and that the task force planned to include testimony from affected individuals and entities in future meetings. He pointed out that there was additional information in the members' folders relating to the role of counties in municipal annexation in nearby states.

Senator Mills commented that the task force would like to hear from other organizations at their July and August meetings. The task force has scheduled to hear from KACo in September and from KLC in October. Generally, members of the task force would like to know what is going on around the state related to the issue of annexation.

Representative Dixon announced that the next meeting of the Task Force would be July 21, 2023. There being no further business, the meeting was adjourned at 2:00 p.m.