

House Bill 142 – Comprehensive Tax Reform

2013 General Assembly

Bill Summary

HB 142 offered by Rep. Wayne builds on the work of the governor's Blue Ribbon Commission on Tax Reform (BRC). It includes many of the recommendations of the commission, but gives greater emphasis to the principles of fairness and adequacy, and generates more new revenue – about \$800 million in all. The major provisions of HB 142 are summarized below.

Individual Income Tax

- Limit itemized deductions to \$17,500 and adjust that amount annually by the consumer price index. (*currently there is no limit on itemized deductions*)
- Lower the exclusion for retirement income to \$35,000 and phase out the exclusion by one dollar by every dollar that adjusted gross income exceeds \$35,000 (*the current exclusion is \$41,110 with no phase out; Social Security income is exempt from state income tax.*)
- Create a refundable earned income tax credit set at 15% of the federal credit.
- Update the Internal Revenue Code reference date to December 31, 2012.
- Change the income tax brackets and rates as follows:

Adjusted Gross Income	Current	New
\$0-\$3,000	2%	2%
\$3,001-\$4,000	3%	3%
\$4,001-\$5,000	4%	3.5%
\$5,001-\$8,000	5%	4.5%
\$8,001-\$75,000	5.8%	5.5%
\$75,001-\$150,000	6%	6%
\$150,000 and over		6.5%

Sales and Excise Taxes

- Broaden the sales tax to include the following services:
 - Golf course greens fees; membership fees in private golf clubs and private country clubs;
 - Janitorial services, including carpet, upholstery, and window cleaning;
 - Garment alteration and repair services;
 - Non-coin operated laundry and dry-cleaning services;
 - Armored car services;
 - Security services;
 - Exterminating and pest-control services;
 - Landscaping services, excluding lawn-care services;
 - Non-coin operated automotive washing and waxing services;
 - Commercial linen services, excluding uniform services and linen services to hospitals and nursing homes; and
 - Limousine services, if a driver is included.
- Raise the cigarette tax to \$1.60/pack and raise the tax on other tobacco products commensurate to the cigarette tax increase.
- Repeal the distilled spirits case sales tax and restore the cigarette rolling papers tax.
- Apply the sales tax to pre-written computer software available for access without a download.
- Apply sales tax and transient room taxes to the entire hotel accommodation price.

The BRC recommended a 1% state utilities tax on residences and business, and exempting horse feed and products from the sales tax. Neither is included in HB 142.

Corporate Taxes

- Lower the threshold for the limited liability entity gross receipts or gross profits tax from \$3 million to \$1 million and phase in the tax to \$2 million (as opposed to phasing it in to \$6 million).
- Add a throwback rule to tax nowhere income.
- Fully decouple from the deduction for U.S. production activities (QPAI).
- Mandate combined reporting for the corporate income tax.
- Make the film industry tax credit nonrefundable and nontransferable.

Discussion: Since Kentucky already has competitive business taxes (rated 4th best among the surrounding 13 states according to BRC consultants), HB 142 takes an approach of closing loopholes that allow businesses to not report some income or that provide preferential tax treatment without a proven benefit. The BRC recommended closing some of these loopholes but actually created several more that would result in a loss of more than \$130 million in revenue from corporate taxes.

Property Taxes

- Freeze the state real property tax rate at 12.2 cents per \$100 in value (*its current rate*)
- Clarify the identification of public service companies for taxation (to include newly developing utility industries).
- Require reporting the rental space for documented watercraft/private airplanes.

Severance Taxes

- Eliminate the export credit under the minerals severance tax.
- Clarify the definition of “gross value” under the severance tax to remove the reference to section 613c of the Internal Revenue Code.

Other Taxes

- Create a review process for all tax incentive programs and require that each program have a sunset date every five years or be reauthorized
- Levy a pari-mutuel tax on advance deposit wagers made on live races at Kentucky race tracks.
- Reinstate the Kentucky estate tax by decoupling from the federal estate tax and re-establishing it to reflect federal law in effect on January 1, 2003 (*in other words, HB 142 takes us back to the policy we had before Congress took this revenue away*)
- Remove the HB 44 recall provisions for local and school real property taxes.

Simplicity, Compliance and Tax Administration (*mostly changes requested by the Dept. of Revenue*)

- Allow non-renewal of professional licenses, driver’s licenses and vehicle registration if taxpayers have exhausted all appeals and still refuse to pay state taxes to improve collections.
- Amend tobacco tax laws to provide clarifications and administrative improvements enabling the Department of Revenue to better enforce Kentucky’s tobacco tax laws.
- Clarify the definition of “pollution control facilities” under tangible personal property tax statutes (clearly state that real property is subject to state and local property tax rates).
- Define “broadcast” and “telephonic equipment” in the tangible personal property tax statutes.
- Clarify installment payment agreement provisions.
- Repeal the Rural Electric Cooperative Corp. and Rural Telephone Cooperative Corp. Tax.
- Under tangible personal property tax statutes, clarify that inventory-in-transit must be delivered to a permanent out-of-state destination in order to qualify for the under 6 month exclusion.
- Update use tax notification and compliance requirements for remote vendors.
- Add clarifying language in KRS 139.480(11) regarding farm machinery that specifies combine header trailers are exempt from sales tax.
- Repeal the school tax rate exclusion from sales tax calculation on “residential telecommunications service” found in KRS 139.470(9).

Road Fund (*this is separate from everything above, all of which affect the General Fund*)

- Raise the floor of the average wholesale price for fuels tax (freezing the minimum at the current fiscal year rate of \$2.616/gallon).
- Reduce dealer’s compensation on motor fuels tax from 2.25% to 1%.