

INTERIM JOINT COMMITTEE ON APPROPRIATIONS AND REVENUE

Minutes of the 1st Meeting of the 2018 Interim

June 28, 2018

Call to Order and Roll Call

The 1st meeting of the Interim Joint Committee on Appropriations and Revenue was held on Thursday, June 28, 2018, at 1:00 PM, in Room 154 of the Capitol Annex. Senator Christian McDaniel, Chair, called the meeting to order, and the secretary called the roll.

Present were:

Members: Senator Christian McDaniel, Co-Chair; Representative Steven Rudy, Co-Chair; Senators Ralph Alvarado, Danny Carroll, Rick Girdler, David P. Givens, Dennis Parrett, Wil Schroder, Robin L. Webb, and Stephen West; Representatives Tim Couch, Myron Dossett, Ken Fleming, David Hale, Regina Huff, Suzanne Miles, Jason Nemes, Ruth Ann Palumbo, Jody Richards, Sal Santoro, Arnold Simpson, Jim Stewart III, James Tipton, Russell Webber, Susan Westrom, and Jill York.

Guests: Greg Harkenrider, Deputy Executive Director, Governor's Office for Economic Analytics; Charles George, VP of Government Affairs, Kentucky Society of CPA's; Eric Scott, Tax Senior Manager, Ernst & Young; and Kevin Doyle, CFO, Congelton-Hacker Company

LRC Staff: Cynthia Brown, Katy Jenkins, Micah Johnson, and Jay Jacobs.

Introduction of New Appropriations and Revenue Committee Staff

Chairman McDaniel introduced Katy Jenkins, Legislative Committee Analyst, and Micha Johnson, Graduate Fellow, as new committee staff.

Update on Receipts

Greg Harkenrider, Deputy Executive Director, Governor's Office for Economic Analytics, gave a revenue update for fiscal year 2018. He reviewed revenue patterns, past forecasting accuracy, and receipts month to date, and discussed general fund and road fund predictions for June 2018.

In response to a question by Chairman McDaniel, Mr. Harkenrider stated that, according to HB 303, 50 percent of the excess revenues goes to the permanent pension fund, and 50 percent goes to the budget reserve trust fund.

In response to questions by Representative Fleming, Deputy Executive Director Harkenrider stated that his office will be taking a prospective position on implementation on the *Wayfair* decision by the Supreme Court. The hardest part about getting money will be getting new members to register. The executive branch is trying to inform people as fast as it can but there will be some challenges such as the diminimus standard of 200 transactions or \$100,000 in gross receipts.

In response to a question by Senator West, Mr. Harkenrider said that the threshold for someone doing business in Kentucky is \$100,000 of revenue or 200 transactions.

In response to questions by Senator Givens, Mr. Harkenrider stated that the fiscal year high was \$1,560,400,000 in 2014. The one stop portal is the best place for businesses to get questions answered and get registered.

In response to a question by Co-Chair Rudy, Mr. Harkenrider stated that he is holding off on revenue estimates for the *Wayfair* ruling until after more people have registered through open enrollment. The GAO estimate of over \$93,000,000 seemed overstated.

In response to a question by Senator Web, Mr. Harkenrider stated that sales tax staff are working overtime and are stretched to capacity working on implementation of the new sales taxes. One thing that helps is that Kentucky is an active streamline participant.

In response to a question by Representative Tipton, Mr. Harkenrider stated that the original budget reductions from the forecasted budget deficit from the consensus forecast group were fully implemented in Fiscal Year 2018.

In response to a follow up question by Representative Tipton, Deputy State Budget Director Kevin Cardwell stated that surplus revenues are split according to HB 303: 50 percent to the Budget Reserve Trust Fund, 25 percent to the Teachers Retirement, and 25 percent to the Kentucky Employees Retirement System. Mr. Harkenrider stated that there have been changes in tax collection for nonprofits. The biggest change affects admissions to events but not collecting taxes on fees for classes within the church; he will ask the Department of Revenue to clarify. The Department of Revenue's website provides some clarifications.

In response to a question by Senator West, Mr. Harkenrider stated that he does not know the thresholds for the streamline process but will verify with the Department of Revenue.

Limited Liability Entity Tax-Cost of Goods Sold Definition

Charles George, VP of Government Affairs, Kentucky Society of CPAs, discussed the Limited liability entity tax (LLET) that applies to all entities that offer limited liability to its owners.

Eric Scott, Tax Senior Manager, Ernst & Young gave a breakdown of how the tax is calculated with two alternative calculations of gross receipts or gross profits. He stated that 92 percent of the entities that file the LLET pay the minimum tax of \$175. He summarized how Cost of Goods sold is viewed and what can be deducted. He reviewed how the owner receives credit on his or her personal income tax.

Mr. George reviewed the projected fiscal year 2019 revenue considerations and options for increasing the tax and how it would impact the Commonwealth.

In response to questions by Chairman McDaniel, Mr. Scott stated that the real issue is what happens in the definitions as it relates to gross profit calculations over \$6,000,000. Mr. George stated, as relates to cost of goods sold, he recommends that the language of definitions mirror federal definitions. The bill that has been filed in the past struck through language and did not add new language to limit the cost of goods sold calculation.

In response to questions by Senator West, Mr. Scott stated the definition differs with the federal definition of cost of goods sold. The statutory language never changed, but the interpretation of the language changed. Kentucky is the only state that disallows certain costs based on this interpretation in the same way that the department of revenue has interpreted it. Mr. George stated that the best way to clear this up would be through a statutory change.

In response to questioned by Representative Fleming, Mr. Scott stated that about 15,000 companies pay one or the other calculations, which equates to eight percent of the 170. The CPA is the compliance cost for companies to stay in compliance. He does not have access to these compliance numbers. Mr. George stated that the level of complexity is high and difficult to quantify.

In response to questions by Senator Givens, Mr. Scott stated that, if the state simplified the process, compliance costs would decrease. There was no statutory change to language in 2013 for LETT; it was created in 2007, replacing the unpopular business license tax.

Correspondence Received

Senator McDaniel reviewed correspondence received since the last meeting.

List of Reports Received Since November, 2017

Senator McDaniel reviewed reports received since the last meeting.

With no further business, the meeting was adjourned.