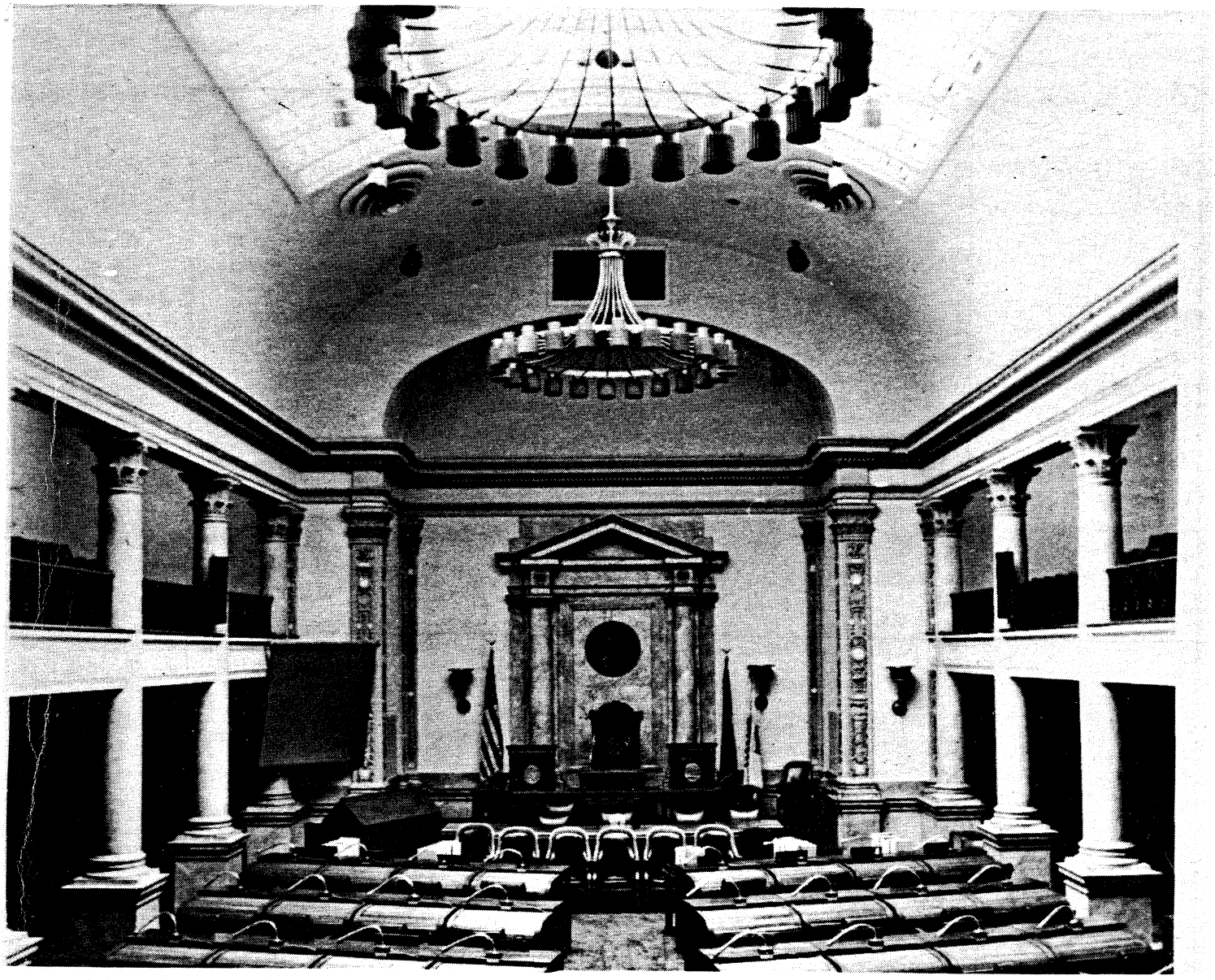
ISSUES CONFRONTING THE 1996 GENERAL ASSEMBLY



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Legislative Research Commission

Frankfort, Kentucky

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The Kentucky Legislative Research Commission is a sixteen member committee, comprised of the majority and minority leadership of the Kentucky Senate and House of Representatives. Under Chapter 7 of the Kentucky Revised Statutes, the Commission constitutes the administrative office for the Kentucky General Assembly. Its director serves as chief administrative officer of the Legislature when it is not in session.

The Commission and its staff, by law and by practice, perform numerous fact-finding and service functions for members of the General Assembly. The Commission provides professional, clerical and other employees required by legislators when the General Assembly is in session and during the interim period between sessions. These employees, in turn, assist committees and individual members in preparing legislation. Other services include conducting studies and investigations, organizing and staffing committee meetings and public hearings, maintaining official legislative records and other reference materials, furnishing information about the Legislature to the public, compiling and publishing administrative regulations, administering a legislative intern program, conducting a pre-session orientation conference for legislators, and publishing a daily index of legislative activity during sessions of the General Assembly.

The Commission is also responsible for statute revision, publication and distribution of the *Acts* and *Journals* following sessions of the General Assembly and for maintaining furnishings, equipment and supplies for the Legislature.

The Commission functions as Kentucky's Commission on Interstate Cooperation in carrying out the program of the Council of State Governments as it relates to Kentucky.

ISSUES CONFRONTING THE 1996 GENERAL ASSEMBLY

Prepared by

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Legislative Research Commission Staff

Edited by
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FOREWORD

This collection of issue briefs, prepared by members of the Legislative Research Commission staff, attempts to bring into sharper focus some of the major issues which have received considerable legislative attention to date during the interim. The report by no means exhausts the list of important issues facing the 1996 Legislature. Nor are the alternatives in the discussion of each issue necessarily exhaustive.

Effort has been made to present these issues objectively and in as concise a form as the complexity of the subject matter allows. They are grouped for the convenience of the reader into the various committee jurisdictions and no particular meaning is placed upon the order in which they are presented. Because of continuing activity by the legislative committees, a supplement to this publication will be prepared in early December.

Staff members who prepared the reports were selected on the basis of their knowledge of the subject matter and their work with the issues during the 1994-95 interim.

Vic Hellard, Jr.
Director

Frankfort, Kentucky
August, 1995

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AGRICULTURE AND NATURAL RESOURCES

AGRICULTURE

Prepared by Brooks H. Talley

Issue

Should state agencies promoting agriculture receive more state funding?

Background

Numerous studies over the years have emphasized the need for Kentucky agriculture to attain a greater portion of its potential and have attempted to rally the agriculture community to attain this potential.

The Governor's Council on Agriculture (now the Kentucky Council on Agriculture) conducted, through the U.K. College of Agriculture, studies in 1965, 1973, and 1977, on the production potential of Kentucky agriculture. The Kentucky Agriculture Development Foundation, Inc., a non-profit agriculture economic development corporation, created the Commission on the Future of Agriculture in Kentucky, which published *Plowshares to Profits: Agriculture Options for Kentucky* in May 1989. This document calls for action by seventeen state agencies to increase marketing of Kentucky agriculture commodities.

Agriculture leaders throughout the state, including representatives of 14 agriculture commodities, the University of Kentucky College of Agriculture, the state Department of Agriculture, the Kentucky Agriculture Resource Development Authority, and the Kentucky Farm Bureau Federation, Inc., developed a comprehensive master plan for Kentucky agriculture, known as *Ag. Project 2000*, which was published in March 1993. The goal of this plan is to increase the state's agriculture income from three billion dollars annually to five billion dollars by the year 2000, with a positive economic impact throughout rural and urban Kentucky.

The Governor's Agricultural Policy Task Force released its report "Retaining and Enhancing Kentucky's Agricultural Economy" in November 1993. The report recommended that the economic development of Kentucky's agriculture and the conservation of farmland could be enhanced by such actions as the promotion of value-added agribusiness and the purchase of agriculture conservation easements.

In April 1995, the Kentucky Agriculture Resources Development Authority, broadly representative of agricultural interests, made policy recommendations to the 1995 gubernatorial candidates, focusing on *Ag. Project 2000.*

The Kentucky Strategic Plan for Economic Development was adopted by the Kentucky Economic Development Partnership Board in May 1994. The strategic plan encompasses five broad goals. One goal is to "manage Kentucky's natural resources and

cultural assets to ensure long-term productivity and quality of life." This goal is to be accomplished through five different strategies. One strategy is to "promote sustainable management of Kentucky's renewable natural resources, especially agriculture and forestry." This strategy is to be implemented through five tactics. One tactic is the implementation of *Ag. Project 2000.* It is anticipated that the Kentucky Economic Development Partnership Board will this summer recommend that *Ag. Project 2000* be implemented through the continuing cooperative efforts of the Cabinet for Economic Development, state Department of Agriculture, U. K. Cooperative Extension Service, Kentucky Agriculture Resources Development Authority, Kentucky Farm Bureau Federation, Inc., and others focusing on market development, expanded value-added agribusiness, and state financing programs.

The legislative Subcommittee on Agriculture of the Interim Joint Committee on Agriculture and Natural Resources has been interested in increasing Kentucky's farm income for a long time. Going back only as far as 1984, the subcommittee has held 19 meetings relating to efforts to increase the state's agriculture income. Also, three members of the subcommittee went on a trade mission in 1987 with the Governor to Taiwan to encourage that foreign government to purchase Kentucky agriculture commodities.

Discussion

At the meeting of the Subcommittee on Agriculture, May 10, 1995, the Commissioner of the Kentucky Department of Agriculture, Dean of the U. K. College of Agriculture, and President of the Kentucky Farm Bureau Federation, Inc. discussed the policy recommendations of the Kentucky Agriculture Resources Development Authority which were made to the 1995 gubernatorial candidates. These policy recommendations focused on implementing *Ag. Project 2000.* The members of the Subcommittee on Agriculture were highly supportive of these recommendations and adopted a motion, which was subsequently approved by the Interim Joint Committee on Agriculture and Natural Resources, stating that they "strongly supported these recommendations, and agreed that now is the time for the General Assembly to financially support and enhance agriculture in the Commonwealth."

These recommendations are:

- Enhance the marketing system for Kentucky farm products - by restructuring the state Department of Agriculture's Division of Market Services and the Kentucky Council on Agriculture, and providing additional funding for more aggressive marketing, such as regional agriculture marketing centers and regional, national, and international trade shows.

- Sustain and enhance environmental and natural resource productivity - by appropriating additional money to the state Division of Conservation for the new cost-share program which assists farmers in implementing practices to protect soil and water quality;

- Achieve agriculture production potential - by appropriating new funds to develop and implement agriculture programs, expand research activities, maintain facilities, and replace inoperable equipment at the departments of agriculture at the state's universities; and

- Expand agribusiness and value-added opportunities - by appropriating funds for agribusiness networks.

The estimated cost of these recommendations is about $17.2 million in fiscal year 1996-97 and increases annually to about $20.3 million in fiscal year 2003-04.

FORESTRY PRACTICES

Prepared by Mary Lynn Collins

Issue

Should Kentucky make changes in its forestry policies?

Background

New opportunities are emerging for Kentucky's forest industries. Experts predict increased demand for timber because of a recovering domestic economy and new international trade agreements. Demand for timber in the national forests of the northwest is expected to shift to the southeast, where much of the forest land is privately owned. Kentucky, with almost 13 million acres of forests, should benefit from these developments. Much of the land cut over during Kentucky's big timber boom around the turn of the century is once again mature forest land. Timber stumpage prices in the state continue the steady upward movement that started in 1992.

Initiatives passed in the 1994 Regular Session of the General Assembly to develop a thriving secondary forest products industry could also increase demand. These initiatives target wood products businesses and include new worker training and technology transfer programs, incentives for wood processing and manufacturing collaboratives, and a commitment by the state to use and showcase Kentucky wood products in its own facilities. A newly-established government corporation, the Kentucky Wood Products Competitive Corporation, is coordinating the new initiatives. While projections for increased demand present real economic opportunities, they also trigger new concerns regarding sustainability of the resource and possible harmful effects to the environment, particularly water resources, if good management practices are not employed.

Over 90 percent of the forest land in this state is owned by non-industrial private owners and holdings tend to be small, the average being 26 acres. Typically, these lands are not actively managed to sustain the resource or to ensure high-quality forest products. Fewer than ten percent of private landowners have sought professional forestry assistance. The state Division of Forestry provides technical and financial assistance to woodland owners through its forest stewardship program, but the division's resources are limited and there is a long waiting list for this assistance.

Most forestry experts agree that Kentucky's forests are not producing as high a quality of commercial timber as they could, due in part to past land management and harvest practices. For several decades much of the timber cut in the state has been by "high grading", a harvest practice where only the best trees are cut and the less desirable ones, often defective, are left to grow and serve as stock for future regeneration. High

grading, over time, leads to a lower-quality forest product. Fire and animal grazing have also affected timber quality.

Timber removal remains a relatively unregulated industry practice in this state. However, legislation adopted in the 1994 Regular Session of the General Assembly requires all agricultural operations, including timber harvesting, to establish plans to protect ground and surface waters. The Kentucky Master Logger Program, a voluntary program, provides training with emphasis on the forest practice guidelines for water quality developed by the state Division of Forestry. In the absence of state regulation, the Letcher County Fiscal Court recently considered an ordinance to license commercial loggers, but the proposal was defeated.

In addition, urban expansion into rural areas is causing concern among woodland owners. Transplanted city dwellers bring with them a different value system and may protest when they feel the beauty and tranquillity of their new rural setting are threatened by nearby logging activities.

Discussion

Discussions on forestry are now underway in a variety of arenas. The 1994 Governor's Annual Conference on the Environment was devoted exclusively to forestry issues. Over 600 people attended the three-day conference. A series of regional forums followed the conference. Comments offered in the forums are to be used by the state Division of Forestry to develop a forest resource plan, probably to be available prior to the 1996 Regular Session of the General Assembly. The Interim Joint Committee on Agriculture and Natural Resources held two meetings on the issue this interim. One of the meetings was a public hearing on forestry concerns; in the other meeting, the committee considered forest policies of other states. The first "Forest Commons" conference convened at Eastern Kentucky University in the Spring of 1995 to consider preservation of private woodlands. While the conferees represented as many as 17 different states, much of the discussion focused on Kentucky's forest resource.

Solutions to many of the issues raised in these public discussions could require legislative action or funding. Most observers agree that a major educational effort and an incentive program targeting both woodland owners and loggers are needed. Suggested ways to accomplish that include: (1) hiring more state foresters to provide technical assistance; (2) developing more cost-share opportunities and other incentives for woodland owners to promote land stewardship; and (3) creating incentives for loggers to complete the Kentucky Master Logger Program and employ best management practices for timber removal. Some feel that education and incentives are not enough and they argue for additional regulatory requirements. Recommendations emerging from this debate range from adoption of a minimum set of standards to a full-blown regulatory program with logger certification, harvest practice regulations, and bonding requirements. Finally, some woodland owners are interested in a "right-to-practice forestry" law to protect them from nuisance suits from new neighbors.

WASTE TIRES

Prepared by Daniel J. Risch

Issue

Should the 1994 amendments to the waste tire law be further refined?

Background

The waste tire law became effective in January of 1991. Unfortunately, the law's effectiveness has been curtailed because of severe shortfalls in the waste tire trust fund. The fund is supported by a one dollar fee paid per new motor vehicle tire sold in Kentucky. However, exemptions allowed under the law as originally written have prevented the expected revenue from materializing.

Nevertheless, by the end of 1993, according to Department for Environmental Protection records, $934,850 was available for grants under the law, and $374,826 for loans. Examples of how the money has been applied include a $375,000 grant to Boyd County. The county sought the funding in order to buy equipment to reduce scrap tires to a powder that could be applied in asphalt and other applications. Louisville requested $50,000 that could be used to help fund community groups that locate and clean up tire piles.

In the view of some, however, the expenditure of this money was too little and too late. Kentucky's citizens throw away an estimated 3,800,000 tires each year. From January 1991, when the waste tire law became effective, to near the end of December 1993, when money first began to be disbursed from the fund, a total of approximately 11,400,000 tires were discarded.

Using national data generated for 1990 by the U.S. Environmental Protection Agency, only 37.4% of the waste tires discarded in those years (4,263,600 tires) can be expected to have been reused in some environmentally preferred manner. The remaining 7,136,400 discarded tires were landfilled, stockpiled, or illegally dumped.

The 1994 General Assembly recognized the shortcomings of the 1991 version of the waste tire law and accordingly amended the law to achieve two main goals.

First, the retailer's exemption from collecting the one dollar fee was more specifically defined. Now, for a retailer to be exempt from collecting the fee, the retailer must enter into a contract for disposal of waste tires with a contractor acceptable to the Department for Environmental Protection as either reusing the waste tires or processing and sending the waste tire material to someone else who will use the material.

This change has a dual purpose. Because the markets for waste tires or waste tire material remain few, more retailers will be required to collect the waste tire fee. Thus, the waste tire fund can be expected to grow. Additionally, fewer "tire jockeys" will be expected to contract to legally dispose of a retailer's waste tires, only to either illegally dump the tires or legally accumulate tires until the accumulation itself creates an environmental hazard and runs afoul of administrative regulations.

The second major goal of the 1994 waste tire amendments was to establish a data base on Kentucky's waste tires.

As the least burdensome manner available, retailers now must include information on waste tires disposed of when the retailer submits the waste tire fee to the Revenue Cabinet. The amendments also require retailers who have received an exemption from collecting the fee to report this same information. In this manner the state will gain accurate information on the number of waste tires disposed of and how they are disposed.

Discussion

It is no overstatement to say that many people have been displeased with the waste tire law over the five years of its life. From the law's sponsors, to the law's implementors, to the regulated community, all assert that minimal progress has been seen in attacking the state's accumulations of waste tires and properly managing the generation of new waste tires. The 1994 amendments have not been operational long enough to show results.

The Department for Environmental Protection conservatively estimates that 10,000,000 waste tires are presently stockpiled or illegally dumped around the Commonwealth. And to this accumulation must be added the estimated 2,378,800 tires generated each year that currently end up being stockpiled or dumped because of a lack of alternatives. These figures alone clearly show that the need to manage waste tires only continues to grow.

However, additional information recently acquired adds some urgency to this need.

Agency surveys have confirmed the presence of the Asian tiger mosquito in 59 Kentucky counties. This mosquito can carry LaCrosse encephalitis and Eastern equine encephalitis. Waste tire dumps are ideal breeding places for this mosquito.

With the 1994 amendments in place the Department for Environmental Protection can be expected to accelerate the pace of implementing the law. As the agency moves forward, further refinements may make the agency's task more effective.

An effort may be made to work with retailers so that they take and properly dispose of waste tires when new tires are purchased. Also, the agency, or perhaps the Attorney General's office, may alert retailers to misleading or fraudulent explanations about the waste tire fee. And the public itself could benefit from government efforts to better explain the fee and its purposes.

Efforts may be directed once again to build markets for waste tire material. County solid waste coordinators could be networked with the Recycling and Marketing Authority. Groundwork might be laid to foster markets for waste tires as a boiler fuel.

ON-SITE SEWAGE TREATMENT LAGOONS

Prepared by Daniel J. Risch

Issue

Should state and local regulations of on-site sewage treatment lagoons be revised?

Background

Lagoons for on-site sewage treatment are used primarily where heavy clay soils do not allow the use of septic tank systems or other on-site systems for treating sewage. The clay soils do not allow sewage effluent to pass through the soil and be cleansed in a process of filtration, adsorption, and microbial decomposition. Consequently, a lagoon is constructed with the limitations of the soil as a cleansing agent in mind.

A lagoon on-site sewage treatment system has three components. The first is a septic tank pretreatment unit that is buried ten to twenty feet from the effluent source. The tank collects most of the solids. The second is the lagoon, which is a pond designed to hold liquid effluent to a three- to six-foot depth. The final component is a pipe to carry overflow into a lateral field when rain causes the lagoon capacity to be exceeded.

Natural processes in both the surface and subsurface layers of the lagoon liquids and in the soils surrounding and in the bottom of the lagoon eliminate contaminants in the sewage.

Since 1982, nine hundred and fourteen lagoons have been installed throughout Kentucky. Geographically, lagoons are concentrated in the northern, central, and western areas of the state. Over 95 percent of lagoons service single-family and multifamily residences.

The state Cabinet for Human Resources regulates the construction, installation, and alteration of on-site sewage disposal systems. In addition, local boards of health may be authorized by the cabinet to issue permits for on-site sewage disposal systems. A local board of health authorized to issue permits may also establish fees to cover inspections related to construction, installation, alteration, maintenance and operation of on-site sewage disposal systems.

Discussion

Some counties have experienced high population growth in suburban or semi-rural settings. When this growth occurs in geographical areas that depend heavily on lagoons

for on-site sewage treatment, and they become more visible to greater numbers of people, concerns arise about the proper construction and operation of lagoons .

Of immediate concern is the coordination between the Cabinet for Human Resources and local health offices. The cabinet is authorized to regulate the construction, installation, and alteration of lagoons. This the cabinet does by standards set out in administrative regulations. Additionally, the cabinet then delegates to local health officials the authority to enforce these standards.

For their part, the local health officials may not only regulate, through the delegation of authority from the cabinet, the construction, installation, and alteration of lagoons, but they may also regulate the operation and maintenance of the facilities. However, at this time no local board of health is known to have exercised the authority to regulate maintenance and operation of lagoons.

The greatest need for regulatory controls on the use of lagoons is to protect groundwater resources. The present requirement that offers this protection is that the bottom of the lagoon be separated from bedrock by a minimum of eighteen inches of soil. The soil will cleanse any effluent that might seep from the lagoon before the effluent reaches the water table.

This requirement necessitates careful construction techniques. To ensure proper construction, greater attention may need to be given to construction inspections by regulatory officials.

A related issue concerns the siting of lagoons. Because of the increased use of lagoons in increasingly populated areas, setback requirements may need to be reviewed. For the protection of appearances, greater distances between a lagoon and property lines may be required. Similarly, a greater minimum lot size before a lagoon may be used may also be required. However, greater setback distances and larger minimum lot sizes will conflict with the ability to develop certain properties. These properties might be restricted to using lagoons as an on-site sewage treatment method but lot sizes or shapes may preclude meeting greater lot size requirements or setback distances.

Finally, maintenance and operation of lagoons may need to be more tightly controlled. This will place greater responsibilities on the lagoon owners and the local health departments.

Maintenance problems range from overgrowth of aquatic weeds, to animals burrowing into berm walls, to damaged fencing. A voluntary program to educate lagoon owners may reduce many of these problems. However, to completely address maintenance and operation problems may require active enforcement by local health officials.

Both of these possibilities may require additional funding for the cabinet to carry out an information program and for local officials to implement maintenance inspections.

APPROPRIATIONS AND REVENUE

MOTOR VEHICLE USAGE TAX AND AD VALOREM TAX

Prepared by Terry Jones

Issue

Should the General Assembly amend the definition of "retail price" for the levy of the motor vehicle usage tax on used motor vehicles and change the valuation method used to value motor vehicles for ad valorem tax purposes?

Background

Kentucky first taxed the sale of motor vehicles under the sales tax law enacted in 1934. Upon repeal of the sales tax in 1936, a special three percent sales or usage tax on motor vehicles was enacted. The tax was levied only upon transactions involving the registration of motor vehicles not previously registered in this state. The tax was collected by the county clerk, and was based upon the value of the vehicle the first time it was licensed in Kentucky. Used motor vehicles taxes were based on the vehicle values listed in an automotive reference manual prescribed by the Revenue Cabinet.

In 1960, with the enactment of the general sales and use tax law, the receipts from the sale of used motor vehicles previously registered in this state were subject to the three percent sales tax. A trade-in deduction was allowed in determining the receipts subject to tax. The tax was remitted and reported by the dealer on the monthly sales tax return.

Thus, from 1960 until 1968, used motor vehicles were being taxed two different ways under two different laws. If the used motor vehicle had never been registered in this state, then it was taxed under the motor vehicle usage tax law, based upon the value appearing in an automotive reference manual prescribed by the Revenue Cabinet, with no trade-in deduction allowed. If the used motor vehicle was previously registered in this state, then it was taxed under the sales and use tax law, on the basis of the actual sales price, with a deduction for the amount allowed by the dealer for a trade-in.

In 1968, when the sales tax rate was raised to five percent, the taxation of used motor vehicles previously registered in this state was transferred from the sales and use tax law to the motor vehicle usage tax law. The taxation of first-time licensed used motor vehicles and used motor vehicles previously registered in this state were combined under one statute and retained some features of both laws. The tax rate was set at five percent of the value of the used motor vehicle. This value was determined from an automotive reference manual prescribed by the Revenue Cabinet. The tax was collected by the county clerk and a trade-in deduction was allowed, provided that the used motor vehicle being traded was previously registered in this state.

In 1990 the tax rate on motor vehicles was raised from five percent to six percent.

Section 172 of the Kentucky Constitution requires that all property not exempted from taxation by the Constitution be assessed for taxation at its fair cash value, estimated at the price it would bring at a fair voluntary sale. KRS 132.485 provides that motor vehicles be assessed at a valuation determined from a standard manual prescribed by the Revenue Cabinet. The Revenue Cabinet uses the average retail value from a manual compiled and published monthly by the National Automotive Dealers Association (NADA). In theory, average retail value should approximate that estimated price that a motor vehicle would bring at a fair voluntary sale, as required by the Constitution.

Discussion

The levy and payment of taxes is an issue that is frequently discussed by citizens of the Commonwealth. The discussion normally focuses on the fairness and equity of the levy and payment of the tax. One area of particular concern that has been mentioned repeatedly to legislators, county clerks, and Revenue Cabinet officials is that the current method of taxing motor vehicles is unfair because it results in the imposition of a tax on a value higher than that actually being paid by purchasers of motor vehicles.

In response to these concerns, legislation was introduced during the last several regular sessions of the General Assembly attempting to alter the method for taxing used motor vehicles. However, none of the legislative proposals have been enacted, primarily because of the lack of credible data relating to the actual selling price of used motor vehicles in the Kentucky market. The lack of credible data left proponents of the legislative proposals unable to substantiate the validity of these concerns. In addition, the lack of data has made it very difficult to accurately analyze the fiscal implications of the adoption of any legislative changes. As a result, the Legislative Research Commission approved a request that LRC staff and Revenue Cabinet officials jointly conduct a study of the current method of taxing used motor vehicles. Although the study was done to examine the motor vehicle usage tax levy on used motor vehicles, the findings are equally applicable to the ad valorem tax levy.

The study shows that on average, used motor vehicles are bought and sold in Kentucky at less than the National Automobile Dealers Association (NADA) average retail value. A significant majority of both buyers and sellers reported paying and receiving less than the NADA retail value. In general, later models are traded closer to the NADA retail value than older models. It may be that mileage plays a more important role in the sale price as the car ages, with a greater premium for low mileage and a greater discount for high mileage. The fact that NADA makes adjustments for high and low mileage reinforces this belief. The Revenue Cabinet's use of the NADA average retail value may need some modification in order to more accurately reflect the market value of motor vehicles in Kentucky.

As long as Kentucky continues to use a method of valuation that assesses used motor vehicles based on a value other than actual purchase price, there will be variations, and buyers will continue to question the fairness of the tax in cases where the purchase price is significantly less than the NADA average retail value. However, a method of

valuation based on the actual purchase price without a reliable method of verification could lead to significant tax equity questions that could undermine the tax, as witnessed by the significant number of buyers and sellers reporting different amounts being paid or received for the same used motor vehicle.

The results of the study cited are presented in the Legislative Research Commission's Research Memorandum No. 468.

INTANGIBLE PERSONAL PROPERTY TAX

Prepared by Terry Jones

Issue

Should the General Assembly propose to amend the Kentucky Constitution to exempt some or all classes of intangible personal property from taxation?

Background

Section 172 of the Kentucky Constitution requires that all property not exempted from taxation by the Constitution be assessed for taxation at its fair cash value, estimated at the price it would bring at a fair voluntary sale.

Intangible personal property includes stocks, bonds, bank deposits, annuities, account receivables, and like property. For tax purposes, intangible personal property is divided into many different classes, which are taxed at different rates. Intangible personal property as a general rule is assessed as of January 1 of each year. The tax generates between $95 and $100 million in state revenues on an annual basis. Following is a list of some of these classifications with the tax rate and the revenues generated.

Type of Property	Statute	State Tax Rate per $100	Local Tax Rate per $100	State Revenue ($ million)
Bank Shares	KRS 136.270	$0.95	$0.19	$30.5
Brokers Accounts Receivables	KRS 136.050	$0.10	Exempt	$ 0.1
Life Insurance Capital	KRS 136.320	$0.70	$0.15	$ 4.0
Savings and Loan Assoc. Capital Stock	KRS 136.300	$0.10	Exempt	$ 6.2
Public Service Co.	KRS 136.120	$0.25	Exempt	$ 0.6
Stocks, bonds, out-of-state bank deposits, etc.	KRS 132.020	$0.25	Exempt	$55.2

There are other classes of intangibles such as in-state bank deposits, profit sharing plans, annuities, and retirement plans that are taxed at $0.001 for each $100 of valuation and are exempt from local taxes.

Discussion

The intangible personal property tax is frequently cited as a tax that is unfair and counterproductive. Proponents of eliminating the tax claim that the tax is a disincentive in

attracting new investments to the state and that it encourages wealthy Kentuckians to move out of state. They claim that the elimination of the tax would be offset by new tax revenues generated through increased economic activity and additional investment.

Opponents of eliminating the intangible personal property tax counter that the positive economic impacts will not offset the negative impact of lost intangible tax revenues and that the elimination would primarily benefit upper income individuals.

It should be noted that some businesses pay intangible personal property tax in lieu of other taxes. This is an important issue that the General Assembly may want to consider in any debate of the complete elimination of the intangible personal property tax. These businesses and the taxes they are exempt from paying are as follows.

(1) Banks and trust company shares (KRS 136.270).

Bank and trust companies currently pay $0.95 on each $100 of taxable value of their shares. The tax is paid by the bank or trust company on behalf of the shareholder and the shareholder is not required to list the shares for taxation. Banks and trust companies pay this tax and are exempt from the corporate income and license tax. Revenues from this tax for FY 1992-93 were approximately $30.5 million.

(2) Savings and loan associations capital stock (KRS 136.300 and 136.310)

Savings and loan associations currently pay $0.10 on each $100 of taxable value of their capital stock. The tax is paid by the bank or trust company on behalf of the shareholder and the shareholder is not required to list the shares for taxation. Savings and loan associations pay this tax and are exempt from the corporate income and license tax. Revenues from this tax for FY 1992-93 were approximately $6.3 million.

(3) Insurance companies taxable capital (KRS 136.320)

Domestic life insurance companies currently pay $0.70 on each $100 of taxable capital. Domestic life insurance companies pay this tax and are exempt from the insurance premiums tax, the corporate income and license tax. Revenues from this tax for FY 1992-93 were approximately $4 million.

(4) Public service companies property tax assessments (KRS 136.120)

Property taxes are assessed against the operating property, non-operating tangible property, and non-operating intangible property of public service companies. Public service companies include utility companies, such as electric, gas, water, telephone, cable television, and transportation companies, such as railroads, air carriers, pipelines, and water transportation. The revenue received during the 1992-93 fiscal year attributable to non-operating intangible property was approximately $0.58 million. Public service companies are exempt from the corporation license tax.

COMPREHENSIVE TAX REFORM

Prepared by Pam Lester

Issue

Is Kentucky's tax system in need of a comprehensive overhaul?

Background

Kentucky's tax system has been in the news a lot lately and most of the news has not been good. In nine of the last twelve years, between-session budget cuts have been made to address revenue shortfalls totaling hundreds of millions of dollars. Lawsuits have been filed challenging different aspects of various taxes. The legislature has been under increased pressure from businesses and individuals to provide exemptions from one tax or another. There has been a series of newspaper articles questioning the long-term wisdom of tax credits offered as a part of Kentucky's economic development efforts. Private citizens groups have repeatedly called for the repeal of the intangibles tax, claiming that this tax causes Kentucky to lose valuable citizens. Businesses threaten to leave Kentucky because of the tax system. Each year, the list of problems with the tax system and proposed solutions to remedy the budget woes grows longer.

Kentucky is not alone in its fiscal problems. On a national level, groups such as the National Conference of State Legislatures, the National Governors' Association, the Federation of Tax Administrators, the Multistate Tax Commission, and the National Association of State Budget Officers have grappled with tax-related issues. They've looked at how the changes in the overall economy, population shifts, and federal tax policy have undermined the traditional bases of state tax systems. These groups have determined that the changing circumstances in the United States and in the world have caused state tax systems in the main to be unresponsive, inequitable, and difficult to manage.

Discussion

The problems with Kentucky's tax system have been discussed, analyzed, and debated by many groups over the years. In fact, The Kentucky Commission on Tax Policy, appointed by Governor Jones in early 1995, is currently meeting to prepare a report that will be issued in August or September of this year. The report issued by the Commission on Tax Policy will join numerous other studies, plans and proposals that identify problems with Kentucky's tax system and propose solutions. At various times, the legislature has addressed one problem or another. However, there has never been a comprehensive effort at tax reform that considers all of the problems and all of the solutions, to create a comprehensive system that meets the existing needs of Kentucky, while insuring that the tax base will grow as the needs of the state grow.

Some of the problems with Kentucky's tax system that have been consistently identified over the years are as follows:

- **The Sales and Use Tax** - The sales and use tax was enacted when manufacturing was the mainstay of the economy. It primarily taxes the sale of goods. In today's world, services have supplanted manufacturing as the backbone of the economy. Business has become more global, and the fastest growing sector in the economy is the information-based industry. Because Kentucky does not generally tax the service sectors of the economy, it is impossible for the sales and use tax to keep pace with the growing needs of the state.

- **The Corporate Income Tax** - Kentucky's corporate income tax was enacted many years ago when most companies manufactured goods and sold them within the United States. Today, companies operate on a worldwide basis. They sell goods, services, tangible items, and intangible items. Since Kentucky's tax system was created to address the domestic sale of goods, it does not adequately address the international sale of goods and services. It does not adequately address income earned by service and information-based companies. The results are unintended loopholes which allow many corporations to legally avoid the payment of tax in Kentucky.

- **Property Tax** - In 1979, the Kentucky legislature passed House Bill 44, which placed limits on the overall permitted growth in property tax assessments on a statewide basis. The effect of this legislation is that the property tax base has failed to grow in proportion to the growth in the economy. In fact, statewide property tax rates have decreased each year since the enactment of House Bill 44. With the property tax shouldering less of the overall tax burden each year, the other major taxes have been relied upon to make up the difference.

- **The Inheritance and Intangibles Taxes** - For many years, the inheritance and intangibles taxes were the two taxes most often identified by those seeking to reform our tax system as being unfair, oppressive and counterproductive, when compared to taxes imposed by other states. The General Assembly recently addressed these claims regarding the inheritance tax, through the enactment of legislation during a 1995 Special Session which phases in, over a four-year period, an exemption from the inheritance tax for all Class A beneficiaries. The intangibles tax, the repeal of which would require a constitutional amendment, remains an issue.

The issue of comprehensive tax reform is renewed every year in one form or another. This trend will probably continue until comprehensive tax reform is considered by the General Assembly. It is a complex problem that will require an unprecedented effort and commitment on the part of the legislature, the executive branch, and the citizens of Kentucky to solve.

ECONOMIC DEVELOPMENT TAX CREDIT PROGRAMS

Prepared by Pam Lester

Issue

Should the reporting and oversight requirements applicable to Kentucky's economic development incentive programs be enhanced?

Background

In business development circles, Kentucky is well known for the incentive and investment packages it can offer companies seeking to locate in Kentucky, and those already located in Kentucky that are seeking to expand. In fact, Kentucky's economic development programs have been called the "state-of'-the-art in business incentives."[1] Kentucky currently has four major economic development incentive programs that offer substantial tax credits to qualifying companies. In addition to the tax credit programs, many companies are also eligible for preferential financing, local tax abatements, and sales and use tax exemptions.

To remain competitive in today's business climate, several other states have enacted economic development legislation similar to Kentucky's. The result has been an increase in interstate tax competition for economic development. As more states join the ranks of those actively seeking economic development projects through tax and investment incentives, the cost of incentives offered per job created get higher and higher.

There have been growing concerns in the General Assembly over the past few years that Kentucky's economic development programs do not contain adequate reporting and oversight provisions. Because of the lack of available information, it has been difficult for legislative committees interested in following up on the state's economic development efforts to do so.

There are no real reporting mechanisms or measuring tools in regular use that can be used by the General Assembly to determine the effectiveness of using tax incentive programs to lure businesses to the state. The Capital Projects and Bond Oversight Committee provides legislative oversight of bonds issued in conjunction with the state's economic development efforts; however, the tax incentive programs are not reviewed by the legislature at all.

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[1] Bidding for Business: Are Cities and States Selling Themselves Short?; Corporation for Enterprise Development, 1994.

Discussion

Prior to the 1994 legislative session, the Capital Projects and Bond Oversight Committee requested that the Appropriations & Revenue Committee and the Economic Development Committee consider whether legislation should be developed which would require greater legislative oversight in the granting of tax credits. Legislation was introduced during the 1994 session that would have required greater disclosure by companies receiving economic development benefits, increased reporting by both the Economic Development Cabinet and Revenue Cabinet, and enhanced legislative oversight of the entire process. The legislation was not enacted, but the issue remains a viable and controversial issue that will face the General Assembly in the 1996 Session.

PROVIDER TAX

Prepared by Susan Gilliland and Pam Lester

Issue

Should Kentucky use the provider tax to fund its share of the Medicaid program?

Background

Prior to the Second Extraordinary Session of the 1993 General Assembly, Kentucky funded a portion of its share of Medicaid expenditures through a special tax levied against health care providers who participated in the Medicaid program. This tax was passed during the 1991 Special Session of the General Assembly. Under the law, a special tax was levied against hospitals and other health care providers participating in the state Medicaid program. Amounts collected under the tax were placed in a fund called the "Medicaid Assessment Revolving Trust." Money in the fund was used to obtain federal matching funds.[2] Participating providers were guaranteed a return of an amount at least equal to the tax paid, although most providers received returns in excess of 200% of the amount paid in taxes. This type of financing was known as "bootstrapping" because it allowed Kentucky to "borrow" money from providers participating in the Medicaid program to obtain the increased federal match.

At that time, Kentucky was one of 39 states that used some form of bootstrap financing for its Medicaid program. The federal government became concerned about this process after the Health Care Financing Administration (HCFA) determined that it had the effect of reducing the actual cost of the Medicaid program for the states, while increasing the cost of the program for the federal government. In response, Congress passed the Medicaid Voluntary Contribution and Provider Specific Tax Amendments of 1991 (P.L. 102-234). In order to comply with P.L. 102-234 by July 1, 1993, Kentucky passed House Bill 1 during the Second Extraordinary Session in May 1993. Significant differences included applying the tax to all providers in a class, regardless of whether the provider participated in the Medicaid program, deleting a hold harmless provision, which guaranteed a return of taxes paid, and basing the tax on income rather that criteria related to Medicaid participation and payments. House Bill 1 was to sunset on the earlier of 90 days after the close of a special session on health care or 90 days after the close of the 1994 Regular Session.

Because there was no special session prior to the 1994 session, the General Assembly had to reconsider the provider tax during the 1994 Regular Session. The General Assembly ultimately reenacted the provider tax as part of House Bill 250, the Health Care Reform Act. The new tax is substantially the same as the tax passed during

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[2]For each dollar that Kentucky spends in the Medicaid program, the federal government provides an approximate 2.32 to 1 match.

the 1993 Special Session, with a few notable exceptions. Under the old provider tax, the Secretary of the Cabinet for Human Resources was permitted to add new providers to those subject to the tax. The Secretary was also permitted to adjust the rate of tax, if necessary, to keep the state within the federally established limits. The provider tax levied under House Bill 250 does not allow for the addition of new groups or adjustment of the tax rates. Another key difference is that the old provider tax prohibited providers from passing the tax on to consumers, while the new tax is silent regarding the ability of providers to pass the tax on. The provider tax levied under House Bill 250 will also allow freestanding psychiatric hospitals, which were taxed at 2.5% under the old provider tax, to be taxed at a lesser rate of 2% if necessary waivers are obtained from HCFA.

The services currently taxed under 1994 House Bill 250 and the applicable rates are as follows: inpatient and outpatient hospital services, 2.5%; nursing facility services, 2%; services of intermediate care for the mentally retarded, 2%; physicians' services, 2%; licensed home health care agency services, 2%; HMO services, 2%; and outpatient prescription drugs, $0.25 per prescription.

The original estimated receipts and the federal match attributable to receipts from each group are as follows:

PROVIDER CLASS[3]	FY 1995	FEDERAL MATCH[4]	FY 1996	FEDERAL MATCH
Hospital (55%)	$ 88.8M	$206.3M	$ 93.7M	$214.3M
Physician (25%)	$ 40.4M	$ 93.9M	$ 42.6M	$ 97.4M
Nursing Homes (9%)	$ 14.5M	$ 33.7M	$ 15.3M	$ 35.0M
Pharmacy (6.5%)	$ 10.5M	$ 24.4M	$ 11.1M	$ 25.4M
IC/FMR (1%)	$ 1.6M	$ 3.7M	$ 1.7M	$ 3.9M
Home Health (3.4%)	$ 5.7M	$ 13.2M	$ 6.0M	$ 13.7M
HMO Services[5]				
TOTAL	**$161.5**	**$375.2**	**$170.4**	**$389.7**
GRAND TOTAL	**$536.7M**		**$560.1M**	

Discussion

Based upon current collections, the existing provider tax should generate around $170 million for the state in fiscal year 1995, with the state receiving $389 million in matching funds from the federal government, for a total of $559 million. This constitutes 28.88% of the Medicaid benefits budget. If the provider tax is repealed, an alternative funding source must be found, or the Medicaid budget will have to be reduced. It has also

[3] Figures presented are based on estimates and have not been adjusted to reflect actual numbers for FY 1994.

[4] Federal match numbers are approximate and have been rounded.

[5] The approximate annual revenue from this source is $50,000, which is too small to show up in the method of presentation selected here.

been suggested that money lost as a result of the repeal of the provider tax could be recouped through better management of the Medicaid program.

One possible way to cut the Medicaid budget is to eliminate all optional services provided under Medicaid. Optional services include intermediate care for the mentally retarded, prescriptions, community mental health, mental hospital services, renal dialysis services, AIS/MR waiver services, HCB waiver services, Kenpac, and preventive health services. Under the projected expenditures for 1995, cutting these services would reduce the Medicaid budget by $542 million.[6]

Another option to reduce Medicaid costs is to reduce the fees paid to doctors and other providers not protected by the Boren Amendment.[7] However, any proposed reduction in fees that results in enough savings to replace the provider tax would probably cause large scale defections from the program by providers.

One of the primary complaints regarding the provider tax by the medical community is that the tax isn't broad-based. They believe that the tax should be levied against services other than just those provided by health care providers. If a broader-based tax is desired, a tax from which more than 15% of the revenues are derived from sources other than providers could be imposed. This new tax would not be considered a "provider tax", as that term is defined under federal law, and the provisions of the Medicaid Moratorium Act of 1991 generally would not have to be complied with.[8] This percentage could be met by imposing a tax on some other selected services, such as professional, personal, or business services, along with the tax on providers, or by grouping the tax on providers with taxes currently imposed on other services.[9]

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[6]Although this number represents the savings of current direct expenditures if enumerated optional services were discontinued, actual savings will most likely be less because many of the optional services are preventative in nature. If preventative services are no longer provided, the cost of acute services will probably increase.

[7]The Boren Amendment requires that cost-based providers be compensated at a rate that reasonably and adequately meets the costs which must be incurred by an efficiently and economically operated facility.

[8]Under the Medicaid Moratorium Act of 1991, a tax is "health care related" if the tax is imposed against the provision of, or the authority to provide, health care services, if the tax is imposed on the payment for health care services, or if the tax is related to health care services (at least 85% of the burden of the tax falls on health care providers).

Some of the specific limiting provisions of the Medicaid Moratorium Act of 1991 that would no longer have to be complied with if the tax was not considered a "health care related" tax are as follows:

1) The tax could be imposed against providers or groups not specifically mentioned;

2) The tax could be imposed other than on a gross income or per bed basis (i.e. a net tax); and

3) Upper revenue limitations would not have to be complied with.

[9]For example, the sales and use tax includes a tax against intrastate and local telephone service, hotel and motel rooms, and amusements. These are really services, and they could be grouped with the provider tax to create a new services tax.

If an alternative funding source is desired, an increase in the rate of the income tax or sales and use tax could be implemented, or some of the exemptions from the sales and use tax could be removed.

BANKING AND INSURANCE

BANK SHARES TAX

Prepared by Greg Freedman

Issue

Should the General Assembly change the method of determining fair cash value for purpose of bank shares taxes, or find a new way of taxing banks that recognizes the multistate operation of banks?

Background

After the U.S. Supreme Court rendered its opinion in 1819 in *McCulloch v. Maryland*, 17 U.S. 315, it became clear that states may not tax national banks without the permission of Congress. In 1864 Congress passed the National Currency Act, which restricted state taxation of banks to real estate and shares. Section 41 allowed the state in which the national bank was located to tax the bank shares. Although the tax was imposed on the shareholder, it was actually paid by the bank. In response to a U.S. Supreme Court decision, the 1900 Kentucky General Assembly enacted a law which imposed a tax on shares of stock of each national bank doing business in Kentucky. The intent of the law was to put national banks on equal footing with state-chartered banks, which had been paying a franchise tax since 1892. In 1906, the Kentucky General Assembly removed the franchise tax from state-chartered banks and extended the shares tax to both state-chartered and nationally-chartered banks in Kentucky. That statute remains in effect today as KRS 136.270. Kentucky retained the shares tax as the method of taxation of national banks although subsequently states were given alternative methods of taxation by Congress. After much litigation over the provisions of the 1864 National Currency Act, in 1923 Congress amended the law and created Section 5219, which allowed a state to choose any one of three methods of taxation: bank shares, dividends, or net income. In 1926 Congress added a fourth option of a franchise or excise tax. Because of the various conditions attached to these options, more litigation followed. In 1959 the U.S. Supreme Court upheld state taxation of nondomiciliary corporations that do business with their residents. The effect of the Congressional laws and court decisions was to free states to tax nondomiciliary state banks but not out-of-state national banks. In 1969 Congress repealed its prior restrictions on state taxation of national banks but delayed the effective date until 1973, which was later extended to 1976. Federal law now allows state taxation of national banks, as long as the taxes do not discriminate against national banks.

The bank shares tax is not a tax on the bank or its property, but is a tax on the intangible property owned by shareholders. As the representative of the shareholder, the bank pays the tax annually to the sheriff of the county. The statute allows a state tax on bank shares of 95 cents per $100 of the taxable fair cash value of shares, and a county and city tax on bank shares of no more than 19 cents per $100 times the fair cash value of shares divided by the taxable fair cash value of shares. When a 1983 U.S. Supreme Court decision held that a Texas property tax on bank shares violated a federal law, Rev. Stat.

Sec. 3701, because the state tax was computed on the basis of a bank's net assets without any deduction for tax-exempt U.S. obligations held by the bank, Kentucky banks requested refunds on the tax. The 1984 Kentucky General Assembly responded with an amendment to the statute that established a method to be used to determine the fair cash value and the taxable fair cash value of bank shares and it added subsection (5) to KRS 136.270, which provides the Revenue Cabinet with the flexibility in "any extraordinary case" to use "other recognized criteria" to determine fair cash value.

During the 1994 Session of the General Assembly, HB 82 was introduced. The bill had been prefiled during the interim and was supported by the Revenue Cabinet. The legislation amended KRS 136.270 to delete the method to determine the fair cash value and the extraordinary case provision. It replaced them with a provision that said beginning on January 1, 1995, the fair cash value and the taxable fair cash value would be determined by the Revenue Cabinet. The bill was referred to the Appropriations and Revenue Committee but was never posted for consideration. The Revenue Cabinet is required by Section 172 of the Constitution of Kentucky for purposes of taxation to assess all property at its fair cash value. The Revenue Cabinet decided that the statutory formula in many cases did not result in the fair cash value of bank shares and issued assessments based on "other recognized criteria," as allowed by statute. This resulted in many Kentucky banks filing protests in 1994 with the Cabinet.

Discussion

Four issues confront the General Assembly relating to the taxation of banks. What is the best method to determine fair cash value? What is meant by "extraordinary cases"? What is the effect of the new federal interstate branching law on revenues generated by the bank shares tax? Whether the bank shares tax should be replaced with a different tax.

With enactment in 1984 of the multibank holding company law, it can be argued that the fair cash value of Kentucky banks increased since the law created a market for banks outside of the county in which the banks are located. Likewise, it can be argued that the new interstate branching legislation (the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994) will increase the fair cash value of Kentucky banks. However, it can also be argued that if a bank is bought by another bank for more than book value, that doesn't mean all other banks are undervalued. Whether these laws and other factors have rendered the statutory formula inadequate is a matter that merits review. The controversy over the new valuation method between the bankers and the Revenue Cabinet has been put on hold, with the Revenue Cabinet returning to the statutory formula.

It can be argued that when state and federal laws change the markets for banks and increase their values, an extraordinary case is created and the Cabinet can use other recognized criteria, in accordance with the statute, to determine fair cash value. One of the arguments against the Cabinet's interpretation of the extraordinary case provision, which was enacted in 1984 after a 1983 Supreme Court decision, is that the enactment was an effort by a part-time legislature to provide a full-time executive branch agency with the ability to act quickly between legislative sessions in response to any future court decisions

that create uncertainty and adversely affect state and local revenues. The Revenue Cabinet acted, not in response to a court decision that required immediate action, but rather in reaction to its own assessment of the adequacy of the statutory formula. The Cabinet presented legislation to the 1994 Session, which seems to be the proper procedure to change a statutory formula, unless there is an "extraordinary case" that requires action before the legislature convenes. Upon failure to obtain relief from the General Assembly, there remains a remedy in the courts if one believes the statutory formula violates Section 172 of the Constitution of Kentucky.

A third issue is whether Kentucky will lose revenues from the bank shares tax when some Kentucky banks become branches of the out-of-state banks, if the General Assembly decides not to opt out of the new federal interstate branching law. The largest Kentucky banks are already owned by out-of-state banks. The federal Act creates the potential for more Kentucky banks to become branches of out-of-state banks and will mean the shares of Kentucky bank stock will become shares of some out-of-state bank stock. Decreasing the number of shares of stock subject to Kentucky's bank shares tax reduces revenues to the state and local governments. The federal Act says first that the Act is not to be so construed as to prevent a state or its political subdivision from applying any bank tax to the extent such tax or tax method is otherwise permissible by or under the Constitution of the United States or other federal law. It then provides that a proportionate amount of the value of the shares of the out-of-state bank may be subject to any bank shares tax imposed by the host state or its political subdivisions. This means the Kentucky General Assembly may need to enact legislation to address the bank shares tax issue, to ensure that the state and local governments do not lose any revenues. That may be a difficult task, since it involves corporations operating in more than one state.

Just as the 1900 legislature decided that the answer was to impose an entirely new tax, the 1996 General Assembly may decide that rather than tinker again with the bank shares tax it might be better to find a new way of taxing banks that recognizes the multistate operation of banks, that is flexible to meet the changing business of banking, and that taxes banks rather than the intangible property owned by shareholders. According to a 1988 survey by the Advisory Commission on Intergovernmental Relations and the National Association of Tax Administrators, only seven states imposed the bank shares tax: Indiana, Kentucky, Louisiana, Mississippi, New Hampshire, Pennsylvania, and Rhode Island. Of those seven states, only Kentucky and Pennsylvania relied exclusively on the bank shares tax. For example, Indiana also imposed a tax on net income and on gross receipts, while Louisiana also imposed a franchise tax and a net income tax. According to the survey, 36 states imposed a franchise tax, 19 states taxed net income, 4 states taxed gross receipts, and 8 states imposed other taxes. Thirteen states imposed more than one of the taxes. The survey shows that while Kentucky has retained the bank shares tax, the majority of states tax the net income of banks, either by a net income tax or a franchise tax measured by net income.

There are different methods of taxing the income of banks and each presents its own problems. One method is to tax all banks domiciled in the state, regardless of where the income is earned, but not tax out-of-state banks. Another method is to measure the income of a multistate bank that is earned in Kentucky and apply an apportionment

formula. A third method is to tax the entire net income of a domicilary bank but allow a credit for taxes paid to other states and apply an apportionment formula to out-of-state banks.

AUTHORIZATION OF BANKS TO ENGAGE IN INSURANCE ACTIVITIES

Prepared by Greg Freedman

Issue

Should statutory authorization for banks to engage in insurance activities be expanded?

Background

The issue of banks selling insurance is a complicated one that changes with each new court decision, state legislative enactment, and action by state and federal regulatory authorities. While there are similarities in the regulation of banks and insurance companies--each must be chartered, meet capital and solvency requirements, and comply with restrictions on investments, and each is subject to government examination--there is a distinct difference in how the two industries are regulated. The dual banking system permits banks to be either state-chartered or nationally chartered. Each system, state and federal, imposes its own regulations and statutes, which don't necessarily coincide. Insurance, on the other hand, is subject to a system of state regulation. When one looks beyond how the industries are regulated, one can see similarities in the industries, in that banks and insurance companies are really just financial intermediaries. Despite any similarities, there exist strong arguments on either side of the issue regarding the extent to which the two industries should be integrated.

The powers of state-chartered banks are established by state laws. As of April 17, 1995, thirty states permit state chartered banks to engage in insurance brokerage, either through direct authorization or state statutes that grant state banks parity with national bank powers. States such as Washington and Kansas restrict this activity to towns with populations of less than 5000, while Tennessee and Nebraska prohibit it in towns of more than 200,000. Of the thirty states in which such activity is allowed, two states allow it only through a subsidiary (Alabama and Arizona) and eight allow insurance underwriting (Alaska, Arizona, Delaware, Florida, Massachusetts, New Jersey, North Carolina, and South Dakota). However, the Federal Deposit Insurance Corporation Improvement Act of 1991 prohibits banks from underwriting insurance, except for the eight banks that were already authorized under state laws. In Kentucky, KRS 287.030(4) provides that no person who owns or acquires more than one-half the capital stock of a bank shall act as insurance agent or broker *except as to credit life or health insurance and insurance of the interest of a real property mortgagee in mortgaged property, other than title insurance.* This provision has been effective since 1972. KRS 287.020(3) gives the Commissioner of the Department of Financial Institutions the discretion to authorize state chartered banks to engage in any banking activity in which they could engage if they were nationally-chartered banks. The statute provides that "this section shall not apply to activities prohibited under Subtitle 9 of KRS Chapter 304." Subtitle 9 of the insurance code contains the provisions on the licensing of insurance agents. The discretion provided for in

this section has been in effect since 1970. The insurance exception has been effective since 1992.

National banks are subject to federal laws and regulations. It is a 1916 federal law that is the source of a great deal of litigation concerning the limits of national banks' power to sell insurance. In 1916 Congress enacted Section 92 of Title 12, which, among other things, allowed national banks doing business in a community of 5000 or fewer residents to act as the agent for any insurance company authorized to do business in the state in which the bank was located. There had been some question as to whether Congress repealed this section in 1918, however, in 1993 the U.S. Supreme Court settled the issue, when it held that the section was not repealed and still exists. *U.S. National Bank of Oregon v. Independent Insurance Agents of America, 113. S.Ct. 2173 (1993).* Therefore, federal law authorizes national banks in towns of 5000 or fewer persons to act as agent for an authorized insurer. The case law over this federal statute is complicated and cannot be fairly addressed in this paper. The decisions vary in the different appellate court circuits. The second circuit held in 1992 that Section 92 prohibited national banks located and doing business in towns of over 5000 inhabitants from engaging in title insurance agency business. The fifth circuit held in 1968 that national banks had no power to act as insurance agents in towns of more than 5000 inhabitants. The D.C. circuit in 1993 upheld a 1986 Comptroller of the Currency ruling that permits the branch bank of a national bank located in a community with a population of 5000 or less to sell insurance to customers located anywhere in the nation even though its principal office is located in a town with a population in excess of 5000. In January 1995, the eleventh circuit held that Section 92 does not preempt a state law that prohibits a subsidiary of a bank holding company from selling insurance. The court ruled that, in light of the McCarran Ferguson Act that prohibits an Act of Congress from superseding any state insurance law, unless the federal law specifically relates to the business of insurance, Section 92 does not specifically relate to the business of insurance and does not preempt the Florida insurance statute. However, the sixth circuit in 1994 held that Kentucky's statute, KRS 287.030(4), which prohibits banks from selling insurance except as noted above, was not an insurance statute and therefore not saved from preemption by McCarran. This seems to mean that the Kentucky Department of Insurance may not deny an application by national banks to be licensed as insurance agents. The court, however, did not say whether other Kentucky laws might prohibit licensure. There is also litigation over a percentage lease agreement between an insurance agency and national bank which are both located in Kentucky. The agreement is being challenged on the grounds of violation of a Kentucky insurance statute that prohibits commission splitting. And it should also be noted that the U.S. Supreme Court in January, 1995, upheld the ruling of the Comptroller of the Currency allowing national banks to sell annuities nationwide, and held that annuities are not insurance for the purposes of Section 92.

Discussion

Each side can make legitimate arguments regarding the effect on competition if banks are granted broad insurance authority. First, it can be argued that banks already have a system of banks and branches in place from which they can compete with

independent insurance agents and sell insurance in a more cost-effective manner, to the benefit of the consumer. It can also be argued, however, that this situation would amount to unfair competition because of access by banks to financial records of customers and tie-in sales. Even if banks are specifically forbidden from requiring purchase from them of insurance as the price for receiving a loan approval, the loan applicant might still feel it was expected. Second, it is alleged that industry concentration will occur which will lessen competition as banks gain more power and wealth through insurance sales. That allegation is countered by those who say the insurance industry is far more concentrated than the banking industry, and that it is insurance companies, not banks, that are exempt from anti-trust laws. Third, banks engaging in insurance activities has been objected to on the grounds of increased risk. That objection is countered with arguments that diversification decreases risk and that appropriate standards could be adopted for underwriting insurance, not unlike those that banks have complied with in underwriting loans.

The safety and soundness of banks and insurance companies is a primary concern of state legislators and regulators. It is clear that the General Assembly may permit state-chartered banks to sell insurance, and just as clear that they have not, except as noted in KRS 287.030(4). In determining to what extent the two industries should be integrated, the General Assembly must weigh the legitimate arguments of opponents and proponents of more integration, while being ever mindful of the safety and soundness issues. It will not benefit Kentucky residents in the long run to increase insurance competition while adversely affecting the safety and soundness of either the banking or insurance industries. Separate from the banks versus insurance industry issue is the state-chartered bank versus nationally-chartered bank issue. The 1916 federal law illustrates how the dual banking system places state legislatures in difficult situations as they enact legislation to define powers of state-chartered banks, while actions beyond their control at the federal level define the powers of nationally-chartered banks doing business in their states in competition with their state-chartered banks. The General Assembly must temper its acts with the knowledge that actions at the federal level and by courts that interpret federal banking statutes and rules could leave state-chartered banks at a competitive disadvantage. Even though the federal courts have issued opinions that restrict state legislative action relating to national banks, there are still gray areas that could be addressed. Should other laws be enacted that could prohibit the licensure of national banks as insurance agents? Should laws be enacted that restrict the sale of annuities by banks? Should legislation be enacted regulating the lease of office space in banks by insurance agencies?

INTERSTATE BANKING AND BRANCHING

Prepared by Greg Freedman

Issue

Should the General Assembly allow interstate branching to take effect in Kentucky or enact legislation to prohibit such activity?

Background

On September 29, 1994, the U.S. Congress enacted the Riegle-Neal Interstate Banking and Branching Efficiency Act. The Act will require the Kentucky General Assembly to make several decisions during the upcoming 1996 Session.

Interstate Banking. The federal Act allows for bank holding companies to acquire banks in any state one year after enactment. The acquired bank must have been in existence for up to 5 years. The acquisition will not be approved if it will result in the bank controlling more than ten percent of total deposits of insured depository institutions in the United States or thirty percent or more of the deposits of insured depository institutions in any state.

Interstate Bank Mergers. Beginning on June 1, 1997, bank holding companies may consolidate two or more subsidiary banks into a single bank with out-of-state branches, unless a state has opted out of interstate branching prior to that date. Also, beginning on June 1, 1997, a bank may engage in a merger transaction with an out-of-state bank and convert any offices into branches of the resulting bank, or may acquire a branch and not the rest of the bank, unless a state has opted out of interstate branching.

De Novo Branches. A bank may establish and operate a branch bank in a state other than the bank's home state if the state in which it seeks to establish a de novo branch expressly permits by law all out-of-state banks to establish de novo branches in the state. A de novo branch is a branch that is originally established by the bank as a branch and does not become a branch due to acquisition of a bank or branch or through conversion, merger, or consolidation.

Branching by Foreign Banks. Foreign banks may branch interstate only by acquisition, unless the state allows de novo branching for all banks.

Discussion

The new federal law allows states to opt out of interstate *branching*; however, there is no option on the interstate *banking* provision. On and after September 29, 1995, the Federal Reserve Board will have the power to approve an application of an adequately

capitalized and managed bank holding company to acquire a bank, no matter where the bank is located and even if the state in which the bank to be acquired prohibits such a transaction. Kentucky has since July 13, 1984, allowed a bank holding company in another state to acquire a Kentucky bank, if the state in which the acquiring bank is located allows Kentucky bank holding companies to acquire banks in that state. Although states may not opt out of the interstate banking provision, states do have options on the age of acquired banks and concentration limits. The federal law allows states to set the minimum age of an acquired bank, as long as it does not exceed 5 years. Kentucky has required since 1984 that an acquired bank be at least 5 years old (KRS 287.900(2)); therefore, current Kentucky law conforms to the new federal law. The federal law also prohibits acquisition of a bank if it would result in the acquiring bank controlling 30 percent or more of the total deposits of insured depository institutions in a state. However, states may raise or lower the limit, as long as it does not discriminate against out-of-state banks, bank holding companies, or subsidiaries. Kentucky has a concentration limit of 15 percent (KRS 287.900(3))and conforms with the federal law.

The 1996 Kentucky General Assembly does have the authority under the new federal law to opt out of the interstate branching provisions. This option may be exercised by enactment of a law between September 29, 1994 and June 1, 1997 that applies equally to all out-of-state banks. If Kentucky opts out of interstate branching, out-of-state banks would be prevented from merging with Kentucky banks. However, enactment of such legislation would also prohibit Kentucky banks from merging with out-of-state banks. If the Kentucky General Assembly takes no action, interstate branching will be allowed in the state effective June 1, 1997. The limits on the age of acquired banks and the concentration of deposits that apply to interstate banking also apply to interstate branching. The new federal law gives states the option to allow interstate branching prior to June 1, 1997, by enactment of legislation that applies equally to all out-of-state banks and expressly permits interstate mergers with out-of-state banks. As of June 1, 1995, five states have acted to opt in early under the provisions of the new federal law. Those states and the effective dates of interstate branching are: Idaho (July 1, 1995), Maryland (September 29, 1995), Oregon (February 27, 1995), Utah (June 1, 1995), and Virginia (July 1, 1995). States that allowed interstate branching prior to the new federal law and need to adjust their laws to conform to the federal law are: Alaska, New York, and North Carolina.

The new federal law allows federal bank regulators to approve an application by a bank to establish and operate a de novo branch in a state in which the bank does not maintain a branch, if the state in which the branch is to be located has enacted legislation expressly allowing out-of-state banks to establish de novo branches. This means the Kentucky General Assembly will have to enact specific legislation before an out-of-state bank which has no presence in Kentucky may establish a branch in Kentucky.

In summary, the 1996 Kentucky General Assembly faces several decisions concerning interstate banking and branching. Kentucky's law seems to conform with the new federal law on interstate banking, and it should be remembered that there is no authority for a state to opt out of interstate banking. However, the General Assembly could act to decrease the age limits on acquired banks and could raise or lower the

concentration of deposits limits. As to interstate branching, the 1996 Kentucky General Assembly does have the option to prohibit interstate branching in Kentucky. If the General Assembly does not enact legislation prior to June 1, 1997 that expressly prohibits interstate mergers, effective June 1, 1997 interstate branching will be allowed in Kentucky. However, de novo branching will not be allowed unless legislation expressly allowing it is enacted. Interstate mergers prior to June 1, 1997 may be authorized by enactment of legislation that expressly allows such mergers at a specific date.

1994 HEALTH INSURANCE REFORMS

Prepared by Greg Freedman

Issue

Should the General Assembly amend the 1994 health insurance reforms?

Background

The 1994 Kentucky General Assembly enacted HB 250, which is a comprehensive approach to improving health care for Kentuckians. The part of the bill that contains insurance reforms was written to take effect on July 15, 1995, which is one year after the effective date of the law. This allowed all persons a full year's notice to prepare for the changes.

When a policy is issued or renewed after July 15, 1995, Kentucky residents select one of four **standard plans** designed by the Kentucky Health Policy Board. The plans are called Enhanced, Standard, Economy, and Budget. Each of the four plans has two levels of cost-sharing and is offered as an indemnity plan and as a managed care plan. All plans are accessible to Kentucky residents who can pay the premium because they are **guaranteed issued**. Also, the plans are **guaranteed renewable**, unless the insured does not pay the premium, or commits fraud, or the insurer stops doing business in Kentucky. The plans may limit or exclude coverage for a **pre-existing condition** for no more than the first 6 months of a policy. However, if a person drops coverage or the insurer cancels or refuses to renew and the person gets a new policy within 60 days after the prior coverage ended, the **portability** provision requires the time the insured was covered under the prior policy to be credited against any pre-existing condition period under the new policy. Policies for individuals, for groups of 100 or less, and all policies issued to members of the Alliance use a **modified community rating** method that restricts the factors used in setting rates. Modified community rating does not apply to policies covering groups of more than 100 persons. However, as to individuals, small groups, and Alliance members, when a health insurer figures rates, it may not consider a person's health condition in determining the rates. Insurers may use age, where the person lives, family composition, and benefit plan designs as rating factors.

Individuals and small groups have the choice to purchase insurance through the **Kentucky Health Purchasing Alliance**. The Alliance is not an insurance company. It negotiates good rates for Alliance members with insurers and HMO's. It does not eliminate the use of agents, because the Alliance and the health plans are specifically authorized to use the services of a health insurance agent. Whereas the administrative costs on an individual or small group policy may be 30 to 40 percent of the premium, the Alliance is restricted to an administrative cost of 1.5 percent, which may be increased only to 3 percent if the Health Policy Board approves. By January 1, 1996, it is anticipated that at least 300,000 persons will have health insurance coverage through the Alliance. This

estimate is based on the law's requirement that employees of the state, universities, and local governments must be members of the Alliance. In addition, the Alliance is open to any individual and to groups of 100 or less who voluntarily choose to become members.

Discussion

The insurance reforms were enacted to increase ensure that Kentuckians can easily access equitably-priced, cost-effective health plans. The objectives of the reforms are that:

- Kentuckians are able to obtain and maintain equitably-priced coverage, regardless of health, occupational, or other status.
- Kentuckians are provided a meaningful choice of private health plans through a structure that is easy to understand and simple to use.
- Competition between plans is based on price, quality and health outcomes, service and convenience, but not based on risk selection.
- Individuals can readily compare the relative merits and costs of each health plan.
- A health insurance system is established with an efficient administrative structure and cost effective health plans that can readily and efficiently achieve universal coverage, if and when the necessary mandates and subsidies are enacted at the state or federal level.

Any assessment of these objectives by the 1996 General Assembly will be limited by the extent to which the insurance reforms are implemented. Because the reforms become applicable as new policies are issued and older policies are renewed, it will take time before the reforms are fully implemented and the objectives are given the opportunity to be achieved. This became an even more important consideration when the Health Policy Board, in April, 1995, authorized health insurers to extend their renewal dates, which delayed full implementation of the reforms. Another important factor is the decision by the Executive Branch to issue health insurance contracts for state employees throughout calendar year 1995 rather than until July 15, 1995. That decision deprived the Alliance of approximately 209,000 members during its first six months of operation. Any concerns raised about the effectiveness of the reforms will need to be balanced by the implementation process and the scope of implementation.

The 1996 General Assembly may confront the same complaints that faced the 1994 General Assembly about the necessity of the reforms, as opposed to their effectiveness. These complaints must be balanced by the needs of health insurers for a level playing field and the needs of insureds for more certainty in their lives. Some health insurers may argue that risk selection is necessary and that they cannot compete based solely on price. Others can argue that health insurers who, as good corporate citizens, operate throughout the Commonwealth and try to serve the entire population are at a disadvantage compared to those health insurers who select certain areas of the state, or only good risks, and leave the

state or refuse renewals when the bad risks increase. Health insurers deserve a level playing field. Some persons may argue that they have no problem finding coverage, that the majority of Kentuckians have coverage, that the number of uninsureds includes those who choose not to buy coverage, and that reform is therefore not necessary. It can also be argued, however, that some persons with insurance are not happy with their coverage, or feel it is inadequate but that they cannot afford adequate coverage, or find themselves locked into inadequate coverage because of a pre-existing condition. In addition, because of the fragility of human life, randomness of accidents, and intentional infliction of personal injury in today's society, there is never certainty that a person's health status today will be the same tomorrow.

STACKING MOTOR VEHICLE LIABILITY COVERAGE

Prepared by Judy L. Fritz

Issue

Should the General Assembly permit uninsured or underinsured motorists liability coverage for a motor vehicle to be stacked?

Background

Since 1970, uninsured and underinsured motorists' policies have applied to the person, not to the car. The Supreme Court of Kentucky has held that where the insured has paid multiple premiums, the insured is entitled to stack multiple uninsured motorist coverages. This holds true regardless of whether the insured has a single policy covering multiple vehicles or multiple policies. Bills have been introduced in recent sessions to prohibit the stacking of uninsured and underinsured motor vehicle insurance coverages, but none has passed.

Discussion

Opponents of anti-stacking measures state that such legislation would move personal protection coverage from the individual and place it on the car. Additionally, they believe that consumers would have to pay for multiple policies on their cars to retain the same coverage they now have with one policy on the drivers; thus consumers would get less coverage for their money.

Proponents of anti-stacking legislation state that insurance companies can not control their liability because they do not know when the policies will be stacked. They believe that without anti-stacking legislation insurers will be forced to raise the cost of uninsured and underinsured premiums.

ECONOMIC DEVELOPMENT

APPLIED AND BASIC RESEARCH PROGRAM

Prepared by Gordon Mullins

Issue

Should the General Assembly amend the applied and basic research infrastructure program provided in KRS 154.35-010 to 154.35-055?

Background

The 1994 General Assembly passed the Kentucky Applied and Basic Research Infrastructure Act, which had as its goal the establishment of a set of programs to link the research needs of Kentucky businesses with the research expertise of state universities. To do so, the bill authorized the Kentucky Science and Technology Council, Inc. to establish the Kentucky Research and Development Infrastructure, in accordance with guidelines set forth by the Cabinet for Economic Development, which would contract with two universities to conduct basic research, and other universities to establish up to six applied research centers. Businesses needing basic or applied research would contract with one of these centers to conduct this research. Financial assistance to businesses could be provided with money coming from a fee paid by beneficiaries of state economic development incentive packages and other state appropriations or private gifts the fund may receive.

Discussion

Proponents of this legislation feel that small to medium-size businesses typically lack in-house research capabilities that are often needed to advance their product or its manufacture and delivery. Universities, which by definition are dedicated to research, house a tremendous amount of research expertise and ability, and are capable of helping businesses to solve their basic and applied research needs. This legislation helps to establish a needed link between the research needs of business and the research expertise of universities.

Some questions remain to be answered about the effectiveness of this approach. Is the amount of funding provided adequate? Will academicians, in fact, choose to participate in this type of research? Will businesses find that universities provide the optimal environment for solutions to their research needs? Without question, according to the Kentucky Science and Technology Council, Inc., there is a need for more applied research. Experts in this country, as well as Europe, point to the economic successes of regions that support research.

In May, 1995, the Council sponsored a study trip to Germany, the Netherlands and Denmark in order to learn how these industrialized nations organize for and deliver strategic research and technology to industry. The study group, sponsored in part by the German Marshall Fund of the United States, was comprised of representatives from government, education and the private sector. It is anticipated that from this trip the Council may gain insight into how best to implement the applied research infrastructure program envisioned by the Kentucky Applied and Basic Research Infrastructure Act of 1994, and make recommendations, if necessary, to the Interim Joint Committee on Economic Development and Tourism for consideration by the 1996 General Assembly.

SECONDARY WOOD PRODUCTS INDUSTRIES

Prepared by Gordon Mullins

Issue

Should the General Assembly establish additional secondary wood products hubs to form a statewide network to support development of secondary wood products industries in Kentucky?

Background

House Bill 561, enacted by the 1994 General Assembly, creates and establishes the Kentucky Wood Products Competitiveness Corporation for the purpose of promoting, enhancing, and developing the Commonwealth's secondary wood products industries. The corporation is mandated to develop workforce training plans, review and make recommendations to the Cabinet for Economic Development regarding proposals to establish business networks in the value-added processing of raw wood products, advise the Natural Resources and Environmental Protection Cabinet and the Labor Cabinet on regulatory matters which impact the secondary wood products industry, advise the Finance and Administration Cabinet regarding procurement of Kentucky-made secondary wood products by state agencies, establish benchmarks to evaluate workforce training and technology transfer programs as they relate to the secondary wood products industry, work with the Kentucky Tourism Cabinet to establish showrooms for Kentucky-made furniture and other wood products, contract with the University of Kentucky College of Agriculture for the operation of the Quicksand Wood Utilization Center as a hub for the expansion of the secondary wood products industry in Kentucky, and make recommendations to the Kentucky General Assembly, by the 1996 Regular Session, regarding the expansion of industrial hubs at two other locations in the state.

In 1994, the Interim Joint Committee on Economic Development designated the wood products industry as an emerging industry deserving special attention and support, because the industry, if expanded, could create a significant number of jobs in regions of the state undergoing traumatic economic transition, by adding value to one of Kentucky's most abundant renewable resources, the Appalachian hardwood forests. Currently, much of the raw timber cut from these forests is shipped from Kentucky to foreign countries and to several surrounding states, including Tennessee, Indiana, and Virginia, for the purpose of processing it and manufacturing value-added products. Simply stated, the higher income jobs in the timber industry are those jobs adding value to the raw product. For that reason, a state such as Indiana produces less board foot of unprocessed timber than Kentucky, but sustains a wood products industry earning several billion dollars more than wood earns for Kentucky.

Discussion

The secondary wood products development programs set forth in House Bill 561 have been put on a fast-track by the Cabinet for Economic Development and incorporated in the *Kentucky Strategic Plan for Economic Development,*[10] including *Strategy 5.1*, to promote sustainable management of Kentucky's renewable natural resources, especially agriculture and forestry. There are four tactics specifically related to the wood products industry. Critical to the success of these programs is the industrial training and technology hub at Quicksand Wood Utilization Center, located in Breathitt County.

The industry hub at Quicksand was selected because of the long history and availability of wood products technology and resources at the Quicksand site. Once the hub is operational, training programs, technology development, and transfer activities will be available to Kentucky wood products industries and businesses. Kentucky is fortunate to have substantial support for these efforts through the continuing work of the Kentucky Department of Natural Resources, Division of Forestry, the University of Kentucky Department of Forestry, the Center for Economic Development at Eastern Kentucky University, the Kentucky Wood Manufacturers' Network, and the continuing efforts in support of the forest industry by the Kentucky Forest Industries Association.

If the Quicksand hub is activated in 1995, it is conceivable that Kentucky's wood products industries may require support of a second industrial training and support hub at a location in West Kentucky, or in the Louisville area, where many of Kentucky's secondary wood products manufacturers are located. Without question, the wood products program will continue to require the careful oversight of the General Assembly, as the programs envisioned in House Bill 561 become reality.

At the April, 1995, meeting of the Interim Joint Committee of Economic Development and Tourism, representatives of the Kentucky Wood Products Competitiveness Corporation presented the committee with a progress report on implementation of HB 561. The chairman and vice-chairman of the corporation reported that an executive director had been employed, and that the corporation's board had begun discussions on the corporation's mission statement, goals and objectives with representatives of the wood products industry. The chairman stated that the corporation would not make any firm decision regarding utilization of Quicksand, as well as future hub sites, until after complete consultation with representatives of the private sector. It is anticipated that the corporation's board will make recommendations to the Interim Joint Committee on Economic Development and Tourism by October, 1995, for consideration by the 1996 General Assembly.

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[10]The Kentucky Strategic Plan for Economic Development is the official guide to develop and implement actions by Kentucky state government deemed most appropriate to improving the overall economic health and prosperity of Kentucky. Strategies are broad areas of emphasis deemed to have greatest importance in overcoming weaknesses in the state's economy, as well as capitalizing on its strengths. Tactics are specific actions to be taken in support of these strategies.

VENTURE CAPITAL

Prepared by Gordon Mullins

Issue

Should the General Assembly repeal KRS 154.20-300 to 154.20-390, regarding the Commonwealth Venture Fund, and authorize the creation of a venture capital fund under the direction and management of the private sector?

Background

The Commonwealth Venture Fund was authorized by the 1988 Regular Session of the Kentucky General Assembly, with an implementation schedule for 1990 and 1991. During the 1990-91 Interim, the Interim Joint Committee on Economic Development received written and verbal testimony from Massey Burch Investment Group, which was the managing firm for the Commonwealth Venture Fund. The Committee also received testimony from CID Venture Partners in Indiana, the Palmetto Seed Fund of South Carolina, the Counsel for Community Development from Massachusetts, and others involved in drafting the Commonwealth Venture Fund legislation in 1988. The reasons for soliciting this testimony were flaws in the 1988 legislation that have made it virtually impossible to implement the Commonwealth Venture Fund. Primarily, the consensus was that the law permitted too much involvement by public officials, too little opportunity for follow-on investments of the fund, and included too many restrictions regarding the use of the fund, e.g., mandated expenditures for agricultural ventures. Changes recommended included, among other things, removal of the secretaries of the Finance and Administration, the Commerce, and the Revenue cabinets from the panel establishing the fund and selecting the management firm. The panel had been given the power to hire or fire the management firm and to establish guidelines and policies for investments by the fund. Additionally, the staff of the Finance and Administration and the Commerce cabinets were to serve as staff to the panel.

During the 1992 Regular Session, recommendations to remove the cabinet secretaries from the panel and otherwise limit their influence were not incorporated in the statutes.

During the 1994 Regular Session, a minor change to the definitions section of the Capital Venture Fund statutes was enacted; however, the provisions regarding involvement by public officials remain unchanged.

Discussion

The Commonwealth Venture Fund (CVF) has not been funded, nor will it be, according to most venture fund experts, as long as the state government maintains any

semblance of control over the fund. Private investors are very skeptical of government's ability to properly manage the funds. Another problem is inadequate deal flow. According to some experts, Kentucky would not provide sufficient number of ventures within a year's time to justify the fund's requirement to give preference to Kentucky businesses.

Regardless of the reasons for inactivation of the CVF, report after report by responsible development groups agrees that potential economic development activities in Kentucky would be greatly enhanced with accessibility to venture capital. Reports by the Kentucky Science and Technology Council, Inc. show that the lack of all forms of risk capital stifles economic growth, and prevents many solid ideas created by promising Kentucky entrepreneurs from becoming new enterprises. The question is: how can risk capital formation and investments in Kentucky businesses be encouraged?

Economic Innovation International of Boston, Massachusetts, reports that experiences in other states show that venture or "seed capital solutions cannot (a) operate in 'grants economy', (b) be structured as a public or quasi-public agency, (c) be undercapitalized, and (d) invest without other experienced partners". EII cites the Ben Franklin Seed Venture Capital Fund, the Connecticut Seed Venture Capital Fund, and The Palmetto Seed Capital Fund of South Carolina, as examples of successful funds.

Other useful models might be the Kansas Venture Capital Tax Credit and the Louisiana Capital Companies Tax Credit. Venture capital companies agreeing to invest their funds in companies in Kansas are given a tax credit equal to 25% of their investment. The credit can be carried forward until fully used, and it can be sold. In 1986 there were no venture capital funds in Kansas; in 1988 there were 12, with a total investment of $27.5 million, $14.5 million of which was invested in Kansas firms.

Under Strategy 2.2 of the *Kentucky Strategic Plan for Economic Development*,[11] Tactic 2.2.1 addresses this very issue. A tactic team was appointed by the Kentucky Economic Development Partnership Board of Directors. Team members are individuals familiar with raising venture capital in Kentucky. Meetings have been held on a regular basis since July, 1994. The team first examined the CVF legislation and concluded that the current statutory authority is not adequate to meet the goals and objectives set forth by the Partnership Board. In looking at what other states have done, the tactic team focused attention on West Virginia legislation, where tax credits are passed to investors through state certified capital corporations. Although they are not suggesting duplicating the West Virginia program, the team's recommendation to the Partnership is:

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[11]The Kentucky Strategic Plan for Economic Development is the official guide to develop and implement actions by Kentucky state government deemed most appropriate to improving the overall economic health and prosperity of Kentucky. Strategies are broad areas of emphasis deemed to have greatest importance in overcoming weaknesses in the state's economy, as well as capitalizing on its strengths. Tactics are specific actions to be taken in support of these strategies.

Repeal KRS 154.20-300 - KRS 154.20-390 and create a new section of KRS 154 to establish, in place of a state developed venture fund, a number of private venture funds (the Funds).

Each Fund will be managed by a Kentucky venture capital company with demonstrated ability and expertise in venture fund management. Each Fund and its respective managing Company will be certified by the Kentucky Economic Development Finance Authority after having raised a minimum capital base of $1 million.

Investors in each fund will be entitled to receive a 40% credit against liabilities of certain Kentucky taxes. The maximum of all tax credits approved, in the aggregate, will be $20 million, with the maximum credits to any one fund equal to $2 million.

State involvement will be for oversight only, and all fund raising will be left to the private sector, which is better suited to the risks associated with the operation of venture funds.

A final recommendation will be made by the Partnership to the Interim Joint Committee on Economic Development and Tourism after July, 1995, for consideration by the 1996 Session of the Kentucky General Assembly.

GLOBAL MARKET DEVELOPMENT

Prepared by Gordon Mullins

Issue

Should the General Assembly restructure the international trade operations of state government and establish state export trade programs to support Kentucky businesses in their efforts to develop new markets for Kentucky-made goods and services?

Background

Throughout the last quarter of this century, it has been the policy of Kentucky state government administrations to encourage economic development through investments in Kentucky's economy by foreign-owned companies, and to encourage Kentucky-based companies to sell goods and services in foreign markets. According to the 1990 *Kentucky Cabinet for Economic Development Reference Guide*, the long-range marketing plan of the Office of International Marketing was "to maintain and improve its (*Kentucky's*) position in the top ten states for attracting Japanese business..." Simply stated, the primary goal of this office was to recruit foreign, primarily Japanese, industrial development to Kentucky. On the export side, the Cabinet for Economic Development stated in its 1990 Marketing Plan that the cabinet's Office of International Marketing was developing services for export market development. However, in reality, market development never received the high degree of support given industrial recruitment.

With enactment of House Bill 89 by the 1992 Regular Session of the Kentucky General Assembly, a legislative mandate was given to initiate new programs deemed appropriate by the Kentucky Economic Development Partnership to enhance the sale of Kentucky-made goods and services in foreign markets, including: "[a] Kentucky export authority to utilize the services of the Kentucky World Trade Center, university export trade programs, and export programs provided by other agencies within a context to provide financial assistance to Kentucky exporters...."

Under the current state administration in Kentucky, the Coal Marketing and Export Council was established by Executive Order 92-387, issued on April 17, 1992, as amended by Executive Order 92-1147, issued on October 27, 1992, and confirmed by the Kentucky General Assembly by enactment of Senate Bill 74 of the 1994 Regular Session of the Kentucky General Assembly. The Coal Marketing and Export Council was created out of a merger of the Governor's Office for Coal and Energy Policy and the Kentucky Export Council. The council is attached to the Cabinet for Economic Development.

Within the Cabinet for Economic Development, as now constituted, the International Trade Office is located within the Department of Community Development, and the Far East Office, located in Tokyo, and the European Office, located in Brussels,

Belgium, are attached to the Department of Job Development. According to information supplied by the cabinet, the International Trade Office offers the following services: export consulting, export marketing, and education and training.

In addition to the cabinet's trade development, other professionals and agencies are engaged in export trade support services, including the Kentucky World Trade Center, the Louisville and Jefferson County Economic Development Agency, the University of Kentucky Center for Agricultural Export Development, the Kentucky District Export Council, the Southern Kentucky Economic Development Corporation, the Bluegrass International Trade Association, the Northern Kentucky International Trade Association, the Kentuckiana World Commerce Council, and the International Trade Office of the Kentucky Cabinet for Economic Development. The question is how best to utilize these resources within the context of state-mandated economic development activities.

Discussion

The importance of export trade development to the state's economy can not be overstated. The *Strategic Plan for Kentucky Export Development*, prepared by the Kentucky District Export Council (1991), reports that "from 1987 to 1990, Kentucky's 60% increase in exports actually surpassed the U.S. average of 55%." The council's report continues to stress the real importance of state-generated exports by noting that "[i]n 1989, the last year for which export-related employment data is available, about 74,500 workers in Kentucky owed their jobs to exports of manufactured goods. Of these, 34,500 were manufacturing jobs directly supported by export sales, while another 40,000 were in non-manufacturing industries indirectly sustained by manufacturing for export."

In July 1990, the Kentucky World Trade Center published "An Assessment of the Export Potential of Kentucky Industries," a report prepared by the University of Kentucky's College of Business and Economics. On the basis of that report, the Kentucky World Trade Council reported that 50% of Kentucky's manufacturing base has real export potential, especially in machinery, electronics, medical products, wood products and chemicals. As the North American Free Trade Agreement (NAFTA) and the General Agreement on Tariffs and Trade (GATT) are implemented, the promise of new jobs and new economic growth through expansion of new markets requires an aggressive response by government and private business, to ensure unimpeded expansion of exportable goods and services produced by Kentucky businesses.

One of the five economic development goals established by the 1992 General Assembly in House Bill 89 addresses the reality of the impact that global competition has had and will continue to have on Kentucky's economic health. It recognizes the fact that major competitors of Kentucky businesses are global. Regardless of the point of sales, if Kentucky businesses are to succeed, and in turn create more jobs and higher wages, the goods and services produced in Kentucky must meet global standards of quality, efficiency and price, and new markets must be acquired in which Kentucky products might compete. It is assumed that if Kentucky products meet global quality and efficiency standards, they will find a market. Sometimes quality products do not make it in the global market,

however, especially products of small and medium-sized businesses, since they do not have the expertise to market goods or services internationally.

Within the context of international trade, the state economic development planning process underway by the Cabinet for Economic Development is addressing the following strategy: *Strategy 3.4- Make Kentucky globally competitive.* Under this strategy there are three tactics being addressed by state government and business leaders: *Tactic 3.4.1- Create a foreign trade and investment office in the Economic Development Cabinet, Tactic 3.4.2- Offer seminars for Kentucky Firms in doing business overseas, and Tactic 3.4.3- Encourage and support industry-based consortia for export development.* The tactical team for Tactic 3.4.1, as set forth in the *Strategic Plan for Economic Development,*[12] has made the following tentative recommendations: to establish an advisory committee to provide input on trade policy development; to develop export financing options and better define the programs by the International Trade Office; to provide counseling to selected industry sectors and businesses located in regions of the state without a trade development entity providing such services; to develop linkages with local agencies capable of providing export-related services without duplicating such services; to provide leadership in the training of local agency personnel whose responsibilities include export-related services; to improve tracking services; and to provide a clearinghouse function.

To say that Kentucky is ahead of the curve would be delusive. Numerous states, including Washington and Illinois, enjoy substantial state financial support, as well as support from the private sector. The Washington State Legislature approved $1.1 million in new funding for state trade development in 1994, to integrate work plans and management of trade between commerce and agriculture; provide an outreach strategy as part of a state rural development initiative; provide for performance-based contracts for the delivery of certain domestic services and overseas market representatives; provide for state paid circuit riders to provide training and support to local businesses; target small and medium-sized enterprises, and stay with them through their first export venture.

Whatever track Kentucky takes concerning export development, achieving success will depend greatly upon continued support from current trade development functionaries and private businesses and industries. The questions raised most often by state business leaders are: What should be the role of state government in export market development? What is the role of the private sector and other trade support groups? How can state government effectively utilize private or other public resources in meeting mandated responsibilities?

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The ultimate question is, is there a role for state government in trade development? On the basis of testimony, state business leaders report that state government has not done enough to help Kentucky businesses gain access to new export markets. Furthermore, they recognize that successful global competition requires more than accessing new markets. Globally competitive companies require flexible production systems capable of maximizing appropriate cutting-edge technologies, managed and operated by a well-trained, world-class workforce capable of implementing world-class production standards. In this regard, cooperative efforts between state government and private enterprise may be in order, to train and retrain the workforce so that these standards are met or exceeded.

CREATING A "SEAMLESS SYSTEM" FOR POST-SECONDARY STUDENTS

Prepared by Mary C. Yaeger

Issue

Should the General Assembly take action to ensure that public post-secondary educational programs offer an effective and efficient method for students to transfer credits and articulate course work among programs and institutions?

Background

The General Assembly has been aware of difficulty post-secondary students have in transferring course work from one public institution to another using credit earned at one institution to meet requirements at another state school. During the 1992 Regular Session the General Assembly passed SJR 36, creating a task force to develop a plan for implementing a common course numbering system for institutions of higher education. During the same session the General Assembly passed HB 171, creating an Interagency Commission on Educational and Job Training Coordination. One of the Commission's mandates is to work to implement programs to provide maximum flexibility for those transferring between post-secondary educational and job training institutions.

Supplemental to these legislative efforts, in 1993, Kentucky was selected to be part of a workforce training initiative sponsored by the National Conference of State Legislatures and Jobs for the Future, Inc. This project, called Investing in People, led to the passage of two pieces of legislation during the 1994 Regular Session of the General Assembly. One of these, SCR 86, requires the Interim Joint Committee on Economic Development to study the workforce training efforts to provide effective programming, including the use of transfer of credits and articulation agreements in public post-secondary programs. Articulation agreements allow students to exchange credits or course work across educational systems without duplication or penalty.

Discussion

Much attention has been given to adult education as an economic development tool to create a globally competitive workforce. American businesses, struggling to create high-performance industries, have stressed the need for high quality, technically skilled, and academically literate workers. Also, the workforce is seeking occupational and career paths that will provide economic relief from the low-paying jobs that we associate with a lack of skills or education. Others, who are unemployed, look for retooling opportunities following layoffs in declining industries and downsizing.

Educational institutions are attempting to meet the increasing expectations of businesses and students. Educators talk about a seamless system in which learning is life-long, existing in a responsive educational system, where individuals can upgrade their skills and advance their educations throughout the various phases of their productive

cycle. One of the methods that increases flexibility for the current and future workforce is the use of articulation agreements and transfer of credit agreements between secondary schools and post-secondary schools, and among post-secondary schools.

The following examples illustrate the need for articulation and credit agreements. A practical nurse with ten years' experience decides that R.N. training would be beneficial to her career advancement, but she does not apply to a community college, since only a fraction of her educational course work will apply to the associate degree requirements. Students who have been in the Tech-Prep program do not want to repeat work they had in high school when they advance to the post-secondary Kentucky-Tech schools. In order to become an office manager, a worker with an associate degree in business administration and management from a community college would like to work toward a bachelor's degree in business, but, in pursuing that goal, she loses credit, as some of her associate degree course hours will not count toward her bachelor's degree. A Kentucky-Tech student with a diploma in electronics technology is advised to go out-of-state to get an associate and bachelor's degree, because in-state schools will not accept his previous course work.

In Kentucky, there may be a particular need for educational systems to collaborate in developing clear pathways for students to make the transition from one level or program to another. While most states offer post-secondary vocational and technical educations through community colleges, Kentucky has two major governance structures: one through the Workforce Development Cabinet and one through the University of Kentucky Community College system. Both award certificates for occupational training, but Kentucky-Tech awards diplomas and the U.K. Community College system awards associate degrees. In addition, the regional universities and the University of Louisville offer associate degree programs.

Since 1992, some progress has been made toward meeting the legislative goals of SJR 36 and HB 171. An agreement on acceptance of community college credits by state universities is forthcoming and the Interagency Commission on Educational and Job Training Coordination has a draft copy of a policy on articulation agreements. There has been progress by individual institutions toward formalizing transfer of credit and articulation agreements with other programs. There has been an increase in awareness of the problems and the need for such agreements.

However, the legislature may be concerned about the scale achieved by these agreements. Do a significant number of institutions and programs have a process to accept students from one program to another? While the community colleges are part of a higher education culture and Kentucky-Tech has a vocational education history, modernization has caused colleges to become more technical in their offerings and vocational/technical schools more academic in their curricula. Do the similarities between the college programs and the Kentucky-Tech programs bring them closer together or do they encourage a competition that makes course transferal more difficult and expenditure of state funds less effective? These issues will be addressed in the SCR 86 report by the Interim Joint Committee on Economic Development.

EDUCATION

HIGHER EDUCATION

Prepared by Ethel Alston

Issue

Should the General Assembly provide additional financial support to higher education?

Background

During the 1980's and early 1990's, the demands on the public institutions of higher education increased dramatically. Growing numbers of students enrolled in colleges and universities amid increasing tuition and student fees, limited financial aid and scholarships, a slow economy and dwindling job prospects.

At the same time, revenue shortfalls demanded that the state impose budget reductions that made it difficult for the universities and colleges to meet their responsibilities. Reductions in institutional budgets, as reported by the Council on Higher Education, greatly impacted general operations and totaled in 1980-82, $27 million, reducing a biennial increase of 23% to 9%; in 1986-88, $16 million, reducing a biennial increase of 19% to 16%; and in 1990-92, $30 million in operating funds and $10 million in debt service, reducing the biennial increase of 25% to 17%. For FY 1992-93, appropriations to the institutions reflected a 5% reduction in the funding base, in accordance with HB 468. In addition, the Governor requested in 1993 that the institutions reserve 2% of the state appropriation for a contingency plan. Approximately $12 million was deducted from institutional budgets for FY 1993-94.

To further illustrate the decreasing proportion of state funding going to higher education, the percentage of the state's general fund allocated to higher education decreased from 20% in 1972 to 14.2% in 1995. Thus, institutions have become dependent on tuition as state support declines. In 1992-93, the state invested in universities and community colleges about $647,000,000, representing 39% of the total revenue. Students paid tuition and fees totaling $261,000,000, representing 16% of the total revenue.

While the Kentucky Education Reform Act of 1990 was in the early stages of implementation, the General Assembly initiated measures leading to reshaping higher education. 1992 Senate Bill 109, now codified as KRS 164.095, directed that the higher education accountability process be implemented in phases, to measure the performance of the statewide system and individual institutions. This evaluation process is based on performance goals and standards developed by the Council on Higher Education and the institutions. First conducted in 1993, the institutional surveys assessed student, alumni, and parental satisfaction with the quality of the educational experience and measured the institutions' success in meeting goals in such areas as research, public service, enrollment, programs and degrees awarded. Overall, the systemwide and the individual institutions'

evaluations indicated that higher education in Kentucky is effective and successful in preparing students for the 21st century.

As a part of the accountability process, the 1994-96 Biennial Budget, HB 2, charged the Council on Higher Education and the Conference of University Presidents to revise the funding formula during the 1994-95 interim and incorporate performance funding principles for use in the 1996-98 Biennium. The collaborative group developed a funding formula model based on principles of equitable and adequate allocations among the institutions, considering their respective missions and operational needs. Components of the model include a formula calculation, funding objectives, an appropriation distribution system and performance-based funding measures.

1994 HB 2 further directed that performance funds included in the general fund operating increase and the general fund surplus expenditure funds be appropriated in FY 1995-96 in amounts the institutions are qualified to expend as determined by the collaborative group. Criteria reflecting the differences in institutional missions and assigned weights for performance measures were developed. To earn 100% of the funding, an institution had to show success in the five categories of performance measures by earning a majority of points in the category. As determined by the collaborative group in May, 1995, eight of the nine institutions, including the community colleges, are slated to receive 100% of the performance funding allocation.

In May 1995, the Legislative Research Commission organized the Task Force for a Comprehensive Study of Higher Education, to recommend measures that would ensure that higher education strives for quality while preparing students to meet the challenges of the future. The Task Force is challenged to identify ways to use tax dollars more efficiently, determine strategies to ensure that students have access to higher education and improve their retention rate, review the tuition-setting process, review the higher education governance structure, and suggest cost-efficient remedies to the course-offering structure. The panel of legislators, university presidents and citizens convened in June to begin its study. Recommendations are expected prior to the 1996 Session of the General Assembly.

Discussion

The 1996 General Assembly will have to address the issue of how to fulfill the commitment to higher education. With the slow recovery of the state's economy and the unanticipated increase in general revenue funds, higher education will compete against other state programs and projects that are also clamoring for a larger share of the state's resources.

Demands placed on higher education to meet societal and economic needs are increasing. The delivery of quality academic programs and an educated workforce is expected, despite strained financial resources and prior budget reductions. Complicating the problem is the belief of some that public institutions are inefficient, offer duplicative programs and lack sufficient controls over expenditures of appropriated funds.

The reformation of elementary and secondary education logically provides impetus for the redesign of higher education to meet the needs of students in the 21st century. Under the accountability and performance-based funding process, accomplishments and failures of an institution are directly tied to funding. As this process is refined during the upcoming years, multiple years of performance data will reveal a clearer picture of how well institutions of higher education are preparing our students.

In this connection, the recommendations of the Task Force, along with the accountability assessments, will provide the General Assembly the opportunity to clarify missions and academic priorities, and to determine the equity and adequacy of the allocations in light of the financial realities the Commonwealth faces.

EDUCATION REFORM

Prepared by Donna Little

Issue

What should the General Assembly expect next in the implementation of the 1990 Education Reform Act?

Background

The Kentucky Education Reform Act, adopted by the 1990 session of the General Assembly, is the most comprehensive and innovative public school restructuring effort in the nation. The Act totally revised all of Kentucky's public education statutes affecting governance, finance, and curriculum. The following summarizes the major changes in each of the three areas since 1990.

Governance: The Kentucky Board of Education (formerly the State Board for Elementary and Secondary Education) was abolished and reconstituted. The members are gubernatorial appointees confirmed by the Senate and the House of Representatives. The board is responsible for employing a Commissioner of Education, who replaces the previously elected Superintendent of Public Instruction as the chief state school officer. The Commissioner, according to law, reorganized the Department of Education, including the establishment of eight regional service centers that have the primary purpose of helping local school districts with professional development activities.

At the local level, the law imposed anti-nepotism requirements on school board members, superintendents, and principals. Hiring responsibilities, for the most part, were removed from the board and given to the superintendent. The most significant departure from the old governance structure was the implementation of school-based decision making, through a six-member school council that includes parents, teachers and the principal. By July 1, 1996, every school must have a school council, unless exempted by the state board. Currently, more than sixty percent of the schools have implemented school-based decision making.

Finance: Support Education Excellence in Kentucky (SEEK) is the primary school funding mechanism that distributes available dollars among school districts so that districts have the resources to provide all students access to a quality education. The new funding approach is narrowing the funding differences among districts. During the 1990-92 biennium, the first biennium under the education reform legislation, the gap in total available revenue between the wealthiest twenty percent of the school districts and the poorest twenty percent of the school districts narrowed by forty-four percent. During the 1992-94 biennium, the gap narrowed an additional six percent. Since the 1989-90 academic year, Kentucky's total revenue per pupil in average daily attendance (ADA) increased from $4,011 (1989-90) to $5,633 (1993-94), helping to improve Kentucky's national ranking from 42nd to 33rd.

Curriculum: The General Assembly established the goals schools must achieve to be successful and created several new program initiatives to assist them. The purpose of the new system is to require a higher level of education for all students, who will be measured primarily by an assessment program that requires them to demonstrate what they have learned. In 1991-92, students completed the first round of assessments, which were used to establish a school's base-line and its improvement goal. Scores for the 1992-93 school year and the 1993-94 school year were averaged to determine progress toward the goals. In early 1995, successful schools received rewards for exceeding their goals. Because of legislation enacted during the 1994 regular session of the General Assembly, the most serious sanction for schools in decline is delayed until after the 1995-96 scores are computed.

A preschool program for four-year old children at risk of school failure and three- and four-year-old children with disabilities has been established in every school district. Other new programs include a primary program for children below the fourth grade, a system of family resource and youth service centers, extended school services to provide more instructional time for children who are not meeting their educational goals, expanded professional development activities for educators, and extensive administrative and instructional technology capabilities.

The structural components of the Education Reform Act will be in place by the 1995-96 school year, but it will take many years to determine whether the General Assembly has successfully improved Kentucky's education system and provided for an efficient and effective system of schools.

Discussion

The Kentucky Education Reform Act provided total systemic change. The legislation also was unique in that it included tax law revisions to help raise the necessary revenue for the new programs. Since 1990, elementary and secondary education has received approximately a forty percent increase in new state and local money.

During the 1992-94 biennium, revenue fell short of projections, forcing a wide array of expenditure reductions in government functions; however, local school districts were exempt from the reductions because of the strong commitment to the success of the new programs by the legislative and executive branches. Revenue during the 1994-96 biennium was sufficient to provide for nominal growth in the elementary and secondary programs.

Each element of reform comes under review each biennium during the budget-making process. In addition to the discussions generated by budget items, members of the 1996 General Assembly will hear comments and receive requests for amendments, since some of the programs continue to be controversial. Areas of concern include school-based decision making, the primary program, the student assessment program, and technology.

THE PRIMARY PROGRAM

Prepared by Bonnie Brinly

Issue

Should the General Assembly provide local school districts more options in offering the primary education program?

Background

The Kentucky Education Reform Act of 1990 established the primary program as the part of the elementary school program in which children are enrolled from the time they begin school until they are ready to enter the fourth grade. The critical components of the program include: developmentally appropriate educational practices, multiage and multiability classrooms, continuous progress, authentic assessment, qualitative reporting methods, professional teamwork, and positive parent involvement.

The philosophy of the primary program is to challenge all students to achieve at high levels. Many students in the early years are ready to learn skills that may not be taught traditionally to students of a certain age. For example, some entering students are already reading. Some have more advanced math skills than their same age peers. Other students may take longer to learn the prerequisite skills for reading, but are ready for more advanced math skills. The primary program is designed to provide instruction based on the student's making continuous progress. The principle of continuous progress allows more time for a student to learn a concept, if needed, or permits a student to progress more rapidly. In other words, the student is continuously challenged.

Barbara Nelson Pavan's 1992 analysis of the research comparing graded and nongraded programs since 1967 showed that students in nongraded groups performed better on academic achievement measures in 58% of the studies, or as well as graded groups in 33% of the studies. The program is also designed to eliminate the failure that a substantial number of children who are retained in the early grades experience. Research also shows that retention in grade, at best, has no effect on academic achievement and, more frequently, it correlates highly with decreased student achievement in the later years of school. In the Kentucky class that entered Kindergarten in 1986, nearly 22% failed by the end of the third grade. There are also associated costs savings as more students are successful and fewer students are retained.

Discussion

The General Assembly passed amendments in 1992 and 1994 to allow for more flexibility for schools in the design of their primary programs. The 1992 changes allowed part-time students, mostly five-year-olds, to be partially included in the primary program,

while 1994 legislation allows five-year-olds to be grouped together when it is developmentally appropriate for the individual students. The 1994 changes also addressed a misconception in the field by clarifying that "based on individual student needs, ... implementing multiage and multiability classrooms need not apply for every grouping of students for every activity throughout the entire day." (KRS 156.160)

Some educators and parents are concerned that the primary program does not emphasize the teaching of basic skills sufficiently, while proponents maintain that the basics are being taught differently, within the context in which they are used. Some are concerned that mixing students of different ages and abilities will not allow all students to achieve at high levels, while others find that both the younger and older children benefit from the experience.

Another issue is local control. The General Assembly authorized school-based decision making councils to make decisions relating to curriculum and the assignment of pupils to classes. Some believe that the primary program requirements have eliminated the local decision making in these areas. The philosophy of the reform was to encourage decision making at the school level, with school staffs held accountable for improving the success of their students. Others respond that there are many other school level decisions relating to these areas that are made within the context of the primary program. The research shows that retention is ineffective and that children at this age learn best using the practices of a model primary program, yet very few schools were using these findings prior to 1990.

Supporters of continuing the program as it is believe the obstacles can be overcome by training, collaborating with teachers who have been successful, using more flexible scheduling practices, and focusing on the continuous progress of each student, as opposed to serving age groups. Others have suggested allowing school-based decision making councils complete authority over instruction in the early years, requiring schools to offer both the primary and traditional classrooms, or permitting successful schools to obtain a waiver from the primary program law and regulations. The General Assembly will need to consider all these viewpoints when determining whether to provide additional options or to eliminate existing requirements for the primary program.

THE EDUCATION ASSESSMENT AND ACCOUNTABILITY PROGRAM

Prepared by Bonnie Brinly

Issue

Should the General Assembly make changes in the education assessment and accountability program?

Background

In 1990, the General Assembly created an education assessment and accountability system to ensure that students achieved the goals established by the legislature and to meet the Supreme Court's definition of an efficient system of common schools. KRS 158.6453 requires the Kentucky Board of Education to develop by the 1995-96 school year a statewide, primarily performance-based assessment program that measures the performance of schools. During the interim, the board is to conduct an assessment of reading, mathematics, writing, science, and social studies in grades 4, 8 and 12. These tests are to be similar to the National Assessment of Educational Progress and they are to provide national comparisons. The board refers to the state's assessment and accountability system as the Kentucky Instructional Results Information System (KIRIS).

KRS 158.6453 directed the board to contract with three or more experts in performance assessment to develop the specifications for the original contract for developing the assessment program and the accountability index. The contract was awarded to Advanced Systems in Measurement and Evaluation, Inc. Baseline data on school performance was collected in the 1991-92 school year. Currently, students take three types of tests: open-ended questions in reading, mathematics, science, social studies, writing, arts and humanities, and practical living/vocational education; performance tasks that require students to use their academic knowledge in mathematics, science social studies, the arts and humanities, and practical living/vocational skills to produce a product or solve a problem; and portfolios that include a collection of the student's best work in mathematics and writing. Arts and humanities, practical living/vocational education and mathematics portfolios have been added since the 1991-92 school year and are not included in the calculation of the accountability index for the first biennium of the program.

A school accountability index score is calculated by combining the results from each of the subject area tests administered in the assessment program, the writing portfolio scores, and non-cognitive factors, including rates of student attendance, retention, dropout, and transition to adult life. Each school has an improvement goal to meet over a two-year period. During the first interim the goal was ten percent of the difference between 100 and the school's baseline score.

Schools that exceed their thresholds by one point or more are eligible for financial rewards, while those that decline are subject to intervention. The schools in decline are required to develop an improvement plan and work with a distinguished educator; they are eligible for funds from the Commonwealth School Improvement Fund. Based on their 1992-94 accountability index, 479 schools were eligible for rewards, 370 schools were successful, 343 schools did not meet their threshold, and 55 schools were in decline. In early 1995 the Department of Education distributed nearly $26 million to reward schools and assigned forty-six distinguished educators to work with schools that are in decline.

Several changes were made in the assessment and accountability program by the 1994 General Assembly and the board. The paper and pencil tests and performance events are now administered in grade 11, as opposed to grade 12, to address concerns that seniors in their last semester may not take the test seriously. The mathematics portfolio was changed from grade 4 to grade 5 to address concerns that the fourth grade teacher was overburdened. Also to assist the fourth grade teacher, students who successfully complete the primary program are to have a writing piece that may be included in their portfolio. The board was directed not to include in the assessment program measurement of a student's ability to become a self-sufficient individual or to become a responsible member of a family, work group, or community. Finally, the General Assembly delayed implementation of the most serious sanction, "school in crisis," until after the 1994-96 biennium results are calculated.

Discussion

The state's assessment and accountability system is often called the cornerstone of education reform, in that it holds schools and districts responsible for continuously making progress toward meeting the goal of higher achievement. Assessment is a powerful force for driving instruction, so it is important that it emphasize academic skills and their application and that it represent a sample of what the public and its educators determine to be important. The Kentucky accountability system is high stakes, in that there are consequences for the results, so it must fairly and accurately measure school improvement.

The KIRIS accountability and assessment program has been the subject of two independent evaluations: one conducted by the Western Michigan University Evaluation Center for the Kentucky Institute for Education Research, the other conducted by a panel of experts from around the country, led by Dr. Ronald Hambleton, from the University of Massachusetts, for the Office of Education Accountability. The Western Michigan study surveyed educators and others and generally found that there is a lack of confidence in the KIRIS assessment, a lack of knowledge about the details of rewards and sanctions, and a lack of knowledge about the involvement of Kentucky educators serving on the advisory committees. On the whole, the panel found the tasks to be well-crafted and that the open-ended questions met technical standards. It recommended improved technical reporting, using a different method for determining the reliability of the accountability index, and adding multiple-choice items. The authors questioned the inclusion of the performance events and the writing portfolio in the calculation of the accountability index, because of

their low reliability. They also emphasized the importance of continuing to communicate with and to involve educators in the assessment development process.

The Office of Education Accountability Panel concluded that because of serious measurement flaws the present form of KIRIS is not meeting the state's assessment and accountability goals. It found that the misclassification rates of schools in some reward categories was high, that evidence from other assessments do not support the large gains reported for some subjects and grades, that the procedure for linking the tests from year to year is faulty and makes accurate year-to-year comparisons questionable, that the method for setting performance standards is inadequate, and finally, that the use of portfolio assessments in a high-stakes environment is problematic, because teachers tend to score their students' work higher than other groups of scorers, and portfolios are not standardized in terms of tasks, instructional support, or time spent. The panel also recommended including multiple-choice items to expand the coverage of content and to increase the tests' reliability and validity. The panel does believe that the testing system can be improved to meet the state's goals and it made twelve recommendations to that end.

The Kentucky Board of Education has agreed with the majority of the recommendations from both studies, with the exception of those concerning portfolios. The Department disagrees that portfolios should be eliminated from the accountability system and wants to explore the recommendation of the OEA panel that teachers not score their own school's portfolios. The Western Michigan panel recommended continuing to have local teachers score portfolios.

After consideration of the OEA panel's report, the Subcommittee on Education Accountability emphasized its support and commitment to assessment and accountability. It recommended that the rewards be suspended until the reliability and validity of the accountability system are adequately demonstrated, that the General Assembly continue to appropriate money to the rewards trust fund, and that the test emphasize content, not just process. It also asked the Department to report on how portfolios may appropriately be used in the accountability system, to make a recommendation on how to have a primarily performance-based system, and also to provide national comparisons both in the short term and the long term. Finally it recommended that the Department obtain recommendations from teachers, superintendents, board members, interested members of the public and testing experts as it makes adjustments, but keep in mind that an accountability system is essential.

A number of additional issues may be considered by the 1996 General Assembly relating to the assessment and accountability system. The General Assembly may have to make adjustments to the law in order to address some of the recommendations relating to the timeline for the accountability system. Another issue is whether the testing should be longitudinal: whether it should measure the change in education performance of individual students over the course of their time in a school, or remain as it is by testing all students at certain grade levels. Continuing the current method of testing certain grade levels holds schools accountable for being successful with all students, while following students who spend all their time in one school would require extensive tracking and could result in

reduced accountability for students who transfer. The law calls for an accountability system designed to measure a school's performance. Many educators and parents believe the system should be designed to measure individual student performance. Finally, the present system is tied to the National Assessment of Educational Progress for national comparisons. These comparisons can only be made in the subjects and grades tested by the National Assessment, which may be insufficient to address the concerns of parents and the public.

There will always be error in any assessment and accountability system and different types of assessments usually serve one purpose better than another. For example, the writing portfolio and other direct assessments of writing are more valid than assessments that do not require students to write, such as multiple choice tests. The writing portfolio has led to an increased emphasis on writing in the schools, an instructional goal, but because the scoring is not as reliable as that for other types of testing it reduces the reliability of the accountability index. The 1996 General Assembly will have to determine the most important purposes of its assessment program: whether it is to measure change in a school's academic performance, drive instructional change, or provide student-level national comparisons. No single assessment will serve all purposes equally well.

ENERGY

SITING CELLULAR ANTENNA TOWERS

Prepared by Linda Kubala

Issue

Should there be local zoning review of cellular telephone antenna towers?

Background

The spectacular growth of the cellular telephone industry has been accompanied by a growth in the number of cellular antenna towers dotting the landscape. The cellular towers, which can be 150 - 200 ft. tall, often are seen by neighbors as eyesores and potential hazards, especially in urban residential neighborhoods. Local planning and zoning boards, however, have no jurisdiction over cellular tower sites, since KRS 100.324 exempts all utility service facilities of companies regulated by the Public Service Commission, among others, from zoning control.

Cellular telephone companies are licensed by the Federal Communications Commission (FCC) and also are regulated by the Kentucky Public Service Commission. The Kentucky commission does not regulate the rates of cellular companies, but does enforce conditions of service. As part of its oversight, the commission reviews and approves applications to construct new cellular antenna towers.

The Public Service Commission has added procedures to include local input in its permit process, so that site-specific issues can be aired. Companies must notify nearby landowners and the local planning and zoning board of proposed projects, and the commission will hold a hearing if objections are received. In the end, however, the Public Service Commission lacks statutory authority to reject a proposal for aesthetic or land use reasons, so local citizens may feel they have no say in the final decision. The cellular industry generally opposes any additional regulation or additional layer of regulation which could lead to delays and higher costs.

Discussion

On its face, cellular tower sites are not locally regulated because they are exempted by KRS 100.324. Removing the exemption would seem to solve the problem. In practice, however, several other factors complicate the matter and need to be considered:

- Federal law and FCC regulations severely limit the power of the state or localities to determine where towers are placed. The FCC controls the entry of companies into specific markets and sets franchise boundaries. States or localities may not keep these companies from doing business (1993 Budget Reconciliation Act, P.L. 103). In the case of tower construction, they may not prohibit a company from erecting an antenna

tower, but may only select the most appropriate site within a designated area, which in urban areas may encompass only a dozen city blocks. Regardless of state law, a zoning commission may not simply prohibit towers in residential neighborhoods, for example.

- Many parts of the state do not have comprehensive land use planning. Any proposal to allow greater local input into the siting of cellular antenna towers needs to address both those parts of the state with planning and zoning boards and those without.

- If state regulation is retained, zoning board review adds an additional review, with added time and cost to the company. If local regulation is enacted in lieu of existing controls, then the value of safety and engineering oversight by the Public Service Commission would be lost, along with any siting review in counties or cities without local planning units.

The cellular industry argues that Kentucky regulation already is unusually stringent, compared to that of other states, and should be loosened, not augmented.

SB 79, which was introduced but did not pass in 1994, attempted to give local governments authority over cellular towers by removing cellular companies from all regulation by the Public Service Commission. Another approach to the problem, embodied in Prefiled Bill, 96 BR 184, is to require both local zoning approval and Public Service Commission approval of a cellular tower proposal, with judicial appeals if the two agencies can not agree. That bill also would give the Public Service Commission more authority to consider land use issues when it reviews proposals for towers in places which are not covered by planning and zoning.

ENERGY EFFICIENCY IN STATE FACILITIES

Prepared by Mary Lynn Collins

Issue

Should the Commonwealth undertake a new program to address energy management and conservation in state-owned and leased facilities?

Background

Kentucky state government, which spends over $40 million annually to heat and cool 50 million square feet in state government-owned buildings, could significantly reduce its use of energy and divert the money saved to much-needed state services. Technology is changing so rapidly that buildings built only ten years ago could benefit significantly from certain energy purchases and retrofit measures. The state Division of Energy, in the Natural Resources and Environmental Protection Cabinet, estimates that the state could save $10 million a year in energy bills by making cost-effective energy improvements like installation of new efficient lighting, cooling, and heating systems. This estimate is based on documented energy savings realized in the energy conservation program for schools and hospitals that the state Energy Division administers with federal funds. Energy improvements undertaken in that program produce on average 25% in energy savings. However, no comprehensive program is currently in place to accomplish such energy savings in other existing facilities.

In addition, the state does not systematically consider energy efficiency in new buildings it constructs or facilities it leases. While new construction of state facilities must meet a minimum energy code, the state does not require architects to design energy efficiency into new state buildings. Nor are actual energy costs considered before the state evaluates bids and enters into lease agreements.

Both the federal government and state governments are paying a lot of attention to their own energy bills these days. The Energy Policy Act of 1992 requires that federal agencies reduce the energy consumed in federal buildings. A goal for federal facilities, set by executive order, is to reduce energy consumption 30% by 2005 (compared to 1985). At least 26 states have created programs to reduce their energy use. Many of these programs are comprehensive and include strict construction standards for new buildings, as well as extensive retrofits of existing facilities. Many of the programs also focus on the human side of energy management, providing education to employees and training and technical assistance for building superintendents.

The issue of energy efficiency in government facilities has been much discussed in this state also. The Governor's Commission on Quality and Efficiency recommended a comprehensive program of energy improvements for existing and newly acquired state buildings. In its 1992-98 Statewide Capital Improvements Plan, the Capital Planning

Advisory Board recommended that legislation be enacted for the implementation of an energy management program for state facilities. A bill addressing the issue was introduced in the last regular session of the General Assembly, in 1994. House Bill 98, which passed the House but died in a Senate committee, called for an energy efficiency unit to be located in the Department for Facilities Management and would have established an energy efficiency policy for state government. Various legislative committees, including the Special Subcommittee on Energy and two subcommittees of the Interim Joint Committee on Appropriations and Revenue, are working on the issue this interim.

The Finance Cabinet recently included in its 1994-2000 capital improvement plan a new energy efficiency unit, similar to the one originally proposed for House Bill 98. The proposed program unit, to be composed of five staff members, would have three major tasks: (1) identifying and completing low cost and no cost energy measures, including promotion of energy awareness among state employees and training building maintenance and operations staff; (2) conducting engineering analysis to determine energy conservation measures that are cost effective; and (3) overseeing the more extensive energy retrofits, where cost estimates indicate a payback from savings within five years or less. As proposed, the plan would take eight years to complete and cost $58 million.

Discussion

If the General Assembly decides to fully implement the program, issues of funding administrative overhead, engineering analyses, and energy retrofits must be addressed. Possible funding sources include: (1) General Fund appropriations, (2) revenue bond issues; and (3) energy performance contracting. While in the long run the least costly approach would be General Fund financing, there are numerous competing demands on this funding source. Although concern about the state's bonded indebtedness makes the second option difficult, a revenue bond issue could probably be structured to use energy savings to create a positive cash flow within the first year. The last option, performance contracting, is a relatively new mechanism that government at all levels is increasingly using to make comprehensive energy improvements in public facilities. Under energy performance contracting, a private energy service company typically installs the equipment and completes all retrofit work, maintains the equipment and provides financing. In most cases, energy savings are guaranteed with the fee for services based on actual value of the reduced energy realized. A key advantage to the financing is that there are no up-front costs to the user. A disadvantage of performance contracting is that the client, in this case the state, would have to give up some control of the energy systems, since the contractor would maintain and monitor the equipment.

Rather than tackle a comprehensive energy program, the General Assembly could choose to focus on low-cost energy measures (estimated to save $4 million annually) and/or fund an energy retrofit demonstration in one or several buildings. In addition to any action regarding energy management in buildings now owned by the state, the General Assembly may also look at various actions to reduce energy use in new construction, leased properties, equipment purchases, and even the state motor pool.

HEALTH AND WELFARE

EARLY PERIOD SCREENING DIAGNOSIS AND TREATMENT SERVICES

Prepared by Bob Gray

Issue

Should the General Assembly establish clearer guidelines governing the provision of Early Period Screening Diagnosis and Treatment (EPSDT) services through the Medicaid Program?

Background

EPSDT stands for the Early and Periodic Screening, Diagnosis and Treatment program. The program is administered through Medicaid and covers the health care needs of children under age 21 who meet state poverty eligibility standards. EPSDT requires four different types of screening: **medical, dental, vision, and hearing**. States must provide each type of screen for Medicaid eligible children. States must also provide treatment for conditions discovered through the screens. EPSDT includes provisions for outreach programs whereby states are mandated to inform eligible families about EPSDT services.

The federal Omnibus Budget Reconciliation Acts of 1989 and 1990 made a number of changes that affect EPSDT:

- States are mandated to reach an 80% screening rate by 1995;
- Intervals for screens must be improved to match those recommended for well child care by the American Academy of Pediatrics;
- Interim screens must be provided if a problem is suspected; and
- Any services covered under federal Medicaid law must be provided for conditions discovered through screening, even if the state does not normally cover that service.

Discussion

There have been questions raised about the extent to which Kentucky is meeting its screening mandate, as well as the actual number of children receiving screening services. According to the Medicaid expenditure report for fiscal year 1994 (MS 264 Report Series), $6,128,279 was spent last year for 4,334 total utilizers in the EPSDT service category. This is a small portion of the over 280,000 children currently eligible for Medicaid. State Medicaid officials have testified that the actual number of children screened is much higher because 267,602 children were treated by physicians through the Medicaid program and these physician visits are not counted as screenings.

An additional concern is the manner in which Medicaid recipients are informed of the availability of services through the EPSDT program, and whether parents of disabled children are fully aware of the services Medicaid will cover for their children. Given the ability of EPSDT to cover a wide range of services for disabled children, and the favorable federal matching rate for Medicaid expenditures, the General Assembly might want to encourage utilization of the EPSDT program by establishing clear guidelines for accessing the program and expanding efforts to inform Medicaid recipients of the program.

STATE HEALTH PLAN AND CERTIFICATE OF NEED

Prepared by Robert A. Jenkins

Issue

Should the General Assembly limit the use of the state health plan in the certificate of need process?

Background

The state health plan provides a general overview of Kentucky health care, documenting needs and inventorying services of different types of health facilities and services. The plan offers goals, identifies problems, and provides criteria and standards for utilization in the certificate of need process.

The 1992-1995 Kentucky State Health Plan analyzes population data, mortality rates, morbidity, and selected factors affecting human health. It notes current trends and issues in the health care delivery system, and proposes solutions.

The Kentucky Health Policy Board oversees the certificate of need and state health plan processes, though prior to July 15, 1994, oversight rested with the Cabinet for Human Resources and its State Health Planning and Development Agency.

Discussion

KRS 216B.015(19) requires the Kentucky Health Policy Board to prepare the state health plan every three years, to update it annually, and submit it to the Governor for approval. The Board plans to hold hearings across the state to learn of concerns of Kentucky residents as it begins the development of the 1995-1998 state health plan.

The fact that any certificate of need approved by the Board must be consistent with the state health plan places great significance on the plan's development and findings. If a health corporation wishes to build a new hospital in a given area, its construction must be consistent with the plan. If the plan indicates that no new hospital beds are needed in that geographic area, then the certificate of need may not be granted. This analysis holds true for the purchase of major medical equipment of $500,000 or more in a physician's office, as well as nursing homes and many other health services and facilities.

It is argued by some that the state health plan and certificate of need process should be repealed because the health needs of some Kentuckians are not being met while the administrative procedures prolong the construction or provision of facilities and services. If a service is needed, business should be allowed to provide it without

government interference. If the company is unable to survive in a competitive environment, or it if puts existing businesses out of business, then that is the nature of business.

Proponents of the state health plan and certificate of need process argue that needless facility construction and provision of service raises the cost of health care and provides services in areas where they may not be needed. If there is no process that seeks to make certain that a service will be provided in an efficient manner in a geographic area needing the service, then needless expansion could jeopardize existing services and facilities.

Should the General Assembly decide to address the state health plan issues, the following alternatives could be considered:

(1) Enact legislation repealing the state health plan;
(2) Enact legislation repealing the significance given to the state health plan by the certificate of need statutes; and
(3) Enact legislation repealing the certificate of need requirements for certain types of health facilities or services.

HUMAN RESOURCES BLOCK GRANTS

Prepared by Dianna McClure

Issue

Should the General Assembly amend the current statutes governing state legislative oversight of federally funded block grant programs in response to federal changes?

Background

A total of 15 federal block grant programs, costing about $32 billion a year, are currently in effect. Many of these block grants trace their roots to the General Revenue Sharing Program passed in 1972, which distributed a virtually unrestricted $5 billion per year for five years to states and local governments, and the Omnibus Budget Reconciliation Act of 1981, which consolidated over 50 categorical programs and three existing block grants into nine block grants in areas such as job training, low income heating assistance, and substance abuse and mental health. During the 1970's, three initial block grants had been designed---the Comprehensive Employment and Training Act (CETA), the Community Development Block Grant, and Title XX of the Social Security Act.

The federal block grants created were broader in scope and offered greater state discretion in the use of funds than categorical programs. Block grants were to encourage administrative cost savings and decentralized decision-making, promote coordination, and allow for target funding.

Legislation enacted in the 1982 Regular Session of the General Assembly required state administering agencies to submit any federal block grant application to the Legislative Research Commission for review and comments at least ninety days prior to the submission of the application for funding to the federal administering agency (KRS 45.350 through 45.359). The General Assembly also enacted separate procedural guidelines for submission of the Community Services Block Grant Application (KRS 273.410 top 273.453), including the provision of a state regulatory formula for allocation of the funds to each community action agency. Further, the legislation required a legislative public hearing on each block grant application to be conducted by the interim joint committee with appropriate subject jurisdiction.

The following table identifies the federal block grants funded at the time of enactment of Kentucky's block grant oversight laws:

Federal Block Grants Funded as of 1981
BLOCK GRANT:
Community Services
Alcohol, Drug Abuse, & Mental Health
Primary Care
Social Services
Maternal and Child Health
Preventive Health & Health Services
Education (Chapter 2)
Low-Income Home Energy Assistance
Community Development

Discussion

Kentucky's block grant oversight laws have not been modified since they were enacted. Some federal block grants identified in Table 1 have been folded into others and some have split (such as Alcohol, Drug Abuse, and Mental Health). The federal block grants are now under review for restructuring by the 104th Congress. Legislation proposed by the U.S. House of Representatives targeted eight broad areas to replace federal welfare programs with block grants to the states. These included food and nutrition, cash welfare, social services, child abuse, child welfare, and employment and training.

Some 336 programs have been identified as possibilities for consolidation by the Congress. These proposals include programs that are different from those included in the 1981 consolidation. For example, Aid to Families with Dependent Children and Supplemental Security Income are entitlements that provide direct cash assistance to individuals based on need. Other programs provide open-ended support for children who are placed in foster care and for those receiving adoption assistance. Under entitlement programs, states receive federal funds on a matching basis. As the number of persons in need increases, so does federal support. If these entitlements are folded into block grants, the open-ended funding to the states could be replaced by capped appropriations.

If such federal legislation as the Personal Responsibility Act, with its proposed consolidation of such entitlement programs such as cash welfare, is enacted, the General Assembly may first decide to modify its state public assistance laws providing benefits to categories of needy recipients of Aid to Families with Dependent Children. The General Assembly could enact state specific welfare reforms instead of requesting federal waivers. In addition, several of the block grant programs include statutorily mandated targeted funding for certain populations.

A few of the many factors state legislatures may have to consider, should block grant funding be overhauled, as is currently proposed, are as follows:

- Whether the current form and content of data collection and reporting related to outcomes is adequate or should be revised if more decision-making occurs at the local level;

- Whether current funding priorities at the state level for needy populations should be repositioned if federal funds are reduced;

- Whether measures of service quality should be included in any reporting requirements of funded service programs; and

- Whether the current method of allocating block grant funds within the Commonwealth is equitable across geographic regions by targeted population.

Nonetheless, the current mix of categorical and block grants is fragmented. There are multiple funding streams directed at the same needy populations, generating duplication of services and wasteful administrative expenditures. Critics support the view that communities need flexibility to identify and fund their own needs rather than being forced to accept "top down" solutions.

POVERTY

Prepared by C. Gilmore Dutton

Issue

Is there any legislative action that could be taken to break the cycle of poverty in Kentucky?

Background

During the decade from 1980 to 1990, the number of Kentuckians living in poverty increased, both in absolute terms and as a percentage of the state's population. And today, one in every five of the Commonwealth's citizens lives in poverty, one in every four children in Kentucky lives in poverty, and one in every three African Americans in Kentucky lives in poverty. No geographic area is immune from this social disorder: poverty rates range from 15 percent of the population living on farms, to 16 percent of urban residents, to 22 percent of those living in rural communities.

These distressing statistics exist despite the fact that Kentucky's per capita personal income has grown faster than the national average in all but one of the last seven years, despite the fact that Kentucky ranked sixth among all of the states in the increase in personal income from 1982-1992, and despite the fact that Kentucky's unemployment rate places it among the lower half of all the states. The number and condition of the Commonwealth's poor continue to worsen, even though Kentucky ranks nineteenth among the states in the number of institutions of higher education, has been cited as having one of the most attractive economic development programs in the nation, and ranks fifth among the states in state and local expenditures for public welfare per $1,000 of personal income.

Discussion

The 1994 Session of the General Assembly, recognizing a growing disparity in income levels among the citizens of the Commonwealth, created the Commission on Poverty. Currently composed of eleven legislative and eleven at-large members, the Commission's charge, embodied in SCR 74, is to ". . . evaluate . . . and recommend improvements in any of the programs which could mitigate the causes of poverty . . ." in Kentucky.

The Commission held its initial meeting on November 2, 1994, and has met monthly since. Recently, the Commission met outside of Frankfort, for the first "field trip," intended to give the Commission members the opportunity to talk face to face to the poor in their home setting.

During the course of its nine months' existence, the Commission has gathered reams of data about the poor, the near poor, and those at risk of being poor; has heard

from a number of practitioners laboring in the field of poverty and has been inspired by countless selfless acts in behalf of those in need; has been thrilled by first-hand accounts from individuals who have pulled themselves up by their proverbial boot straps to rise above poverty; and has taken testimony from academicians, and government employees, federal and state, Kentuckians and otherwise. And in answer to the question, is there anything that can be done to break the cycle of poverty in Kentucky, the Commission will undoubtedly respond in a resounding "yes," with its convictions reflected in its recommendations for consideration by the 1996 session of the General Assembly.

A sampling of recommendations which will likely be considered by the Commission include:

(a) The employment of individuals from a "targeted workforce" of welfare recipients or the unemployed, as a criterion for participation by business in all, rather than some, of Kentucky's economic development/tax incentive programs;

(b) The establishment of "one-stop" worker assessment and job placement centers in various communities throughout the state;

(c) The stipulation that preference be given for economic development loans to those firms that promise to provide child care for dependents of their employees;

(d) The award of tax credits to businesses to partially offset the cost of providing child care for employees' dependents;

(e) The encouragement of teacher-mentoring programs throughout all the high and junior high schools in the state;

(f) The funding of child care centers in high schools in each of the state's counties, for dependents of yet to be graduated students;

(g) A directive that the state seek waivers from federal rules that would enable AFDC recipients engaged in starting a business to retain their AFDC eligibility while exceeding current asset limits; and

(h) The empowerments of local communities to select and direct local services provided to children and families through the creation of mandated, Oregon-style local Commissions on Children and Families in each county in the Commonwealth.

While it has become evident to the Commission on Poverty that there is no "quick fix" or "cure-all" to poverty, it has become equally evident that there are a number of actions that can be taken by the state to forever sever the bonds of poverty for a large number of Kentuckians. Prioritizing recommendations for apportionment of limited resources among not-so-limited needs will be the Commission's biggest challenge.

JUDICIARY

PARENTAL LIABILITY FOR JUVENILE CRIME

Prepared by Norman W. Lawson, Jr.

Issue

Should parents be held liable for juvenile crime?

Background

Many experts cite the breakdown of the family as a source of juvenile crime; thus as juvenile crime has increased, demands for more controls over parental involvement with juveniles has increased. Traditionally a parent who sat by and did nothing to protect a child was liable for permitting the child to become neglected, needy, or dependent. Kentucky many years ago decided to hold parents liable for juvenile vandalism and for shoplifting. However, in recent years there has been a call for holding parents liable for more offensive acts committed by their children, even if they didn't participate in or know of the act. Following the lead of Florida, Montana, and other states, Kentucky will now hold parents liable if a juvenile obtains a handgun and commits a crime with it, even if the parents were merely negligent in storing the firearm. The 1994 General Assembly was presented with legislation which would have held parents liable if a juvenile violated a municipal curfew ordinance. The curfew legislation did not pass. Questions legitimately arise as to what parents may and may not legitimately do to control delinquent children, particularly those who are continually delinquent and cannot be controlled, even by the court system.

Discussion

Proponents of such legislation feel that parents are lax in the control of their children and that parental control can be encouraged by holding the parents liable for the child's acts. A typical proposal made at the 1994 session of the General Assembly would have set a curfew for children and made the parents liable for each offense of violation, but no action would have been taken directly against the child until the third offense.

Opponents offer the proposition that many children who get into trouble are in conflict with their parents and would use any opportunity to get the parent in trouble, either alone or along with them.

One possible compromise involves the use of the "one free bite" theory for some offenses where the parent had no prior knowledge that the child was committing an offense; parents would be held liable after the first one. Another compromise involves not holding a parent liable when the parent has first turned the child over to the juvenile court as beyond parental control, or has reported the offense himself.

JUVENILE CODE

Prepared by Norman W. Lawson, Jr.

Issue

Should the juvenile code be replaced by a more adult type of system?

Background

Violent crime and other crime by juveniles continue to increase and draw persistent news media coverage. Throughout the years the juvenile court system has been designed to protect the name of the child, to use the least restrictive and least punitive alternatives in dealing with the child, and to encourage counseling over punishment. Over the years jailing of juveniles with adults has been prohibited but spending on juvenile detention facilities has been discouraged, and the costs of building such facilities has risen significantly, not to mention the cost of the operation of these facilities. As a result judges have few meaningful options for dealing with seriously delinquent youth. Nationwide, the states, led by Colorado, Florida, and others, have adopted "get tough" policies on juvenile crime, stripping anonymity from the system, treating an ever-increasing number of juveniles as adult criminals (although still incarcerating them in juvenile facilities) and changing the demeanor of the juvenile court from one of advocacy for the child and its rights to protection of the public against what are perceived to be juvenile criminals.

With respect to these issues, Kentucky has increased the number of children covered by "youthful offender" legislation, which covers children who commit felony offenses, and by trying older children who commit felony offenses with firearms as adults. The General Assembly has also permitted victims of juvenile crime to attend the juvenile court proceedings relating to their cases. Despite these initial measures, juvenile violent crime is increasing.

Discussion

Proponents feel that the current juvenile court system pampers juvenile criminals by protecting their names from disclosure and not reacting effectively until the juvenile is a repeat felon; they feel this system has too few real sentencing options. They allege that the juvenile court is virtually unable to deal with juveniles, that there are no secure detention facilities, and that probation and counseling have not worked. They want more penalty options, increased use of jail and detention, mandatory labor, mandatory restitution, and similar penalties.

They also want publication of juvenile names and opening of juvenile court sessions to press and public alike. If courts cannot be open and other things cannot be

done to classify more juvenile crime as adult crime, they argue, we should add juvenile curfews and impose other restrictions.

Opponents cite the proposition that juvenile court has been designed from the outset as a place where informal adjustment in a closed setting, combined with counseling and treatment, using incarceration as a last resort, have always been the approach, and that the program has worked well over the years, if enough resources have been given to it. They cite the major problems as having too few resources, not enough social workers, not enough treatment programs and treatment facilities available, and a general failure to realize that children are not adults and may not benefit from adult penalties.

Both sides feel that early detection and intervention in delinquency and behavior problems in school and in the home at the ages of 6, 7, or 8 may offer hope of effective treatment. As the child becomes older and has more contact with the courts, the chance of rehabilitation may decrease, as indicted in testimony before the Juvenile Subcommittee of the Interim Joint Committee on Judiciary.

VIOLENT OFFENSE SENTENCES

Prepared by Norman Lawson

Issue

Should sentences for offenders be lengthened?

Background

As public concern over crime increases and the press attention to violent crime remains unrelenting, there are calls for stiffer penalties for violent criminal offenders and for repeat offenders. In recent years the Kentucky General Assembly has passed truth-in sentencing legislation, to permit juries in the penalty phase of a trial to know the defendant's prior record, bifurcated trials to permit introduction of the evidence about the defendant's past record, lengthened the time to parole for violent offenders, increased sentences, created new crimes and prohibitions against probation of violent offenders, sex offenders, persons using firearms in the commission of crimes and various other types of offenses, and created a sentence of life without parole for 25 years as an alternative to the death penalty (which, while still on the books, has not resulted in an execution since 1962).

Proposals have been made to lengthen sentences through statutes setting life without parole as the penalty for various offenses, requiring life without parole for second or third violent offenses, and setting statewide standards for pretrial diversion programs for felony offenders. (Pretrial diversion means that a defendant undergoes counseling, agrees to do community service, or pays restitution, without admitting guilt and without going to trial.) Georgia voters just approved "two strikes and you're out" legislation, while various other states and the federal government (through various funding programs in the 1994 Crime Bill) favor requiring "three strikes and you're out" (imprisoned for life without possibility of parole) for repeat violent offenders.

Discussion

Proponents cite the reduction of crime which has occurred in states which have lengthened sentences for violent offenders. They feel that the offense of murder needs a new penalty (life imprisonment without parole), rather than the life with parole in 12 years or 25 years, as now permitted in Kentucky, that repeat violent offenders are better kept in prison for the protection of the public, and that "three strikes and you're out" and sentence lengthening will protect the public from these criminals. Similarly, proponents feel that pretrial diversion and alternatives to trial programs should not be available to violent offenders, and that, since there are no statewide standards for these programs, set statutory standards might prevent abuses of these programs.

Opponents of such programs cite the often criticized federal sentencing guidelines and the federal elimination of parole as a model not to follow. They cite the tremendous costs of prison construction and of keeping offenders in prison (a typical 20-year-old prisoner sentenced to life without parole will live to be 70 years of age and cost $1 million or more to keep in prison--not counting prison construction costs), the increasing costs of caring for geriatric prisoners, and the success of some rehabilitation and retraining programs. They feel that the new attitude is retribution and that it creates a situation where, in the absence of the use of the death penalty, a person sentenced to life without parole may be less manageable in prison and more prone to escape, since they know that the most they can get is the sentence they already have.

DOMESTIC VIOLENCE

Prepared by Norman Lawson and Susan Lewis Warfield

Issue

Should the General Assembly amend statutes relating to domestic violence?

Background

The last decade in Kentucky has seen extraordinary changes in the service system for domestic violence victims and survivors. As reports of instances of domestic violence (spouse abuse, adult abuse, child abuse, child sexual abuse, and abuse of the elderly) have risen, the General Assembly has acted in each of these areas to attempt to reduce the violence and to punish perpetrators. The 1992 Kentucky General Assembly enacted landmark legislation relating to the crime of domestic violence; it has served as one of five state models used by the National Council of Juvenile and Family Court Judges to draft the Model Code on Domestic and Family Violence. Funding for shelters has increased. Model law enforcement training has been developed. Standards of care for mental health services provided in domestic violence cases have been written. A prosecutor's manual for domestic violence has been completed.

Domestic violence in the home setting now brings on domestic violence orders from the courts, with statewide registry of the orders, arrest by police for violation of the orders, and other court-related sanctions including criminal sanctions. Child abusers and sex offenders now face mandatory imprisonment in most cases, without being paroled until they successfully complete a state-operated sexual offender treatment program. Reporting of child abuse and adult abuse incidents to the police is now mandatory. Adult abuse by persons who are in a caregiver relationship is a crime, stalking is a crime, and sentence lengths for these offenses have been increased. These initiatives have moved Kentucky far ahead of many other states, earning the Commonwealth national attention.

There has been a growing recognition in Kentucky, however, that despite the enactment of strong and progressive legislative reform, significant problems in the state's domestic violence service system remain. The tools provided by law to the professionals working in the justice system are not being applied in a uniform or consistent manner. System and professional accountability is an elusive goal. Additionally, funds for protective, support and treatment services for domestic violence victims and their families are insufficient. The number of homicide and homicide-suicide cases related to domestic violence continues to increase. Approximately every seven days in the Commonwealth, a victim of domestic violence is murdered.

Discussion

In response to these trends, the Co-Chairs of the Legislative Research Commission called for the establishment of the Legislative Task Force on Domestic Violence in August 1994. This Task Force was directed to study the causes and extent of domestic violence in Kentucky families and the implementation and enforcement of existing laws dealing with domestic violence. Members of the Task Force include legislators and representatives of the judiciary, prosecutors, law enforcement, social services, mental health, victims services, court administration, and advocates for change.

The Task Force is to develop legislative and budgetary recommendations for the 1996 Regular Session of the Kentucky General Assembly. In addition, the Task Force is to identify policies, procedures, or regulatory changes which can be implemented prior to January 1996. The Task Force has been directed to submit recommendations to the Legislative Research Commission on or before October 1, 1995.

Testimony before the Task Force has suggested that additional training is needed by some system personnel to increase awareness of the dynamics of domestic violence; that perhaps second and subsequent offenses should incur enhanced penalties; that a mandatory 24-hour hold until arraignment for some offenses should be required; and that prevention and protection efforts should be coordinated at the state and local level by establishing interagency councils. Others suggest that what is really needed is to enforce the laws that currently exist, making certain that social services, law enforcement, prosecution, and the courts actually make the current system work.

The goals of the Legislative Task Force include the following:

1. Review the implementation of 1992 legislation on domestic violence, with specific identification of areas of non-compliance;
2. Review levels of funding for domestic violence services, including the adequacy of spouse abuse center beds, adult protective services, mental health services for victims and perpetrators, and law enforcement and criminal justice services;
3. Review Kentucky's efforts toward the prevention of domestic violence;
4. Review the impact of domestic violence as a public health problem and the specific impact of providing domestic violence related care by medical professionals;
5. Review the extent of domestic violence related homicide and homicide-suicide in the Commonwealth and make recommendations related to effective intervention and preventative efforts; and
6. Make recommendations to the 1996 General Assembly for vital changes in policy, statute, administrative regulation or budget to ensure an effective, comprehensive service delivery system to families at risk of domestic violence.

LABOR AND INDUSTRY

WORKERS' COMPENSATION SPECIAL FUND

Prepared by Linda Bussell

Issue

Should the General Assembly amend the workers' compensation law to address the problems of the special fund?

Background

The 1994 General Assembly enacted major reforms in the workers' compensation law. The 1994 reform effort was the second in less than a decade. The 1994 reforms were major and affected almost all aspects of the program, including: its administration and organizational structure, the definition of injury; benefits paid to injured workers and the attorneys who represent them; reimbursement levels for medical providers and the manner in which medical services are provided, including managed care; and the insurance financing mechanisms of the program, including the creation of a competitive state fund.

Although the full impact of the reforms will not be fully realized for two to three years, a cost analysis conducted by a national ratemaking organization indicated that the reforms will result in significant savings to employers in the Commonwealth.

Despite the fact that the full impact of the reforms will not be known for two or three years, many believe additional reforms will be necessary in 1996. Most observers and administrators of the workers' compensation program in Kentucky generally agree that the financial problems of the special fund will probably be the most significant workers' compensation issue facing the 1996 General Assembly.

The special fund pays for subsequent or second injuries, a portion of most occupational diseases, all costs of administering the workers' compensation program, and most of the administrative and program costs of the Labor Cabinet. Most other states have similar funds and several are experiencing problems similar to those of Kentucky's special fund. Kentucky's special fund, however, is the largest in the country, with a projected unfunded liability of almost $2 billion.

Discussion

The special fund is financed through assessments on employers' workers' compensation premiums. Despite past reform efforts, the liability of the special fund continues to grow dramatically; large increases in the total annual assessment on employers would be necessary to achieve the objectives of the 30-year funding mechanism adopted in 1987.

Results of actuarial studies and recent loss statistics indicate that most of the liability of the special fund is attributable to the coal industry for awards made for black lung and coal related injuries. Accordingly, the coal industry is assessed more than non-coal industries to finance the special fund. Although the coal industry is assessed more than non-coal industries, significantly larger annual assessments would be required from all employers to fund the special fund in accordance with the objectives of the thirty-year funding mechanism adopted in 1987. There is concern that increased assessments will threaten economic development efforts of the Commonwealth. There is a great concern that the impact on the coal industry of increased assessments for the special fund, combined with recent large increases in workers' compensation premiums, could devastate an already struggling and declining major industry in Kentucky.

Kentucky's special fund, like similar funds in other states, was originally created to serve as an incentive to employers to hire workers with disabilities. The theory underlying the creation of Kentucky's special fund and similar funds in other states was that an employer would be encouraged to hire a handicapped worker with a disability, if there was a special fund to pay a portion of the benefits paid to a disabled worker whose disability was worsened as a result of a work-related injury. There are no studies that indicate that the original purpose of second or subsequent injury funds was realized. On the contrary, research indicates that many of these funds, like Kentucky's special fund, have been expanded to the point that they have become major payors in the workers' compensation system, and a financial burden on employers who fund them. Consequently, several states are considering solutions to the financial problems of their funds. During the past few years, seven states (Alabama, Colorado, Kansas, Maine, Minnesota, Oregon, and Utah) have abolished or greatly reduced the scope of their second or subsequent injury funds.

The Interim Joint Committee on Labor and Industry, like similar legislative committees in other states, is in the process of studying the problems with the workers' compensation special fund in Kentucky. The committee plans to develop recommendations to present to the 1996 General Assembly.

INDEPENDENT CONTRACTORS

Prepared by Biff Baker and Vinson Straub

Issue

Should the General Assembly enact legislation to address independent contractor issues?

Background

Independent contractors, by general definition, are not considered employers under state, federal, or case law. There is an ongoing issue, however, regarding individuals who allege to have "independent" contractor status but who are actually employers. Individuals who falsely claim independent contractor status could possibly be circumventing several laws, primarily in the areas of wage and hour provisions, workers' compensation, unemployment insurance, and taxation. There is no uniform definition of independent contractor in the Kentucky Revised Statutes, and there is no absolute rule on what actually constitutes an independent contractor. The absence of an employer-employee relationship is indicative that work is being performed by an independent contractor. Case law has carved out a generally accepted test for determining the existence of an employer-employee relationship. There are as many as 20 factors that can be used in determining the relationship. The primary basis for the test is the issue of control over the work. If the employer exercises little or no control over the performance of work, the work is probably being performed by an independent contractor and there is no employer-employee relationship.

Agencies that administer the workers' compensation program, the unemployment insurance program, the wage and hour provisions, and the tax provisions, utilize variations of the common law employer-employee relationship test to determine whether work is being prepared by an independent contractor. The lack of a uniform definition of independent contractor may weaken enforcement efforts by these agencies.

Individuals may sometimes allege independent contractor status to avoid compliance with laws relating to wages and hours, workers' compensation, unemployment insurance, and taxation. Independent contractor problems reportedly are most common in the construction industry. Contractors who have employees and who comply with applicable laws and administrative regulations complain that they are at a distinct competitive disadvantage with contractors who fraudulently or erroneously claim that they are independent contractors with no employees and evade the applicable statutory and regulatory requirements.

The independent contractor issue was the impetus for the enactment of House Concurrent Resolution (HCR) 60 during the 1994 General Assembly. HCR 60 directed the Interim Joint Committee on Labor and Industry to conduct a study of independent

contractors and to develop recommendations for the 1996 General Assembly. A subcommittee of the Interim Joint Committee on Labor and Industry is conducting the study.

Discussion

There is currently no definition of independent contractor in the Kentucky Revised Statutes. In legal dictionaries, an independent contractor is generally defined as "one who, in exercise of an independent employment, contracts to do a piece of work according to his own methods and is subject to his employer's control only as to end product or final result of his work" (Black's Law Dictionary). The employer-employee relationship to determine independent contractor status has derived out of judicial interpretation and common law guidelines.

Establishing a uniform definition of independent contractor is an option that has been discussed as a means of strengthening agency enforcement of laws and regulations. Proponents contend that it would result in a better understanding between state agencies as to who does, or does not, meet the definition. This understanding should lead to better communication between agencies when sharing information about individuals who might be improperly claiming independent contractor status, and help improve enforcement and compliance activities. A uniform definition might also reduce litigation, since it would mean more reliance on a concrete definition than on guidelines used in common law defenses.

Opponents argue that because agencies have different priorities when enforcing statutes, writing a definition that would be acceptable to everyone would be very difficult; some organizations would want a very strict definition of independent contractor; others wouldn't. Reducing the factors in the test to establish an employer-employee relationship would still involve subjectivity (some states, in determining independent contractor status, rely on many of the 20 old factors cited to make the determination). Because of this subjectivity, opponents contend, litigation would still be prevalent.

The improper use of independent contractor status, whether inadvertent or intentional, is a problem that is acknowledged by most state agencies. This situation is heightened, some people allege, because of lax enforcement of the statutes by those agencies.

Supporters of stricter enforcement of existing labor and tax laws relating to employers who inappropriately assert independent contractor status contend that it will result in fewer job-related injuries, improved employer compliance, broader coverage of employees regarding worker's compensation and unemployment insurance, increased tax receipts, and more equitable competition between employers.

Opponents argue that requiring agencies with limited budgets to more strictly enforce laws that relate to the employer/employee relationship will result in agency personnel being diverted from concentrating on more important agency issues. The

alternative is to allocate more money for the agencies to hire additional investigators and auditors. Opponents contend that this could ultimately lead to higher taxes and more bureaucracy within the agencies.

Problems associated with the independent contractor issue are not unique to Kentucky. Other states have attempted a variety of solutions to the issue, with varying degrees of success. Reducing the factors used in determining the employer/employee relationship, enacting licensing laws for contractors, and increasing fines and penalties for violating labor and tax laws are options that are being utilized by other states. Other options that could be considered in dealing with independent contractors include requiring proof of compliance with workers' compensation and unemployment insurance under the building code laws and establishing an interagency computer database to share information regarding employers.

LICENSING AND OCCUPATIONS

CHARITABLE GAMING

Prepared by Michael L. Meeks

Issue

Should the statute regulating charitable gaming in Kentucky be changed?

Background

In 1992, the Interim Joint Committee on Business Organizations and Professions (now Licensing and Occupations) completed and submitted to the Legislative Research Commission a report on the regulation of charitable gaming, as directed by Senate Bill 321 (1992 Session). That report concluded that a comprehensive system for regulating charitable gaming should be developed and enacted. Shortly thereafter, in November 1992, voters ratified an amendment to the Kentucky constitution authorizing legalized gaming for charitable purposes. The General Assembly then began the task of creating enabling legislation to regulate charitable gaming in Kentucky.

The Interim Joint Committee on Business Organizations and Professions, and subsequently the newly established Subcommittee on Charitable Gaming, looked at the issue of how to regulate charitable gaming. The subcommittee engaged in many hours of research, consultation, and deliberation. The subcommittee also listened to testimony from various interested and affected groups throughout the Commonwealth in an effort to define, and adequately regulate, charitable gaming. House Bill 206, proposed by the subcommittee and now codified at KRS Chapter 238.500 to 238.995, was passed by the 1994 General Assembly.

Recognizing that charitable gaming conducted by charitable organizations was an important method of raising funds for legitimate charitable purposes, the General Assembly sought to establish an effective and efficient mechanism for regulating such activity. It sought to define the scope of charitable gaming activities, establish standards for the conduct of charitable gaming that insure honesty and integrity, provide for a means of accounting for all moneys generated through the conducting of charitable gaming, and provide for suitable penalties for violations of laws and administrative regulations promulgated by the newly created Division of Charitable Gaming. The General Assembly also declared its intention to prevent the commercialization of charitable gaming, to prevent participation in charitable gaming by criminal and other undesirable elements, and to prevent the diversion of funds from legitimate charitable purposes.

Discussion

The Legislative Research Commission staff has received numerous written comments from the general public, various interested entities, and the Division of

Charitable Gaming, and has cataloged each suggestion. The Subcommittee on Charitable Gaming of the Interim Joint Committee of Licensing and Occupations is currently considering all suggested changes to the charitable gaming statutes in Kentucky. A bill has been prefiled, 96 BR 125, which proposes to substantially revise many provisions of the charitable gaming statutes.

The main elements of BR 125 include the following:

- To require the Attorney General, county attorneys, and Commonwealth's attorneys to notify the Division of Charitable Gaming of any intent to prosecute any violation of the charitable gaming laws;

- To allow charitable organizations engaging in charitable gaming to conduct two bingo sessions per week, and delete the authorization for suborganizations and subordinate organizations to conduct charitable gaming;

- To clarify which of those individuals associated with the charitable organizations must have a criminal history background check;

- To specify that certain organizations engaging in charitable gaming that is exempt under the current statutes must still qualify as a charitable organization under the provisions of the Internal Revenue Code;

- To allow certain public schools, institutions of higher education, and volunteer fire departments to engage in charitable gaming prior to receiving their 501(c) status;

- To require organizations engaging in charitable gaming to designate chairpersons for the charitable gaming activities, and require at least one chairperson to be in attendance and be in responsible charge of each charitable gaming activity conducted; and

- To impose a one-half of one percent tax on the gross receipt derived from manufacturers and distributors of charitable gaming equipment and supplies, and to impose a one-half of one percent tax on charitable gaming facilities. The revenues from the tax would be used to defray the cost of administration and enforcement by the Division of Charitable Gaming.

Other issues discussed include a repeal of the "tipping" ban. KRS 238.540(4) states that no person engaged in the conduct and administration of charitable gaming shall receive any compensation for services related to the charitable gaming activity. The statute further provides that any effort or attempt to disguise any other type of compensation shall be considered an unauthorized diversion of funds and shall be actionable under KRS 238.995(4). The division has interpreted this provision to prohibit any person from receiving money or anything of value for the performance of volunteer work. The Attorney General has issued an opinion upholding this interpretation. Conversely, many interested parties believe that the prohibition only applies to the

charitable organization and does not prohibit patrons of the gaming activity from "tipping" volunteers.

Another issue discussed is the regulation of raffles and pulltabs. The Division of Charitable Gaming has promulgated several administrative regulations that many in the industry believe to be unduly burdensome or unnecessary. The Division's position is that the administrative regulations that have been promulgated are necessary to insure the integrity of the charitable gaming activities.

Another issue discussed is the perceived unnecessary restrictions on marketing incentives. This complaint involves the prohibition on distributors and manufacturers of supplies and equipment from engaging in the managing, or otherwise being involved in the conduct, of charitable gaming; providing bookkeeping or other accounting services related to the conduct of charitable gaming; handling any moneys generated in the conduct of charitable gaming; advising a licensed charitable organization on the expenditure of net receipts; providing transportation services in any manner to patrons of a charitable gaming activity; providing advertisement or marketing services in any manner to a licensed charitable organization; or providing personnel or volunteers in any manner. This complaint also includes the prohibition on charitable gaming facilities from providing transportation services in any manner to patrons of a charitable gaming activity; providing advertisement or marketing services in any manner to a licensed charitable organization; or providing personnel or volunteers in any manner.

It is the position of the Division of Charitable Gaming that charitable gaming should be conducted solely by the charitable organizations through their volunteers, and that the other entities (i.e., manufacturers, distributors, and charitable gaming facilities) should not be involved in the day-to-day operations of charitable gaming. Further, the division states that to allow the additional help of another entity would have the effect of giving an unfair advantage to charitable organizations that utilize charitable gaming facilities, over the smaller charitable organizations that do not or cannot utilize such facilities.

REGULATING HOME INSPECTORS

Prepared by Vida Murray

Issue

Should the General Assembly regulate home inspectors to protect the public?

Background

Increasingly, real estate sales associates are suggesting that prospective home buyers obtain home inspections before purchasing homes. Under this practice, home inspectors visually inspect the house's various components, including its structure, exterior, roofing, plumbing, electrical system, heating system, central air conditioning, interior, insulation, and ventilation.

To date, five states regulate home inspectors: Texas, Maryland, South Carolina, North Carolina, and Oregon. Their statutes vary from less burdensome requirements such as those in place in Oregon and Maryland, respectively, which require home inspectors to register and pay a license fee, and disclose their educational training and on-the- job experiences to potential clients, to the more extensive requirements used in North Carolina, South Carolina, and Texas, which also require home inspectors to obtain a license.

In the majority of the states, a person may hold himself or herself out as a home inspector without satisfying testing or experiential requirements. However, some inspectors regulate themselves, by voluntarily obtaining certification from the American Society of Home Inspectors or similar organizations. The Society, with chapters in each state, establishes training requirements for its members, including written tests, on-the job training, and continuing education, standards of practice, and a code of ethics. The number of members who are certified by the American Society of Home Inspectors has grown gradually over the years. Today, there are 1,441 full-fledged members and 2,560 candidate members. The full-fledged members have satisfied the Society's certification requirements, which include passing a written test, having reports verified by the Society, and participating in a minimum of 250 fee-paid inspections; the candidate members are in the process of obtaining a license and have one or more unmet requirements.

In April 1995, the legislative body of the Lexington-Fayette Urban-County Government enacted an ordinance requiring any person doing business as a home inspector within the county's limits to be licensed. The requirements for licensure include: passing a locally-developed test or an approved equivalent, conducting 250 paid home inspections, participating in 100 home inspections under the supervision of a licensed home inspector, completing a minimum of 48 hours of approved classroom instruction, and completing 15 hours of continuing education when a license is renewed. Moreover, the ordinance "grandfathers", for a one-year period only, those inspectors holding a

regular business license or employed by a qualified home inspection business; requires home inspectors to maintain liability insurance and pay an annual fee; and penalizes those who practice without a license.

Discussion

The Interim Joint Committee on Licensing and Occupations is considering whether home inspectors should be regulated and, if so, how extensive the regulation should be. Proponents of regulating home inspectors assert that this regulation is necessary to safeguard the public from unscrupulous and incompetent inspectors. They note that since home inspectors are not required to meet acceptable standards of practice or satisfy any educational or experiential requirements, these inspectors may have little training or may be trained in only one specialty, which may cause significant physical or financial harm to the consumer. Moreover, the proponents assert that since home inspection is a unique practice and is dissimilar to the practices of other professionals engaged in the construction and sale of housing, professional home inspectors should meet certain requirements.

Opponents counter that the incidence of abuse by home inspectors is small and does not warrant government intrusion. They note that a minute number of the complaints received by local better business bureaus in 1993 involved home inspections. Other opponents assert that government regulation should be established only if needed and should be as unintrusive as possible. Others strongly oppose the enactment of laws which merely require registering and paying a fee, and posit that if government regulation exists, standards of practice should be established to assure consumers that a minimum level of proficiency is required of practicing home inspectors. They further note that home inspectors should take part in regulating themselves and that the regulating boards should be independent of those boards regulating other professionals involved in the construction and sale of housing. To support this contention, they assert that home inspection is a unique discipline, and its practice and goal of supplying the potential buyer with accurate and thorough information on the condition of the home is at odds with the goals of those whose main purpose is to sell houses.

LOCAL GOVERNMENT

SPECIAL DISTRICTS

Prepared by Bill Van Arsdall

Issue

Should the General Assembly take action to further regulate special-purpose local governments in Kentucky?

Background

Special districts are an important, if little known, form of local government. In Kentucky the term "special district" encompasses more than 30 different types of limited-purpose units of local government. While most special districts are created by one of two uniform procedures, they vary widely in the powers they possess, the functions they perform, and the way they operate.

For general purposes, special districts may be defined as subdivisions of the state (other than counties or cities) that are created to perform a limited number of services within a limited geographical area. They provide such important services as road building and upkeep, library services, sewage disposal, fire protection, water supply, and garbage pickup. It is estimated that there are 1335 special districts in Kentucky.

One reason for creating special districts has been the failure or inability of general-purpose county government to provide all the services desired by citizens. Constitutional limits on debt or taxing power have, in some cases, prevented general-purpose government from providing certain services. Special districts with taxing or bonding authority have provided a way to get around such limits, because they are independent of county government and their taxes or bonded indebtedness do not count as part of the county limit. Other reasons for the creation of special districts include the unwillingness of existing governments to assume new functions, the desire to take a particular set of services "out of politics," and the psychological appeal of applying a specific tax to a specific purpose.

Discussion

The independence that makes special districts a means of getting around tax and debt limits has been a source of criticism. Complaints have been raised that special districts are not accountable and that they create problems of coordination in local government. Specific criticisms include:

--The lack of county governments' control over the day-to-day operation of special districts.

--The lack of regular or complete reporting of special district fiscal affairs, limiting the public's ability to determine whether a district is well or poorly run.

--The tax burden on citizens, many of whom pay more property taxes to special districts than they do to county government.

--The power to spend and invest large amounts of money with little or no public comment.

--The appointment, rather than the election, of many board members.

--The lack of control over conflicts of interest of board members.

During the last eleven years the General Assembly has passed two pieces of legislation calling for financial reports by special districts. A 1984 law requires special districts to file annual budgets and periodic audits, and a 1990 law requires local governments to submit "uniform financial information reports" or risk losing state funds. Many special districts have complied with these reporting rules, but some have not, and the penalties for failure to comply are not always effective.

During 1995, the Interim Joint Committee on Local Government has discussed ways to make special districts more accountable to the public. Members of the committee have suggested tightening penalties, extending local ethics laws, and changing reporting requirements, in an effort to remove the barriers between special districts and the people they serve.

STATE GOVERNMENT

STATE LEGISLATIVE REDISTRICTING

Prepared by Clint Newman and Joyce Honaker

Issue:

How should Kentucky's state legislative district boundary lines be redrawn in order to comply with the Kentucky Supreme Court decision in *Joseph M. Fischer v. State Board of Elections, et al*?

Background

In December, 1991, the Kentucky General Assembly, in its Second Extraordinary Session, undertook the task of redistricting legislative district boundaries based on the population counts of the 1990 U. S. Census. Using a sophisticated computer-based geographic information system, the General Assembly created Senate districts with a population deviation range of -3.26% to +3.09% from the ideal population of 96,981. House districts were created with a population deviation range of -4.97% to +4.94% from an ideal population of 36,853. The Senate plan divided 19 counties, and the House plan divided 48 eight counties.

The plaintiff in the above cited case successfully challenged the constitutionality of the 1991 legislative redistricting, arguing that the redistricting plan unnecessarily violated Section 33 of the Kentucky Constitution. While requiring population equality, Section 33 prohibits the dividing of counties in legislative redistricting.

In a 5 - 2 decision, the Kentucky Supreme Court ruled, in essence, that population equality requirements and preservation of county integrity requirements should be better balanced in a redistricting plan and that fewer counties should be divided. The court found that the splitting of counties could be significantly reduced by adopting population variation limits of -5% to +5% from an ideal legislative district.

The Supreme Court has permanently enjoined the conduct of any election pursuant to the 1991 legislative district boundaries after January 3, 1995.

Discussion

As was the case with 1991 redistricting, the General Assembly must concern itself with equality of population, contiguity of area, and the preservation or creation of minority districts, pursuant to the Federal Voting Rights Act. As a result of the Fischer decision, population variation limits of +5 or -5% from the ideal and a reduction in the number of split counties become important goals in the upcoming redistricting deliberations.

RECOMMENDATIONS OF GOVERNOR'S COMMISSION ON QUALITY AND EFFICIENCY

Prepared by Joyce Honaker

Issue

What is the status of the recommendations of the Governor's Commission on Quality and Efficiency?

Background

In March, 1993, the Governor established a 55 - member Commission on Quality and Efficiency to develop recommendations to improve state government's efficiency and the quality of its services. The members were drawn from both the public and private sectors. A consultant, KPMG Peat Marwick Government Services, managed a study of these matters, which was conducted for the Commission by seven work teams of loaned state employees and private sector analysts, working under the guidance of seven committees composed of Commission members. The topics assigned to the committees and work teams were fiscal management, government operations, human resource management (state personnel), human services, public safety, technology, and workforce training.

The Commission's final report, *Wake-up Call for Kentucky: Out of Crisis, Into Action,* was delivered to the Governor and members of the General Assembly in late November, 1993. It contains over 200 recommendations for change, which the Commission estimated would result in a five-year net savings of $905.9 million, if adopted. Among the Commission's recommendations relating to the general operation of state government were proposals to:

- Establish a method to assess what state programs and services should be privatized;
- Consolidate state personnel systems and "reinvent" the merit system;
- Institute strategic planning and performance-based budgeting in state government;
- Use a legislative and executive consensus forecast for revenue estimating;
- Establish an Office of State Controller;
- Develop improvements in office space acquisition and management, and in state purchasing and procurement activities, generally;

- Merge the administration and support services of the Kentucky Retirement Systems and the Kentucky Teachers' Retirement System; and

- Build a statewide network of voice, video, and data transmission systems linking all 120 counties.

Several of the Commission's recommendations were implemented by executive order of the Governor or administrative action in 1993-94. Others were addressed in 1994 bills and enactments of the General Assembly. Among the recommendations of the Commission enacted in the 1994 Regular Session are the following:

- Authorization of pilot programs for new personnel management policies and practices in state agencies, subject to supervision by a Personnel Steering Committee and legislative oversight.

- Consolidation of state postal services, with an estimated annual savings of $825,000.

- Authorization for the Finance and Administration Cabinet to contract on behalf of state agencies and universities with entities operating an information highway.

- Creation of an Office of State Controller to centralize and improve cash management, accounting, and financial reporting functions of state government.

- Expansion of state government's video teleconferencing capabilities.

During the January, 1995, Second Extraordinary Session, the General Assembly passed HCR 8, directing the Interim Joint Committee on State Government to follow up on the Commission's recommendations. In March, the Finance and Administration Cabinet Secretary provided the interim committee with a status report on implementation. The Secretary emphasized that many of the Commission's recommendations are designed to initiate a long-term process of government reform, requiring the on-going commitment of the members of both the General Assembly and the executive branch. Progress made in implementing Commission recommendations since the 1994 Regular Session has included:

- Approval and initiation of pilot personnel programs in 12 state agencies, including a job re-engineering program in the Revenue Cabinet, a new performance planning and evaluation policy at the Kentucky Veterans' Center, and use of broadbanded classification models in the Department for Vocational Rehabilitation to allow employees in technical jobs to be promoted without necessarily moving into management.

- Development of a statewide strategic plan for economic development and detailed strategic plans for eight state government cabinets.

- The December, 1993, awarding of a contract to build a statewide information highway for voice, video and data transmission within four years.

- Establishment of a Privatization Commission to recommend criteria and procedures for determining what state programs and services should be privatized, focusing on long-term accountability, cost effectiveness, customer service, and employee needs.

The General Assembly can anticipate continuing interest in the recommendations of the Quality and Efficiency Commission. The Secretary of Finance and Administration noted that Commission members are exploring options for continuing the commission's work in the private sector. While implementation of approximately 170 of the Commission's 242 recommendations has been completed or is in progress, it is estimated that implementation of about one-fourth of the initial recommendations remaining will require legislative action.

PRIVATIZATION AND PUBLIC ACCOUNTABILITY

Prepared by Alice Hobson and Henry Marks

Issue

Should the General Assembly enact legislation to address purchasing, contracting, and public accountability in the privatization process?

Background

Recently, the Governor's Privatization Commission estimated that $399 million of taxpayers' money is spent on privatized state services in Kentucky. As this trend in Kentucky and in the nation continues, there may be increasing challenges to the public's right to know, as well as to the state's overall contracting and purchasing policy. The public may not have access to financial information about privatized services because the private companies claim the information is confidential or proprietary. The lack of access to financial data and other information makes it difficult for state agencies, legislative committees, and the public to adequately monitor and assess these privatized services.

As part of a study of the State Park system, the Legislative Program Review and Investigations Committee reviewed both the public and private operations of State Park marinas. Increasingly, the Parks Department has elected to privatize these marina operations, giving marina operators 15- to 20-year contract extensions and reduced commission rates, in exchange for the replacement of state-owned facilities with facilities built and owned by the private marina operators. In studying the marinas, the Committee encountered problems that illustrate the difficulties in monitoring and evaluating privatized businesses.

During its review, the Committee asked for financial audits of marinas operated by private businesses contracting with the Parks Department and the Finance Cabinet. The marina audits are filed annually with the Parks Department, pursuant to an administrative regulation and the operator's contract. The administrative regulation, 304 KAR 3:010, contains record-keeping and auditing requirements for all private marinas which are intended to permit the state to effectively evaluate the marina operations.

When the legislative committee asked to review these audits, the operator of the marina at Lake Cumberland State Resort Park sued the Committee to block both the Committee's and the taxpayers' access to audits of the marina. For many months, the private marina operator fought the Committee's effort to review these financial audits, claiming the audits contained proprietary information. After inspecting and examining the marina audits, however, the Franklin Circuit Court held that the audits were not confidential or proprietary under the Open Records Act. The Court said the release of these documents would not give an unfair commercial advantage to competitors. The Court of Appeals upheld the Circuit Court's decision.

On appeal, the state's Supreme Court affirmed the Committee's right to the audits under KRS 6.900 - 6.935, the Committee's enabling legislation. However, the court refused to allow the release of the audits to the public. The Court's opinion said the audits contain proprietary information that is exempt from disclosure under the Kentucky Open Records Act.

In a dissenting opinion, two Justices agreed with the lower courts that these audits should be available to the public. They said:

> . . . there is a trend in government toward the privatization of various services which have been traditionally performed in the public sector. It is thought that in many cases privatization would improve the efficiency, economy and delivery of services. However, it would be unfortunate that this worthwhile development might be tainted by the cloak of secrecy. It would be unfortunate if by contracting out any service, information which had been available to citizens and taxpayers could be hidden from public scrutiny. The result would be an absence of public oversight of both the private contractor and the public official who awarded such private contracts. When public funds are involved in any way, the public has an absolute right to expect that clear and open accountability be maintained.

Another factor which hampers public scrutiny of privatized services is the lack of competitive bidding and the length of the contracts. For example, Kentucky statutes do not specifically deal with privatizing marina operations. The Finance Cabinet has a great deal of discretion and has contracted many of the marina operations without competitive bidding. This procedure is a non-bid process, used when competition is not feasible or when there is only a single potential provider.

Discussion

The marina case could affect all legislative committees, since the Open Records law is an important information-gathering tool for legislators. Unlike the Program Review Committee, most committees do not have direct authority to subpoena records. Access to state agency records related to contracts with private businesses could be obstructed. Since legislative access to all state agency information is imperative to ensure sound public policy, the General Assembly may want to consider statutory language to assure this access.

Kentucky law does not address the general issue of privatization. The purchasing and procurement statutes found in the Kentucky Model Procurement Code (KRS Chapter 45A) do not deal specifically with privatization. However, the General Assembly provided for the privatization of adult correctional facilities in KRS 197.500-530, and these statutes could provide guidance in establishing reasonable procedures for privatization of other government services. Likewise, administrative regulations dealing with record-keeping and audits for marinas may provide useful elements in developing legislation.

The General Assembly could consider the following topics to ensure public accountability in privatization:

- competitive bidding on all projects;
- public hearings;
- submission of privatization proposals to the Capital Projects and Bond Oversight Committee;
- state agency oversight and powers;
- financial management requirements;
- language in all state contracts defining access to financial and other data;
- open records status for all private provider documents;
- legislative committee access to all relevant private provider records;
- State Auditor and Attorney General access to all relevant private provider records;
- unannounced inspections of facilities; and
- penalties for noncompliance.

UNIFORM ADMINISTRATIVE HEARING PROCEDURES

Prepared by Joyce Honaker and Mike Greer

Issue

What is the status of the implementation of 1994 legislation establishing uniform administrative hearing procedures for state agencies?

Background

The 1994 General Assembly enacted HB 334, which establishes a uniform procedure for hearings conducted by state administrative agencies. The bill contains an effective date of July, 1996, and outlines a procedure for preparation of amendments to conform current hearings laws to the uniform procedure. The uniform law, codified as KRS Chapter 13B, affects over 400 types of hearing processes in about 700 existing statutes.

With a new Division of Administrative Hearings in the Office of the Attorney General and the Legislative Research Commission overseeing, agencies are to prepare the draft amendments and may request exemptions of hearings from the uniform procedure. The Interim Joint Committee on State Government, and ultimately the 1996 Regular Session of the General Assembly, will review the conforming amendments and requests for exemption, which must be submitted with detailed justification.

Discussion

In 1994, the Attorney General appointed a chief hearing officer, and state agencies designated liaisons to work with the Attorney General's Office and LRC in preparing information and drafts for legislative consideration. In May, 1995, the Interim Joint Committee on State Government's General Government Subcommittee held hearings on 26 state agencies' requests to exempt 118 types of hearings, or approximately 25% of all hearing procedures identified, from the uniform procedure. It recommended granting a full, limited, or conditional exemption for eighty procedures and denying thirteen requests. In addition, agencies withdrew petitions for nineteen hearing procedures prior to or during the hearings. The Subcommittee took no action on six of the exemption petitions, after determining that the six hearing procedures did not fall under the purview of KRS Chapter 13B.

In May, the full Interim Joint Committee on State Government adopted the Subcommittee's report, in order for agencies to prepare and submit draft legislation containing conforming amendments by July, 1995. The recommended exemptions and conforming amendments will be considered by the interim committee prior to the 1996 Regular Session of the General Assembly.

LEGISLATIVE CODE OF ETHICS

Prepared by Joyce Neel Crofts

Issue

Should the General Assembly amend the Legislative Code of Ethics?

Background

In a February 1993 Extraordinary Session, the General Assembly adopted a new Code of Legislative Ethics (KRS 6.601 to 6.829). The code amended statutes originally enacted in 1976 and created new statutes to establish a comprehensive, updated set of guidelines for legislators to follow if their interests as private citizens and their duties as public servants conflict. The code created an independent commission with various oversight, advisory, investigatory, and sanctioning powers to implement the code. The code addresses such issues as disclosure of certain interests and finances, acceptance of gifts, nepotism, post-term employment restrictions, conduct relating to state agencies, contracting with state agencies, ethics education, honoraria, acceptance of campaign contributions from legislative agents (lobbyists), and legislative lobbying. The code provides for advisory opinions to assist legislators in complying with the code, and it includes certain civil and criminal penalties for those who fail to comply. In 1994 HB 891, the General Assembly amended the code in several areas.

Four legal challenges to the code have been initiated in Franklin Circuit Court:

1. *Associated Industries of Kentucky v. Commonwealth of Kentucky* challenged both the legislative ethics code and the executive branch ethics code on a variety of issues relating to lobbyists. Franklin Circuit Court upheld the registration, disclosure, and reporting requirements; found the prohibition against contingency fee lobbying constitutional; did not rule on whether certain penalties violate the First Amendment rights of association and petition; did not rule on the prohibition against lobbyists making campaign contributions; and found that the state's compelling interest in "maintaining the proper operation of democratic processes, including deterring corruption and the appearance of corruption, overbalances" any difference in treatment between paid lobbyists and unpaid lobbyists. A.I.K. appealed the judgment and asked that the case be transferred directly to the Supreme Court of Kentucky. The Supreme Court granted the transfer, and the case is pending in that court.

2. *Kelsey E. Friend, Senator of the 31st Senatorial District of the Commonwealth of Kentucky v. Kentucky Legislative Ethics Commission, et al.* challenged the code as violative of "numerous provisions of the constitutions of Kentucky and the United States." Franklin Circuit Court dismissed the case, citing lack of an actual controversy and stating that the dismissal "in no way

represents a decision on the merits of the issues brought before the Court." Senator Friend's appeal is pending in the Kentucky Court of Appeals.

3. *Thomas J. Burch, Representative of the 30th House District of the Commonwealth of Kentucky v. Kentucky Legislative Ethics Commission* challenged the code on constitutional grounds. The case is pending in Franklin Circuit Court.

4. *Golden Rule Insurance Company v. Commonwealth of Kentucky, Kentucky Legislative Ethics Commission, et al.* challenged the Legislative Ethics Commission's authority to compel disclosure of the amount Golden Rule spent on media broadcasts to oppose the Health Care Reform Act when it was pending before the legislature. KRS 6.821(4)(a)1. and 3. require a lobbyist employer to disclose the "total amount of lobbying related expenditures made by the employer" and to list a "complete and itemized account of all other amounts expended for lobbying." To "lobby" is "to promote, advocate, or oppose the passage, modification, defeat, or executive approval or veto of any legislation by direct communication" with legislators, the Governor, a cabinet secretary, or a member of the staff of any of those officials [KRS 6.611 (26)(a)]. Lobbying does not include "news, editorial, and advertising statements" in the media [KRS 6.611 (26)(b)2.]. The Court ruled that because the media campaign was of an "indirect" or grass roots nature, and therefore did not meet the statutory definition of lobbying, the Legislative Ethics Commission lacks the authority to compel Golden Rule to disclose amounts spent for broadcasts in opposition to the Health Care Reform Act. The Legislative Ethics Commission did not appeal the decision.

Under KRS 6.666(17) the Legislative Ethics Commission is required to submit a report to the Legislative Research Commission containing its recommendations for revisions in the code. The Legislative Ethics Commission formed a nine-member advisory committee, consisting of educators, newspaper publishers, legislative agents, former legislators, and a former U. S. attorney, to review the code and advise the commission regarding recommended changes. The advisory committee held six public meetings and presented its report to the Commission on May 24, 1995. On June 27, 1995, the Commission adopted its final report on recommended changes to the code and submitted the report to the Legislative Research Commission.

Discussion

Various recommendations for changes in the code have been discussed by the Legislative Ethics Commission and its advisory committee. Some of the major issues and recommendations addressed by the Commission are:

Spending Limit Reduction -- The code sets a $100 limit on the amount per year that legislative agents and their employers may spend for food and beverages consumed on the premises by each legislator and his or her immediate family [KRS 6.811(7)]; this is

considered an expenditure and must be reported. The Commission proposed deleting the $100 limit from the code and recommended that the general rule prohibiting legislative agents and employers from giving, and legislators from accepting, anything of value, be extended to cover food and beverages consumed on the premises. The Commission proposed two new exceptions to the provision prohibiting legislative agents and employers from giving anything of value to a legislator: (1) That agents and employers be allowed a $3 daily spending limit (to cover minor social courtesies such as offering cigarettes or mints) which could not be accumulated and would not have to be reported; and (2) That employers of legislative agents be allowed to provide food and beverages consumed on the premises for a legislator who is an invitee or program participant at a scheduled public meeting of a bona fide association.

Legislative Agents and Campaign Activities -- KRS 6.811(6) prohibits a legislative agent from making a campaign contribution to a legislator, a candidate for the legislature, or a legislative campaign committee. The code is silent regarding other involvement in political campaigns. The Commission recommended that the code be amended to: (1) Allow legislative agents to make campaign contributions to legislative races in the agent's own district; (2) Restrict an agent's ability to be involved in the management or conduct of the campaign of a legislator or legislative candidate; and (3) Prohibit legislative agents from serving as fund-raisers (not simply registered fund-raisers) in legislative races.

Disclosure of Gifts -- KRS 6.787 requires legislators, candidates for the legislature, and major management personnel in the legislative branch to disclose the sources (not amounts) of gifts of money or property with a retail value of more than $200 received by the filer or the filer's immediate family. KRS 6.811(6) prohibits legislative agents and employers from giving "anything of value" to legislators. The definition of "employer" (KRS 6.611) refers to a person or business entity that hires a lobbyist, and excludes an individual officer, director, or employee unless that person makes an expenditure for which he or she is reimbursed by the business entity. The Commission said there is a perception that the code allows certain business and organization representatives to give things of value to legislators even if their business or organization is an employer of a legislative agent. To counter this perception, the Commission recommended requiring filers of statements of financial disclosure to report sources of all gifts, not just money and property, of $25 or more.

Application of the Code to Legislative Lobbying Activities of Certain State and Local Government Agencies and of Colleges and Universities -- The code's definition of "legislative agent" does not apply to public servants who lobby on behalf of state agencies, local governments, and colleges and universities, unless the person engaged by a de jure municipal corporation, such as the Kentucky Lottery Corporation or the Kentucky Housing Corporation, an institution of higher learning, or a local government, has lobbying as a "primary responsibility" during legislative sessions [KRS 6.611(22)(b)]. The Commission said that executive branch state agencies have employees designated as "legislative liaisons" to represent the agencies' legislative interests. The legislative liaisons' objectives and activities "differ largely from those of the private sector" agents, but their duties to communicate with legislators are similar to those of their private sector counterparts. The Commission recommended that legislative liaisons be required to

identify themselves to the Commission by name and agency but not otherwise be subject to the lobbying provisions of the code.

Likewise, state institutions of higher learning, de jure municipal corporations, and local governments utilize persons to represent their legislative interests. However, the code considers these persons legislative agents only if their "primary responsibility" during legislative sessions is to lobby. The Commission said that the term "primary responsibility" has created confusion and resulted in few of these people actually registering. The Commission proposed eliminating the word "primary," thus applying the code to all of those representatives whose responsibilities include lobbying the General Assembly. It would not, however, apply to local elected officials.

Application of the Code to Indirect, or Grass Roots, Lobbying -- The code's definition of "lobby" means to promote or otherwise influence legislation through "direct communication" with a legislator, the Governor, a cabinet secretary, or a staff member of any of those officials [KRS 6.611(26)(a)]. Indirect, or grass roots, lobbying is not covered in the code, although certain legislative agents and employers spend vast amounts of money influencing legislation through media campaigns. The Commission recommends expanding the definition of "lobby" to include indirect lobbying as well as direct lobbying. The Commission said that the code should not in any way limit indirect communication but that amounts spent on it should be reportable. The Commission also pointed out that the code would maintain its current exemption for publications primarily designed for, and distributed to, members of bona fide associations or charitable or fraternal nonprofit corporations [KRS 6.611(26)(b)(4)]. Further, the Commission proposed a revision to clarify that news and editorial statements in the media by bona fide media representatives are not lobbying activities.

Other Recommendations -- Regarding other issues, the Commission recommends:

- Requiring legislative agents and employers to file reports quarterly each year, rather than six times during session years and three times during nonsession years.

- Allowing technical experts who limit their lobbying to public appearances before legislative bodies to communicate informally with legislators immediately before and after their public testimony without having to register as legislative agents.

- Resolving penalty inconsistencies between two related offenses by making both Class B misdemeanors. Under the giving and accepting "anything of value" provisions of the code, a legislative agent or employer who gives anything of value to a legislator, the legislator's spouse or child is guilty of ethical misconduct for the first violation; and the second violation is a Class D felony. On the other hand, a legislator's acceptance of anything of value is a Class B misdemeanor. The recommendation would make both violations a Class B misdemeanor.

- Clarifying an apparent discrepancy in the code by prohibiting legislative agents and employers from giving anything of value to the Governor or other executive branch officials if the agents and employers are attempting to influence legislation through those individuals.

- Deleting KRS 6.611(2)(b)(8)(e), to clarify that legislators may not accept travel expenses from legislative agents and employers. Under KRS 6.747(2), a legislator would still be allowed to accept prepaid, or be reimbursed for, transportation, food, and lodging for out-of-state travel associated with the performance of legislative duties if prior approval is obtained from the Legislative Research Commission.

- Amending the code to allow legislators and their children to accept benefits (e.g., meals, earned bonus vacations, even health insurance) offered by a spouse's employer, but only if the same benefits are offered to other, similarly situated employees.

- Allowing children of legislators, as well as spouses, to be employed by the employer of a legislative agent as long as the children or spouses are not employed to lobby.

- Prohibiting legislators from accepting campaign contributions during regular sessions of the General Assembly.

- Eliminating the provision that allows the Commission to issue confidential reprimands upon a finding of probable cause after a preliminary investigation.

- Allowing Commission members to receive compensation for participating in Commission-approved activities; and changing the deadline for the Commission's annual report from February 15 to March 15.

The Commission's report states that it discussed, but made no recommendations on, the following issues: suspension of legislators who are convicted of a crime, reduced registration fee for non-profit organizations, legislators and potential conflicts of interest, legislators' contact with state agencies, the legislator/attorney's right to practice law before state agencies, code of conduct for legislative agents, mandatory ethics training for legislative agents, changes in the Commission's educational activities.

LEGISLATIVE COMPENSATION

Prepared by Barri Christian

Issue

Should annual salary and expense allowances of General Assembly members be adjusted?

Background

HB 737, passed by the 1994 General Assembly in regular session, re-created the Legislative Compensation Commission to study and make recommendations on matters relating to legislative compensation, KRS. 6.226-6.229. Although it was originally created by the 1980 General Assembly, the provisions of the statute were never implemented and the Commission had never been activated prior to the implementation of HB 737. Resultingly, there is no current standard method by which to govern salary and expense adjustments for General Assembly members, should they be desirable or necessary.

Discussion

In its deliberations, the new Legislative Compensation Commission, meeting since March 1995, has studied the history of legislative compensation of Kentucky legislators from 1893 to the present; compensation data from all other states; time and expenditure data of current Kentucky legislators; and the effect of the CPI on legislative salaries and expenses.

The current salary for legislators is $100 per day while on legislative business, with members of leadership and committee chairs receiving additional pay for their additional duties. In addition, each member receives a stationary allowance of $50 for each session, a federally adjusted daily expense allowance of $74.80 during a session, an expense allowance of $950 per month during the interim , and actual travel expense reimbursement when traveling on legislative business during the interim. Mileage is reimbursed at $.25 per mile and is indexed to the federal travel rate.

The last salary increase for legislators was in 1984. The last monthly expense increase was in 1982. Since that time, some expenses that were not previously taxed have been deemed subject to tax withholding. For, example, whereas a legislator once received the full $950 monthly expense allowance, currently the average net take-home amount is approximately $554, with reimbursement subject to documentation of actual expenditures.

While executive branch constitutional officers' salaries are adjusted according to the consumer price index, under the "rubber dollar" theory, the legislature has not participated in this method of indexing, although several Attorney General's Opinions have

ruled it appropriate. Application of the annual CPI back to 1984 indicates that salaries and expenses would have increased 42.6% over current levels, had it been instituted at that time. If so implemented today, the cost of the legislative per diem would increase the legislative biennial budget by $1.17 million.

VETERANS' NURSING HOMES AND CEMETERIES

Prepared by Kenton G. Downey

Issue

Should the General Assembly authorize additional facilities for veterans' nursing homes and state-run veterans' cemeteries?

Background

The state of Kentucky, through the Finance and Administration Cabinet, operates the Kentucky Veterans' Center, a veterans' nursing home, in Wilmore. This is a 300-bed facility. The Kentucky Veterans' Center is 80% occupied. Kentucky's veterans' groups, led by the umbrella group the Joint Executive Council of Veterans' Organizations (JEVCO), are calling for establishing two additional 120-bed facilities, one in Western Kentucky and one in Eastern Kentucky.

There are four National Veterans' Cemeteries located in Kentucky. The Veterans' Administration estimates that by the year 2000 all four cemeteries could be full. Kentucky veterans' groups want to establish two state-run veterans' cemeteries, one in Western Kentucky and one in Eastern Kentucky.

Discussion

The state-run veterans' nursing home program constructs homes on a 65/35, federal/state, matching basis. The yearly operational costs are provided by Veterans' Administration reimbursements and General Fund appropriations. The Kentucky Veterans' Center should be filled sometime this year. The number of veterans requiring nursing home care is increasing, as the average age of veterans continues to increase. Kentucky's veterans' groups are lobbying for more General Fund money to move forward with their expansion plans. Many veterans' organizations are trying to alert Kentucky's veterans to the potential for establishing more homes.

Kentucky's Veterans' Organization, the Joint Executive Council of Veterans' Organizations (JEVCO), wants the state of Kentucky to enter into a federal-state program to establish state-run veterans' cemeteries. The program is a 50/50, federal/state, match on the construction phase of the project. Once cemeteries are completed, operation becomes the responsibility of the state. The operation funding would come from General Fund dollars.

VOTER ASSISTANCE

Prepared by Rob Williams

Issue

What changes are necessary to conform state election laws to federal law regarding voter assistance?

Background

Under Section 208 of the federal Voting Rights Act and KRS 117.255(3), a voter who requires assistance in voting because of blindness, disability, or inability to read or write English may be assisted by a person of the voter's choice, other than the voter's employer or an agent of that employer, or an officer or agent of the voter's union. However, amendments made to Kentucky law in 1994 prohibit a precinct election officer, a county clerk, or employee of a county clerk from providing assistance to a voter, and also prohibit any person from assisting more than two voters in any primary, regular, or special election. In October, 1994, a consent decree issued in a federal lawsuit challenging the restrictive provisions of Kentucky's voter assistance law found them to be invalid and unenforceable, because they unduly restricted a voter's right to have anyone of the voter's choice provide assistance, as guaranteed by federal law. Following discussions with the U. S. Department of Justice regarding permissible state restrictions on voter assistance, the State Board of Elections and the Office of the Attorney General advised county clerks and county boards of elections that even Kentucky's earlier statutory restrictions on voter assistance (as they existed prior to the 1994 amendments, requiring an election officer from each political party to render assistance when required, and setting a limitation against assisting more than two voters on election day) would violate federal law.

Discussion

Federal laws regarding voter assistance preempt state laws on the subject. The restrictions on voter assistance were enacted in 1994 as a vote fraud prevention measure, since vote buyers in some parts of the state would "assist" multiple voters in casting their ballots, especially absentee ballots, to ensure that votes were cast the way the buyers wanted. In some counties, collusion between precinct election officers further aided those vote buyers who wanted assurances that votes were being cast as intended. It appears that all current statutory restrictions on voter assistance must be deleted to comply with federal law, unless a compliance waiver is obtained on the basis of a demonstrated pattern of vote fraud achieved through voter assistance, which at this point appears unlikely. More stringent investigation and enforcement of the vote buying and selling prohibitions may be the only methods available to ensure that voter assistance is not used as a vote fraud technique.

PUBLIC FINANCING OF ELECTIONS

Prepared by Rob Williams

Issue

What changes should the General Assembly consider making to the law providing public financing of campaigns for Governor and Lieutenant Governor?

Background

In 1992, the General Assembly enacted legislation providing public financing of up to $1.2 million per slate of candidates for Governor and Lieutenant Governor to those who agree to abide by a spending limit of $1.8 million per election. As a further inducement to participate in the program, those slates agreeing to limit their spending may accept a contribution of $500 per person, PAC, political party, or contributing organization, while nonparticipating slates are limited to individual contributions of $100. Participating slates could be released from the spending limit if a nonparticipating slate raises or spends more than $1.8 million. A total of $11.7 million has been appropriated from the General Fund over this biennium to provide matching funds to participating slates. Since participation in the program must be voluntary, to avoid violating the First Amendment right of free speech, it is possible that a slate that chooses not to limit its campaign spending could spend more than $1.8 million, thereby releasing participating slates from the spending limit and again making them eligible for additional matching public funds above the $1.2 million for which they could be eligible. Since it is generally believed that no restriction can be placed on independent expenditures (those made by persons not affiliated with a campaign which are made without the slate's knowledge or approval), it is expected that the use of independent expenditures in this year's election will increase significantly over prior gubernatorial elections.

In November, 1994, two lawsuits were filed seeking an injunction against the law's implementation and challenging the constitutionality of several provisions of the law. Those provisions include the different contribution limits for participating and nonparticipating slates, the provision of additional matching funds to participating slates if a nonparticipating slate raises or spends more than $1.8 million, and the prohibition against a slate's acceptance of cash contributions. In January, 1995, a U. S. District Court ruled that the separate contribution limits for participating and nonparticipating slates were unconstitutional, but upheld the other challenged provisions of the law.

Discussion

Since the objectives of the public financing program are to reduce the amounts of money spent in races for Governor and Lieutenant Governor and to level the playing field for those candidates who are unable to self-finance an expensive campaign, the General

Assembly might first examine the level of participation in the program, to determine whether the desired results were achieved. In this year's Democratic primary, three of five slates agreed to limit their spending and accept public financing. In the Republican primary, only the slate which secured the party's nomination agreed to limit its spending. Both slates in the regular election are participating in the public financing program. However, while participation in this year's campaigns was generally considered to be satisfactory, there are circumstances that could affect application of the law in the future. If no credible slates participate in the program in a future election, and candidates again spend millions of dollars to seek election, it is logical to assume the need for the program might then be reevaluated. Likewise, if a nonparticipating slate spends so much in a future election that the appropriated funds can not provide participating slates with sufficient public funding, then the level of public funding appropriation or the spending limit itself may need to be increased.

The Registry of Election Finance is closely monitoring the use of independent expenditures in this year's election, to determine whether they are truly independent of a campaign's direction and thus should not be considered to apply against a slate's spending limit. The Registry is also likely to suggest changes to the public financing law to lessen the benefit which slates may derive directly from independent expenditures, especially those made by political parties. Part of the 1992 campaign finance reform law requires advertisers and publishers to provide identifying documentation for funds they receive to produce campaign advertisements. How well that documentation effort succeeds in preventing collusion between campaigns and those who seek to help the campaign without making their expenditures part of the candidates' spending limit will be critical if the program's objectives are to be realized. Expenditures made to benefit an all-but-announced candidate will also need to be examined, and some consideration may need to be given to establishing guidelines on exploratory efforts prospective candidates may make prior to filing candidate nomination papers.

The Registry promulgated several administrative regulations during the primary election period to respond to campaign finance scenarios which were not fully anticipated and addressed when the public financing law was enacted. It is expected that the Registry will recommend that the law be amended to incorporate the provisions of those administrative regulations, to round out the coverage of the public financing law. Issues addressed by administrative regulation this year include the manner in which slates may dispose of cash contributions they receive, the frequency with which slates may request transfers of public funding, the disposition of contributions received after a slate has accepted the permitted maximum to qualify for public funding, and the conditions under which a slate that has agreed to limit its spending may raise more than the maximum threshold qualifying amount in private contributions when no opposing slate qualifies for public funding.

The Registry is expected to submit its legislative recommendations for the 1996 Regular Session to the Task Force on Elections and Constitutional Amendments at its August meeting.

TOURISM DEVELOPMENT

KENTUCKY STATE PARK SYSTEM

Prepared by Mike Greenwell, Adanna Hydes and Hank Marks

Issue

Should the General Assembly amend KRS 148 to restructure management of the Kentucky Park System?

Background

Historically, the Department of Parks has been placed within a number of cabinets and agencies. The management of the park system has been located under the authority of the Board of Public Property, the Department of Conservation, the Commerce Cabinet and finally, in its current placement, within the Tourism Cabinet. The park system has not had ideal relationships with any of its previous Department locations, as each of these organizations is concerned with only a part of the multiple missions that the parks system must manage and address.

Discussion

During a management review of the state park system conducted by the Program Review and Investigations Committee, a common complaint from park managers centered on the fact that parks are not typical state agencies, and operating as such is burdensome, inefficient, and often ineffective. The committee adopted 19 recommendations directed towards assisting the park system with better management tools. However, in light of these recommendations, the park system still faces hurdles within state government and within its present location in the Tourism Cabinet.

The park system has missions beyond tourism, including natural and historical preservation, wildlife management, economic development and regional recreation. If the Parks Department were removed from the direction of the Tourism Cabinet, it would not be restricted by the conflicting or limited objectives of the Tourism Cabinet. For example, the Tourism Cabinet exists for the promotion of the private tourism industry. The resort parks are often viewed as competition by the private sector. The Cabinet may be placed in a conflicting role of supporting the private sector or the resort parks. As a revenue-generating (but subsidized) state agency, the parks should be encouraged to generate additional revenues, decreasing the burden on taxpayers. However, at this time initiatives undertaken to generate additional revenues, such as expansion of lodge accommodations or marinas, appear to be viewed as unfair competition by the private tourist industry, due to the subsidy from the General Fund.

Beyond conflicting missions, the park system is not a typical state agency. The unique nature of the park system requires more flexibility for successful operation and

management. The park system operates 24 hours a day, seven days a week, 363 days a year, generating income and providing services to paying customers, yet it is encumbered by state government agency operating statutes and regulations, particularly those relating to personnel and purchasing.

One of the recommendations adopted by the Program Review and Investigations Committee would require the Governor to appoint a Parks Advisory Commission. This commission would be composed of state government officials whose agencies might impact or be impacted by Parks operations, and by private sector individuals whose backgrounds include tourism, hotel and restaurant management, accounting and architecture. The responsibilities of this commission would include defining the Parks' mission, monitoring the implementation of the recommendations of the Committee's study, and implementing a Parks Department central management design which recognizes the changes evolving in Parks management and the tourism industry. Discussions at Commission meetings have arisen regarding the establishment of a foundation or similar board to assist the parks system in meeting its unique needs.

In its deliberations the Commission could consider options to present to the General Assembly to provide the Parks System greater flexibility in operation. However, these concerns would need to be weighed along with the concerns of those who perceive that removing the park system from government agency requirements may also remove the protections afforded by these requirements. Public confidence in the administration of tax dollars may be diminished if state regulations are relaxed.

TRANSPORTATION

GRADUATED DRIVERS' LICENSES

Prepared by Jeff Kell

Issue

Should the General Assembly establish additional restrictions for persons under twenty-one years of age who apply for drivers' licenses?

Background

Traffic accident studies and traffic violation statistics over the years have shown that, proportionally, teenage drivers have a worse driving record than the general population. This fact is reflected in higher automobile insurance rates. Many states have enacted legislation to restrict the driving privileges of juvenile drivers or establish such requirements as driver education or alcohol and drug awareness programs.

Discussion

Kentucky is relatively permissive on issuing driving permits and licenses. Imposing additional requirements upon young drivers holding Kentucky drivers' permits or licenses would require statutory authorization. These requirements could be defined in the statutes, or the Kentucky Transportation Cabinet could be directed by statute to promulgate administrative regulations creating a "Young Driver Provisional Licensing System," as described in SB 329, which was introduced in the 1994 Regular Session.

Proponents of tightening restrictions on young drivers say that young people should:

- be issued a "provisional" license until they are eighteen years old;
- be required to have supervised driving practice for a period of time after the issuance of an instruction permit;
- be subject to night-time curfews;
- be subject to stricter DUI standards; and
- have stricter points and suspension standards.

Opponents of tightening restrictions say that young people:

- often do not have a vehicle available to them that can be devoted to spending the time necessary to comply with a longer time period for obtaining a regular license;
- frequently need an unrestricted license right away because their job requires it;
- should not be subject to discrimination due to their age; and
- should not be penalized as a group because of the actions of a few.

INTERNATIONAL FUEL TAX AGREEMENT (IFTA)

Prepared by Jeff Kell

Issue

Should the General Assembly repeal the heavy motor carrier fuel surtax of two-cents on carriers over 60,000 pounds, in order to join the multi-state pact known as IFTA?

Background

Congress enacted the Intermodal Surface Transportation Efficiency Act (ISTEA) in 1991, which compels the states to participate in IFTA by September 30, 1996. This multi-state agreement allows a trucking company to register and pay fuel tax to its base state for operation in all member jurisdictions. A motor carrier based in Kentucky would send its fuel tax report to Kentucky, which then would be responsible for distributing the tax receipts to other states. As of May, 1995, thirty-five states have joined IFTA, including all of Kentucky's neighboring states.

Although there are some other minor compliance problems in the KRS relative to joining IFTA, the main problem seems to be the loss of tax revenue from the two-cents surtax on heavy vehicles. This tax is not levied at the pump but only on carriers' quarterly reports. According to the Executive Director of the International Fuel Tax Association, the surtax is not collectible under IFTA. It is estimated that this restriction would cost the Kentucky road fund approximately $7 million annually, unless it is willing to raise fuel taxes collected at the pump, which are not affected by IFTA.

IFTA is a mechanism whereby all states are being required to regulate and tax the trucking industry in the same way. States are not supposed to charge differential rates for different classes of motor carriers through any fuel tax reporting methods. If a state does not comply with IFTA, the Federal Transportation Secretary can seek an injunction prohibiting the state from collecting motor fuel taxes on interstate carriers. Thus an additional $30 to $40 million a year might be lost to the road fund if Kentucky does not join IFTA, since this is the range of revenue generated by the collection of the 5.2 cents per gallon tax on registered vehicles over 26,000 pounds that file fuel use tax reports.

Discussion

During the 1994 Regular Session of the Kentucky General Assembly, legislation was introduced (HB 285) to bring Kentucky into compliance with IFTA. This bill was sent to the Appropriations and Revenue Committee, where it died. The subject of IFTA compliance has been discussed on two occasions by the Interim Joint Committee on

Transportation, at its March and May 1995 meetings. Also it has been discussed at a Subcommittee on Budget Review meeting during the 1994-95 Interim.

Proponents of IFTA compliance are of the opinion that compliance will:

- Ensure that Kentucky does not jeopardize its ability to collect fuel tax surcharges from the trucking industry; and

- Possibly raise state revenues by simplifying the tax reporting requirements.

Opponents of IFTA compliance are of the opinion that:

- Kentucky does not want to raise fuel taxes or other taxes to make up for the approximately $7 million that would be lost from the two-cents per gallon heavy vehicle surtax; and

- If the two-cents per gallon surtax is removed it could prompt an overall restructuring of motor carrier taxation with respect to the usage tax and the weight distance tax.