Local Option Sales Tax
Testimony to
Interim Joint Committee on Local Government

September 25, 2013
Importance of Kentucky local government
Local governments have challenges generating the revenue they need

• Constitutional & statutory limits
  – Property tax limits
  – Limits on types of taxes they can levy
  – Limit on general revenue sharing

• Other issues
  – Role of business tax incentives
  – Lack of a commercial & business base needed to make occupational & sales taxes viable
  – Loss of taxes due to industry declines
Kentucky’s property taxes are low

- $21 in state & local property tax revenue per $1,000 in state personal income (2009-2010)
- 42% lower than US average of $36
- Ranks Kentucky 45th among states

Source: Computed from Census Bureau Census of Governments
Real Property Tax Rates in Louisville/Jefferson County Have Fallen Dramatically

35% decline in Louisville and 42% decline in Jefferson County since 1978.
Business Tax Incentives Another Challenge

• Abatement of 1% occupational tax part of many tax incentives
• Growth of tax increment financing
• Cities can exempt occupational & property taxes of new manufacturing facilities for up to 5 years

126 large companies in Jefferson County have received final approval for tax incentives according to state database
Sales Tax is a Regressive Tax

Who Pays Sales Taxes Vs. Who Pays Income Taxes in Kentucky

Source: Institute on Taxation and Economic Policy
Who Pays?

Kentucky State & Local Taxes
Shares of family income for non-elderly taxpayers

Source: Institute on Taxation and Economic Policy
Other Challenges with Local Option Sales Taxes

- Not deductible against federal taxes like occupational tax & property tax
- Limited growth of sales tax revenue because not modernized
- Loss of state sales tax revenue because of border & consumption effects
- Not a solution for localities without a sufficient commercial base
- Problem with earmarking for specific projects
Sales Tax Base is Eroding

Sales Tax Revenue as Percent of State Personal Income

Source: KCEP analysis of OSBD, BEA data
Context Needed for Local Option Sales Tax

• Need for a comprehensive tax reform package that includes sales tax modernization & refundable EITC to address fairness

• Can’t be a tax swap or include a tax offset—that would simply shift responsibility
Considerations for local taxation

- Broad view of the issue of local taxation should be taken
- Tax fairness and revenue sustainability must be part of the conversation
- Need to address decline in the property tax
  - Recall provisions
  - Create a circuit breaker & amend homestead exemption
- Greater scrutiny & disclosure of tax breaks