

Kentucky Tax Talk: What Governor Candidates Would Change

By **Mark Sommer and Daniel Mudd** (October 18, 2019, 11:53 AM EDT)

Last year was the year of significant tax reform in Kentucky and 2019 is the year of clean-up (with the second round of major tax changes snuck in at the end).

Given this, many wonder how gubernatorial candidates Andy Beshear, a Democrat, and incumbent Gov. Matt Bevin, a Republican, propose to produce tax revenue over the next four years.

Will Bevin continue to bless further pro-business tax legislation, including an additional lowering of the corporate income tax rate down from 5% (previously 6%) to 4%, or even lower? Will Beshear attempt to overhaul changes previously made under the Bevin regime? Will both create new ways to produce tax revenue? This article seeks to provide insight on the two candidates' public stances on tax reform.

As a refresher, during Bevin's first term, the General Assembly made several changes to the state's tax code during the 2018 regular session through the passing of H.B. 366 and H.B. 487.

Some of these changes included expanding the sales tax to several services; enacting remote seller provisions to tax certain online sales ahead of the South Dakota v. Wayfair Inc.[1] decision later that year; reducing both corporate and individual income tax rates to a flat 5%; updating Kentucky's corporate tax structure through the adoption of single-sales factor apportionment, market sourcing and mandatory combines (unitary) reporting; creating an income tax credit to offset Kentucky's property tax on inventory; and bulking up several pro-taxpayer rights provisions.

Any 2019 tax legislation was intended to involve less drastic revisions to Kentucky's tax code and focus more on cleaning up any unintended consequences of the 2018 tax reform (e.g., sales tax on nonprofit activities, clarifications to the new unitary reporting structure, etc.).

Nevertheless, several substantial changes were still made through the General Assembly's passage of two more bills, H.B. 458 and H.B. 354. Some of these changes included exempting event admissions and fundraising sales for most nonprofit organizations from the expanded sales tax, adding a minimum threshold before certain services are subject to Kentucky's sales tax, and adding back the itemized income tax deduction for investment interest and gambling losses.

Additionally, several pro-business changes were made in 2019 including clarification for which corporations are considered a combined group, excluding countries with tax treaties from the "tax haven" provisions, shortening the election period if a corporate taxpayer elects to file consolidated returns, and creation of a new deferred tax deduction for publicly traded companies.



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Other industries such as banking and manufacturing benefitted from changes made in 2019, and taxpayer transparency was restored via H.B. 458 after taxpayer rights were threatened by other legislation prohibiting the Department of Revenue from releasing tax guidance via an open records request.

While the Kentucky General Assembly and Bevin have not always seen eye-to-eye on the tax changes made in 2018 and 2019, overall, Bevin signed a tax cut into law that lowered individual and corporate tax rates by 17% during his term, which is expected to reduce the \$11 billion general fund annually by \$100 million, and was supportive of several pro-business tax changes which were ultimately passed by the General Assembly in some form or fashion during his tenure.

While in office, Bevin's repeated mantra for tax reform has been to lower income taxes and focus on taxing consumption by expanding sales taxes, along with a major focus on Kentucky's massive unfunded pension liabilities, arguably the highest in the nation when he took office. Despite some new wrinkles, this focus does not appear to be changing based on his recent comments.

Looking toward 2020, Bevin again recently promised to propose a comprehensive tax overhaul. In his first term, Bevin discussed a comprehensive tax plan, but never made a formal announcement.[2] This time around, Bevin claims his plan for comprehensive tax reform will make changes in a variety of fields.

Rather than focusing on one area of reform, he believes in order to make impactful tax change, there must be reform in many different areas. These areas include income taxes, gas tax, death taxes, retirement taxes and local option sales taxes.[3] Ultimately, Bevin states his plan is to create tax revenue by increasing job creation, but he has not provided specific goals for these fields of tax reform.[4]

Most recently, while at a veterans' coalition campaign event, Bevin proposed new wrinkles such as exempting veteran's retirement income from state taxation.[5] He argued the benefit received by the state from this income is minute in comparison to the sacrifice provided by local veterans.[6] It is estimated that Kentucky receives a few million dollars yearly from roughly 27,000 retired military incomes in the state.[7]

In contrast, rather than promising a general tax overhaul, Beshear has focused on specific areas he wishes to see Kentucky create tax revenue.

Beshear's primary focus is to raise tax revenue by expanding gambling in Kentucky. He wants to legalize casinos, sports betting and online poker in order to create new tax revenue.[8] While campaigning, Beshear stated he plans to direct 100% of tax revenue received from gambling directed toward funding pensions.[9]

His argument is that Kentucky is losing revenue opportunities when its citizens visit neighboring states such as Indiana, Illinois and Ohio, each of which allow these activities. He estimates the change would generate approximately \$500 million in new sustainable annual revenue.[10] According to Beshear's campaign, as of 2017, the 24 states that allow commercial gaming raised over \$9 billion in tax revenue collectively.[11]

Instead, Kentucky currently prohibits stand-alone casinos and sports betting, but allows for horse race betting and the Kentucky Lottery program, as well as what is known as "historical horse racing" in the form of pari-mutuel tax wagering at multiple horse tracks

and stand-alone facilities throughout the commonwealth (an activity which is still not 100% sanctioned in Kentucky as the issue is on review before the Kentucky Supreme Court for the second time).[12]

Beshear's website claims if gambling laws are expanded in Kentucky, his administration will work with nonprofit organizations dedicated to assist gambling addiction.

Many, including Gov. Bevin, are not in favor of this form of tax revenue because of the negative societal effects of gambling and that it may not even put a dent in Kentucky's unfunded pension liability, or add much to the general fund.

During a recent debate between the two candidates, Bevin expressed his lack of support for expanding commercial gambling in Kentucky because he believes he will be able to fully fund pensions during a second term without resorting to this form of revenue generating. Bevin has also expressed his opposition to the use of gaming to raise tax revenue by calling the practice a "sucker's bet." [13]

Another tax objective proposed by Beshear is to eliminate certain tax incentives for the wealthy such as eliminating tax loopholes on private jets and yachts. His stated ultimate objective is to change the law in order to keep giving tax incentives to companies providing "jobs that pay a living wage." [14] He has not, however, provided a plan for how he is going to achieve that up to this point.

Both candidates have expressed support for legalizing medical marijuana but disagree on using it to generate tax revenue. While Beshear states medical marijuana should be taxed, Bevin believes it should be exempt along with other prescriptions. [15]

While tax reform has always been an important discussion point during gubernatorial campaigns, because of the pension crisis in the commonwealth, the candidates' plans to raise revenue to fund the state's pension program is of the utmost importance to many voters.

Whether it is Bevin's promise for a comprehensive tax plan to continue the pro-business and pro-taxpayer changes made under his helm in 2018 and 2019, or Beshear's focus on legalizing gaming, both candidates have given the public a plethora of promises in the area of tax reform.

This has left much of the commonwealth wondering if either candidate will be able to bring these promises to fruition, and what the right answer is from a tax and public policy perspective. Only time will tell who wins the race in November, but there is no question that additional tax changes are on the horizon in the commonwealth.

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[1] South Dakota v. Wayfair, Inc., 585 U.S. ___, 138 S.Ct. 2080, 2094, 201 L.Ed.2d 403, 86

USLW 4452 (2018).

[2] Tom Loftus, Casinos or taxes? Can Andy Beshear or Matt Bevin deliver on budget promises?, Louisville Courier Journal (Sept. 27, 2019).

[3] Joe Sonka, Matt Bevin says he will propose comprehensive tax reform that caters to veterans, Louisville Courier Journal (Oct.1, 2019).

[4] Id.

[5] Id.

[6] Id.

[7] Jack Brammer, Bevin again promises 'comprehensive' tax reform as he pushes tax break for veterans, Lexington Herald Leader (Oct. 1, 2019).

[8] Tom Loftus, Casinos or taxes? Can Andy Beshear or Matt Bevin deliver on budget promises?, Louisville Courier Journal (Sept. 27, 2019).

[9] Andy Beshear, Beshear releases priorities on vision to expand gaming & create new revenue for pensions, Medium (Sept. 12, 2019).

[10] Id.

[11] Id.

[12] The Family Trust Foundation of Kentucky, Inc., D/B/A The Family Foundation vs. The Kentucky Horse Racing Commission, et al, 2018-SC-000630 (Ky); BloodHorse, Historical Racing Returns to Kentucky Supreme Court (Jun. 18, 2019), <https://www.bloodhorse.com/horse-racing/articles/234294/historical-racing-returns-to-kentucky-supreme-court>

[13] Tom Loftus, Casinos or taxes? Can Andy Beshear or Matt Bevin deliver on budget promises?, Louisville Courier Journal (Sept. 27, 2019).

[14] Id.

[15] Id.