COMMONWEALTH OF KENTUCKY STATE FISCAL NOTE STATEMENT
LEGISLATIVE RESEARCH COMMISSION
2018 REGULAR SESSION

MEASURE

2018 BR NUMBER **0892** **HOUSE** BILL NUMBER **162**

RESOLUTION NUMBER_____ AMENDMENT NUMBER _____

SUBJECT/TITLE An ACT relating to tax-exempt property of purely public charities and declaring an emergency.

SPONSOR Representative DeCesare

NOTE SUMMARY

FISCAL ANALYSIS: ☒ IMPACT ☐ NO IMPACT ☐ INDETERMINABLE IMPACT

LEVEL(S) OF IMPACT: ☒ STATE ☒ LOCAL ☐ FEDERAL

BUDGET UNIT(S) IMPACT: _____

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

FISCAL SUMMARY

FISCAL ESTIMATES	2017-2018	2018-2019	2019-2020	ANNUAL IMPACT AT FULL IMPLEMENTATION
REVENUES	(Indeterminable)	(Indeterminable)	(Indeterminable)	(Indeterminable)
EXPENDITURES	Minimal	Minimal	Minimal	Minimal
NET EFFECT	(Indeterminable)	(Indeterminable)	(Indeterminable)	(Indeterminable)

( ) indicates a decrease/negative

MEASURE'S PURPOSE: The purpose of this measure is to provide an exemption from state and local property tax for property which is owned by a purely public charity and has been leased or possession otherwise transferred to a natural person, association, partnership, or corporation in connection with a business conducted for profit. The exemption only applies when the property and the income derived from it is used to further the mission of the charity.

PROVISIONS/MECHANICS: Section 1: Amends KRS 132.195(2) to add property of purely public charities to the list of leasehold interests exempt from state and local property tax, when the property and the income derived from it is used to further the charity's mission.

Section 2: Adds a retroactive clause to allow the exemption to apply to all outstanding refund claims with taxable years ending prior to the effective date of the Act and to all claims for those taxable years pending in any judicial or administrative forum.

Section 3: Adds an emergency clause to have the Act take effect upon its passage and approval by the Governor or upon its otherwise becoming law.

<u>FISCAL EXPLANATION</u>: Section 170 of the Kentucky Constitution exempts property owned by institutions of a purely public charity from taxation. However, in accordance with KRS 132.195(1), the leasehold interest of that tax-exempt property can be taxed when the interest is transferred to a taxable entity. While KRS 132.195(2) provides a list of properties exempt from tax on the leasehold interest, purely public charities are not included in that list. HB 162 creates a new tax exemption by adding purely public charities to the list of properties exempt from tax on leasehold interests.

<u>State Impact</u>

The exemption created by HB 162 applies to both tangible and real property. The state tax rate for tangible property varies from one-tenth of a cent per one-hundred dollars of valuation to 45 cents per one-hundred dollars of valuation. The state tax rate for real property is currently 12.2 cents per one-hundred dollars of valuation. Since the tax dollars collected by the taxation of leasehold interests owned by purely public charities are not tracked, the exact tax implication of HB 162 is unknown.

In general, unless offset with economic growth or a stream of revenue from another source, a newly created tax exemption results in a negative impact to the General Fund. Since it is unknown how many purely public charities lease or transfer possession of their property to taxable entities, it is unclear how much of an impact HB 162 will have on the General Fund.

HB 162 is expected to have a minimal impact on state expenditures as a verification method will need to be developed and administered to confirm that the charity's income and property is used to further the charity's mission.

<u>Local Impact</u>

At the local level, property tax 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, 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. The unintentional consequence of shifting the tax burden may result in an increase in tax collection issues, especially in counties that already have a struggling economy. An increase in unpaid tax bills will result in decreased revenues for local taxing districts.

HB 162 is expected to have a minimal impact on local expenditures as a verification method will need to be developed and administered to confirm that the charity's income and property is used to further the charity's mission.

<u>Local School Funding and the SEEK Formula</u>

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 total assessed value of taxable property in each district. If a district's local assessment base is reduced, which may result when taxable property becomes exempt, 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.

Retroactive Clause
This bill has a retroactive clause that allows all claims for those taxable years pending in any judicial or administrative forum to qualify for the exemption. Currently, there is pending litigation pertaining to this matter. *The Grand Lodge of Kentucky Free and Accepted Masons, et al. v. City Taylor Mill et al.*, No. 2015-CA-001617-MR (Ky. App. Feb. 10, 2017).

Emergency Clause
HB 162 has an emergency clause. If enacted, the fiscal impact of the bill will take effect upon its passage and approval by the Governor or upon it otherwise becoming law.

DATA SOURCE(S): **LRC A&R Committee; LRC Economists; Department of Revenue;**
PREPARER: **Cynthia R. Brown** **NOTE NUMBER**: **40** **REVIEW**: **JAB** **DATE**: **1/25/2018**