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POLICY SPOTLIGHT

Prosperity amid Population Growth in Kentucky

Tax, housing, and labor reforms to support a stronger economy

JACK SALMON | JULY 2026

Americans made nearly 34 million interstate moves between 2018 and 2023, redistributing population, income, and economic activity among states. Kentucky ranked 22nd in net interstate migration, gaining 25,000 residents but losing \$630 million in income—suggesting it attracts lower-income movers while losing higher-income residents.¹ Research shows that taxes, economic freedom, and housing supply are key drivers of migration. Tax reforms have improved Kentucky’s competitive position, but tax code complexities, low housing permitting, and one of the nation’s highest occupational licensing burdens weigh on its appeal.

Tax Policy Reforms

The competitive landscape

Kentucky ranks 25th out of 50 states on the Tax Foundation’s State Tax Competitiveness Index. The Commonwealth has improved its tax climate by reducing the flat income tax and lowering sales tax rates. Kentucky still imposes county and municipal occupational and net profit taxes, creating additional complexity and costs. Kentucky also lacks a bonus depreciation allowance for corporate equipment investments, caps business expensing, and levies an inheritance tax. Compared with neighboring Indiana and Tennessee, Kentucky’s tax burden is less competitive, reducing its appeal to interstate movers.

Indiana	Flat income tax reduced from 3.15% to 2.95%; scheduled to fall to 2.85% by 2030 if revenue targets are met. No local income-based occupation taxes.
Tennessee	No state individual income tax. No local occupational taxes layered on top of state rates.
Kentucky	Flat income tax of 3.5% (down from 4.5% in 2023). County and municipal occupational license taxes and net profit taxes add to the burden. Business expensing capped at \$100,000 vs. \$1 million in most states. Inheritance tax affects beneficiaries across the income spectrum. Ranks 25th on State Tax Competitiveness Index.

¹ See Jack Salmon, “Interstate Migration Trends in the United States, 2018–2023: Where Are Americans Moving, and Why?” (Mercatus Policy Brief, Mercatus Center at George Mason University, July 2026). For the full analysis including sources, scan the QR code on the next page.

Recommended reforms

- **Continue phasing down the income tax rate** by protecting automatic rate-reduction triggers.
- **Reform or eliminate county and municipal occupational taxes** to improve overall competitiveness.
- **Modernize business investment incentives** by conforming to federal bonus depreciation.
- **Repeal the inheritance tax**, which puts Kentucky at a disadvantage relative to its neighbors.

Housing Policy Reforms

The supply gap

Kentucky issues approximately 3.4 housing permits per 1,000 residents annually—roughly half the rate of neighboring Tennessee (approximately 6.6 per 1,000). Constrained supply raises housing costs, reduces affordability for incoming residents and workers, and diminishes Kentucky’s attractiveness relative to peer states. The barriers are not primarily financial; they are regulatory. Slow permitting processes impose costs on developers that further raise the costs of the final housing products.

Recommended reforms

- **Permit residential and mixed-use housing development by right in commercially zoned areas.**
- **Reform minimum lot sizes.** Follow Texas by limiting minimum lot size requirements in larger municipalities and growth areas with water and sewer service.
- **Establish vested-rights protections.** Clarify when development rights become protected from zoning changes. As in Tennessee, rights could vest upon submitting a substantially compliant permit application.

Labor Market Freedom Reforms

The licensing burden

According to the Archbridge Institute, Kentucky has the 4th-highest occupational licensing burden in the US and ranks 2nd among the four states in the East South-Central region. Kentucky’s licensing barriers and number of licenses, above regional and national averages, raise the entry cost into licensed trades and reduce economic mobility—particularly for lower-income workers.

The portable benefits gap

More than 300,000 Kentucky residents work independently, yet many lack access to benefits because companies risk legal liability when providing benefits to nonemployees. Importantly, survey evidence shows that in the United States 80.3% of self-employed workers want to remain independent while 80.1% want access to portable benefits. Portable benefits legislation in the state would allow workers to access benefits without compromising worker flexibility or exposing companies to legal risk.

Recommended reforms

- **Expand universal recognition of out-of-state licenses** to eliminate unnecessary barriers.
- **Enact portable benefits legislation** that allows workers to create portable benefits accounts while enabling firms to contribute without triggering worker reclassification rules.



For more information or to meet with the scholar, contact
Mercatus Outreach, 703-993-4930, dschroeder@mercatus.gmu.edu or mercatusoutreach@mercatus.gmu.edu
Mercatus Center at George Mason University, 3434 Washington Blvd., 4th Floor, Arlington, Virginia 22201

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