

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

MEASURE

2018 BR NUMBER **0361**

SENATE BILL NUMBER **40**

RESOLUTION NUMBER _____

AMENDMENT NUMBER _____

SUBJECT/TITLE **An ACT proposing an amendment to Section 170 of the Constitution of Kentucky relating to property exempt from taxation.**

SPONSOR **Senator Kerr**

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			(\$1,200,000) GF (\$12,000,000) Local	(\$1,200,000) GF (\$12,000,000) Local
EXPENDITURES			Minimal	Minimal
NET EFFECT			(\$1,200,000) GF (\$12,000,000) Local	(\$1,200,000) GF (\$12,000,000) Local

() indicates a decrease/negative

MEASURE'S PURPOSE: The purpose of this measure is to provide a state and local property tax exemption for property maintained as the primary residence of an owner who has a permanent and total one hundred percent service-connected disability rating from the United States Department of Veterans Affairs and to allow that exemption to transfer to the surviving spouse upon the death of the veteran and remain with the property until the surviving spouse passes away, relocates, or remarries.

PROVISIONS/MECHANICS: Section 1 of the bill proposes an amendment to Section 170 of the Kentucky Constitution to increase the homestead exemption to exempt from state and local property taxes real property maintained as a permanent residence of the owner, when the owner has a permanent and total one hundred percent service-connected disability rating from the United States Department of Veterans Affairs. It also has a provision to allow the tax exemption to transfer

to the surviving spouse upon the death of the veteran and remain with the property until the surviving spouse passes away, relocates, or remarries.

For all other homeowners, who qualify for the homestead exemption, this bill proposes that the homestead exemption be indexed every two years. In 1974, KRS 132.810 was amended to state that the \$6,500 homestead exemption amount shall reflect the purchasing power of the dollar in 1972 and allow for a two-year adjustment of the exemption amount based on the United States Department of Labor cost of living index. As a result, the exemption amount has gradually increased from \$6,500 in 1974 to \$37,600 in 2018. The exemption is expected to continue to increase in future years. Section one of the bill incorporates the two-year statutory index adjustment into Section 170 of the Kentucky Constitution.

Section 2 of the bill proposes that the following question be submitted to the voters: "Are you in favor of amending the Constitution of Kentucky to exempt from ad valorem property taxes real property owned by and maintained as the permanent residence of a veteran with a permanent and total 100% disability rating by the United States Department of Veterans Affairs due to his or her service in the United States Armed Forces and to allow, upon the death of the veteran, the exemption to remain with the property until the death, relocation, or remarriage of the surviving spouse?"

FISCAL EXPLANATION: If the bill is enacted, the increase in the homestead exemption would eliminate qualifying veterans from paying real property tax on their residence. The exemption would also transfer to the veteran's surviving spouse, which extends it beyond the veteran's life span. This bill will not affect the tax revenues payable by other homeowners that qualify for the homestead exemption, since KRS 132.810 already incorporates the index adjustment and it has been applied since 1974.

State Tax Revenues and Expenditures

The average assessment value of a home owned by a disabled veteran in Kentucky is \$141,793. If you remove the already approved homestead exemption of \$37,600, the additional exemption granted by this bill is estimated at \$104,193. The US Department of Veterans Affairs reports that 9,120 veterans that are 100% disabled reside in Kentucky. Assuming each 100% disabled veteran owns a home, the total additional exemption is estimated at \$950,240,000. The state real property tax rate for 2018 is 12.2 cents per one hundred dollars of assessed value. Using this tax rate, the expected impact of SB 40 to the General Fund is approximately a negative \$1,200,000. This total may vary each year as tax rates, property values, and the number of qualifying veterans will fluctuate. Also, this total does not take into account the change in taxpayer behavior that may occur to take advantage of the exemption.

No additional expenditures are expected for the state in order to implement SB 40.

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 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.

Local Tax Revenues and Expenditures

The impact this Constitutional amendment may have on local property tax revenues received by counties, cities, school districts, and other local special districts with taxing authority would depend on the tax rate levied by the given locality. Most local taxing jurisdictions undertake an annual rate setting process through which the governing body chooses a tax rate to impose for that year, which may or may not be subject to various public hearing and voter recall provisions based on the rate imposed for the prior year. Unlike the state, local taxing jurisdictions generally have the ability to offset a reduction in revenues that may occur as a result of reductions in the total assessment base, by imposing an increased tax rate on all property remaining subject to the tax through this annual process.

Specifically, most local taxing jurisdictions would have the statutory authority to impose a “compensating tax rate”, which would be the rate estimated to produce an amount of revenue in the current year approximately equal to the amount produced in the preceding year. If a jurisdiction chooses to impose this rate, it would not be subject to voter recall. The practical effect would be a tax burden shift from the newly exempted property to all other property remaining subject to tax at the increased rate. The shifting of the tax burden, in general, is meant to prevent a reduction in tax revenues from occurring. However, the unintentional consequence can be an increase in collection issues, especially in counties that already have a struggling economy. The increase of collection issues will result in decreased tax revenues for the local taxing districts.

Jefferson, Hardin, Fayette, Boone, and Christian counties have the highest number of resident disabled veterans. The taxing districts within these counties are impacted more due to the increased number of disabled veterans residing in larger city populations or near the military bases, Fort Knox and Fort Campbell. Therefore, these areas could experience more tax revenue loss and thus, may impose a higher tax rate to compensate. On the flip side, counties like Estill, Owsley, and Robertson, which have no disabled veterans, would not be impacted by this amendment.

Using the average local property tax rate, the estimated total impact on local revenues would be a negative \$12,000,000. This total may vary each year as tax rates, property values, and the number of qualifying veterans will fluctuate. Also, this total does not take into account a change in taxpayer behavior to take advantage of the exemption. Each impacted locality may elect the compensating tax rate in order to try and recoup any lost tax revenues.

Ballot Costs

Section 256 of the Kentucky Constitution specifies that constitutional amendments are only added to the ballot for the general election in even-numbered years (“next general election for members of the House of Representatives”). Therefore the constitutional amendment would be submitted to the voters in November, 2018.

According to Harp Enterprises, a vendor that provides electronic voting machines to 97 Kentucky counties, there are additional programming costs associated with adding a new category to the ballot on an already scheduled statewide election. For example, the cost to add a new category to

the ballot for Lexington-Fayette Urban County Government, with 291 precincts, is estimated to be between \$3,000 and \$4,000, and for Franklin County, with 44 precincts, the cost is estimated to be between \$1,250 and \$2,000.

The additional expenditures of SB 40 to local governments due to adding a constitutional amendment to a ballot would be minimal.

DATA SOURCE(S): LRC Economist and Staff, U.S. Census Bureau, American Community Survey, Public Use Micro-data Sample, U.S. Department of Veterans Affairs, National Center for Veterans Analysis and Statistics, Kentucky Department of Revenue; Harp Enterprises
PREPARER: Cynthia R. Brown NOTE NUMBER: 66 REVIEW: JAB DATE: 1/26/2018