

**COMMONWEALTH OF KENTUCKY STATE FISCAL NOTE STATEMENT
LEGISLATIVE RESEARCH COMMISSION
2015 REGULAR SESSION**

MEASURE

2015 BR NUMBER **0298**

HOUSE BILL NUMBER **130**

RESOLUTION NUMBER _____

AMENDMENT NUMBER _____

SUBJECT/TITLE **An ACT relating to the property tax on unmined coal.**

SPONSOR **Representative Short**

NOTE SUMMARY

FISCAL ANALYSIS: IMPACT NO IMPACT INDETERMINABLE IMPACT

LEVEL(S) OF IMPACT: STATE LOCAL FEDERAL

BUDGET UNIT(S) IMPACT: **Energy & Environment Cabinet - KY Heritage Land Conservation Fund and Department for Energy Development and Independence**

FUND(S) IMPACT: GENERAL ROAD FEDERAL RESTRICTED AGENCY _____ OTHER

FISCAL SUMMARY

FISCAL ESTIMATES	2014-2015	2015-2016	ANNUAL IMPACT AT FULL IMPLEMENTATION
REVENUES		(<\$1 million)	(<\$1 million) in FY 2015-2016
EXPENDITURES		Minimal	Minimal in FY 2015-2016
NET EFFECT		(<\$1 million)	(<\$1 million) in FY 2015-2016

() indicates a decrease/negative

MEASURE’S PURPOSE: HB 130 would reduce the state and local property tax burden on some unmined coal reserves by amending the way in which the fair cash (taxable) value of certain reserves is assessed by the Department of Revenue. The bill also includes a taxpayer education component, by requiring the department to prepare an informational brochure on the procedure to follow to appeal an assessment of unmined coal and other energy resources.

PROVISIONS/MECHANICS: The bill amends KRS 132.820 to establish a “standard value” of zero (\$0) for unmined coal reserves that have not had any amount of coal severed during the 10-year period immediately preceding the Jan. 1 assessment date, effective for reserves assessed on and after Jan. 1, 2015. The constitutional mandate of assessment at a property’s “fair cash value” would still apply to these reserves, so the bill provides that the department may deviate from the defined standard value if information became available that warranted that action.

Pursuant to the ruling of the Kentucky Supreme Court in *Gillis v. Yount*, 748 S.W.2d 357 (Ky. 1988), unmined coal is a form of real property, and as such the constitution requires that it be assessed for state and local property tax at its fair cash value (in place), estimated at the price it would bring at a fair voluntary sale. The valuation method currently used by the department to centrally assess the fair cash value of all unmined coal in the state was developed as a result of a settlement reached in 2005, and approved by order of the Franklin Circuit Court, in the *Kentuckians for the Commonwealth v. Blanton* case, No. 88-CI-0407.

The method takes into account numerous factors impacting the market for unmined coal, using an income-based approach that seeks to estimate and assign a present value to the future income to be derived from the ownership of the property, which is complicated due to the volatile nature of the market for coal. One of the many factors is whether the reserve is actively being mined, or is idle. Idle reserves are either not being mined currently, or are not projected to be mined for some time. If a coal reserve is classified as idle, its present assessed value is reduced because it will not be worth as much in a fair voluntary sale in today's market due to the distant and/or uncertain time period before it will likely be mined to generate income for its owner.

Related to the concept of an idle reserve's possible *future* mining income, HB 130 would require the department to take into account the mining activity in a given reserve over the *immediate past* 10 years. If no coal has been mined from a reserve in that time period, that is, if the reserve has been idle for 10 full years prior to the assessment date, the "standard value" will be zero (\$0), unless some other information is available that warrants a deviation from that value.

The bill would also amend KRS 132.820 to require the department to prepare, through administrative regulation, an informational brochure explaining the basis of the property tax on unmined coal and energy resources, the valuation procedures used to assess these various types of property, and the procedure for taxpayers to follow to appeal assessments. The brochure would be mailed to each taxpayer, along with each annual notice of tax assessment.

FISCAL EXPLANATION: HB 130 would impact state revenues, local revenues, and school funding provided through the SEEK formula. These impacts will be discussed separately.

State Impact

The bill would have a negative impact on state property tax revenues. While the precise degree of impact is difficult to estimate, it is expected to be less than \$1 million annually, beginning in FY 2015-2016. The impact will not be borne by the general fund. By statute, the first \$400,000 in state revenues from the state property tax on unmined coal is reserved for use by the Energy & Environment Cabinet (EEC) for public education of coal-related issues. All remaining revenues are deposited into the Kentucky Heritage Land Conservation Fund administered by the EEC for the purchase and management of natural areas and wetlands by various state agencies and private entities.

Because the assessments of unmined coal do not impact the annual calculation of the state real property tax rate, any decrease in assessed value of this property would result in a reduction in receipts to these two programs. The total current assessment of reserves that have been idle for a full 10-year period is not readily available; however the total assessment of all idle reserves can

serve as a relatively good indicator of the scale of impact. The assessed value of all currently idle reserves is approximately \$100 million, which at the current state rate of 12.2 cents per \$100 assessed value generates approximately \$122,000 in state receipts. As a result, the state impact of this bill will likely be less than \$1 million annually, even in future years assuming coal production continues its current downward trend and more reserves become idle.

Additionally, the new assessment procedures and brochure mailing requirements would present new administrative burdens and costs on the Department of Revenue.

Local impact

At the local level, unmined coal assessments are figured into the annual computation of property tax rates (performed as a result of “House Bill 44.”) Local taxing jurisdictions are allowed to impose a compensating tax rate on real property, which is the rate that will generate approximately the same amount of revenue as was collected in the prior year. The effect of this rate calculation is that if the total assessment of taxable property within a jurisdiction is reduced (which would occur by virtue of this bill in the 43 counties having unmined coal property), a local taxing jurisdiction may impose a higher compensating tax rate which would be applied to all taxable property. Therefore, **a locality could possibly mitigate a reduction in revenues by levying the compensating tax rate, effectively shifting the tax burden to other properties.**

Local school funding and the SEEK formula

Local school districts are funded with a mix of state and local tax dollars, in amounts determined by the SEEK funding formula and based in large part upon the assessed value of taxable property in each district. **If a district’s local assessment base is reduced, as would occur in some districts due to HB 130, it is considered less wealthy and the amount of required local tax effort is reduced. The amount of state SEEK funding provided to that district would also likely change. The change in state funding would differ among districts, due to the many other factors in the formula.**

Collectively, the school districts receiving revenues from unmined coal property already tend to be less wealthy than the state average because their per-pupil assessment is substantially lower than the state per-pupil average. As a result, these districts, as a group, already have a larger share of their funding provided by the state than the other districts do. HB 103 would reduce the assessed value of some coal reserves and therefore further reduce the already below average per-pupil assessment base in these counties. This could result in an even greater share of their funding coming from state SEEK dollars, which would have an impact on the state general fund.

DATA SOURCE(S): DOR; APA audit reports; *Taxation of Unmined Coal in Kentucky*, J. Parrish, 4 Ky. J. Equine, Agric. & Nat. Resources L. 231; LRC staff

PREPARER: Eric Kennedy NOTE NUMBER: 3 REVIEW: GMR DATE: 2/3/2015