

HB 2457 Proponent Testimony – written only
4.95% flat tax and corporate tax reductions
House Taxation Committee
Dave Trabert – CEO
March 21, 2023



Chairman Smith and Members of the Committee,

We appreciate this opportunity to submit testimony in support of HB 2457, which creates a tax rate of 4.75% on individual taxable income and reduces corporate income taxes. We support both, but our comments focus on the individual aspects of HB 2457, as that will produce the greatest piece of tax relief.

The new tax model is designed to give everyone a tax savings. An income tax rate of 4.95% is charged to taxable income in excess of \$11,250 for joint returns and \$5,624 for single individuals. Exempting the first \$5,624 single / \$11,250 married ensures that everyone pays less tax.

| High-Income Taxpayers Pay More Than Their Fair Share of Kansas Income Tax | | | | | | | | |
|---|-------|------------|-------|------------|-------|------------|-------|------------|
| Adjusted Gross Income | 2018 | | 2019 | | 2020 | | 2021 | |
| | % AGI | % Tax Paid | % AGI | % Tax Paid | % AGI | % Tax Paid | % AGI | % Tax Paid |
| Up to \$50k | 18% | 10% | 17% | 10% | 16% | 9% | 17% | 9% |
| \$50 - \$100k | 23% | 23% | 23% | 23% | 22% | 21% | 22% | 21% |
| Over \$100k | 59% | 67% | 59% | 67% | 62% | 69% | 61% | 70% |

Source: Kansas Dept. of Revenue, data for state residents as of Sept. 30, 2022. Rounded to zero decimal points.

The savings is smaller for people with lower incomes, but that is because people with higher incomes are paying a larger portion of the total income tax. For example, resident taxpayers with

adjusted gross income below \$50,000 account for 17% of total AGI but they only pay 9% of the total resident income tax. Taxpayers with incomes above \$100,000 account for 61% of total resident income but they pay 70% of the income tax.

Further, people with lower incomes will still pay a lower effective tax rate because a larger portion of their income is exempt from taxation. The adjacent example compares the results for a family of four with adjusted gross incomes of \$250,000 and \$40,000. Both families get a standard deduction of \$8,000 and personal exemptions totaling \$9,000 (four at \$2,250 each). They also have the first \$11,250 exempt from the 4.95% income tax.

| Lower Incomes Have a Lower Effective Tax Rate | | |
|---|----------------|-------------|
| Description | Married 2 kids | |
| Adjusted Gross Income | \$ 250,000 | \$ 40,000 |
| standard deduction | (8,000) | (8,000) |
| Personal Exemptions | (9,000) | (9,000) |
| Taxable Income | \$ 233,000 | \$ 23,000 |
| Exempt from taxation | \$ (11,250) | \$ (11,250) |
| Income that is taxed | \$ 221,750 | \$ 11,750 |
| Tax at 4.95% | \$ 10,977 | \$ 582 |
| effective tax rate | 4.39% | 1.45% |

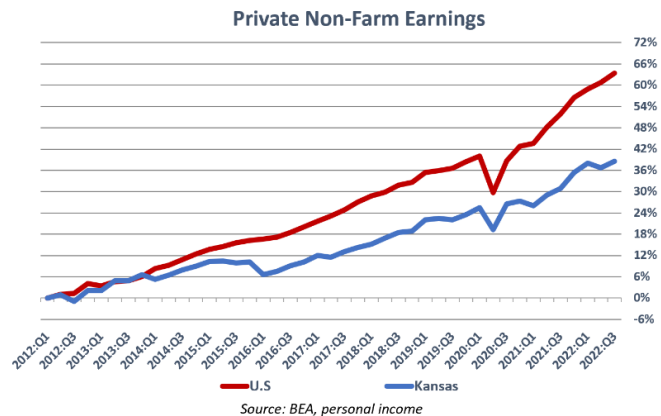
Source: SB 169

The family with the higher income would pay \$10,977 in tax, with an effective tax rate of 4.39% (tax divided by gross income). But the effective tax rate on the lower income is just 1.45%. So while the tax rate is the same for everyone, the mechanism in HB 2457 still results in progressive effective tax rates.

There are many ways to ensure that a move to a flat tax is implemented in a responsible, sustainable manner that gives everyone a tax cut. What's most important is that the Legislature

must provide as much income tax relief as possible for multiple reasons, including (in no particular order):

- Kansas is the third-worst state for taxation on retirees (Kiplinger).
- Inflation caused by excess federal spending is forcing many Kansas to pay higher state income taxes.
- Many states already have lower income tax rates than Kansas and others are cutting rates.
- Kansas is in its fifth straight decade of economic stagnation, and falling farther behind national average increases in job growth, population, and economic activity (GDP). Having high taxes and offering subsidies to a few businesses has proven to not work, and continuing down the same path only digs the hole deeper.
- The gap on private-sector non-farm earnings in recent years is especially troubling. The adjacent chart shows that Kansas grew with the national average in 2013. The near simultaneous plunge in oil and farm commodity prices in 2014 and 2015 created a growth gap that grew significantly worse after the Legislature imposed the largest tax increase in state history, and it gotten much worse in the last two years.
- Kansas was one of just 18 states that lost population between July 1, 2021 and July 1, 2022.
- States that spend less, tax less...and grow more. For example, between 1998 and 2021, the states without an income tax experienced private-sector job growth of 36%, while jobs grew by just 13% in the other states.



The balance of my testimony addresses the tax plan implemented under Governor Brownback, explaining some of the flaws in the plan and dispelling misinformation that continues to this day.

What was really the matter with the Kansas tax plan

Tax relief opponents in Kansas and other states repeatedly point to the 2012 Kansas tax plan as to say that tax cuts don't work.

But other states like North Carolina and Tennessee successfully cut taxes while Kansas struggled.

The Tax Foundation says, "Before the 2013 reforms, North Carolina consistently ranked among the worst states on the Index, indicative of high tax rates on a narrow tax base, with economically inefficient incentives and carveouts that benefited declining legacy industries. Since then, however, it has seen the most dramatic improvement of any state over the past decade, with reforms that broadened individual and corporate income tax bases and lowered rates, broadened the sales tax base to additional consumer services, and repealed the estate tax. These reforms have helped reverse the state's previously sluggish growth, with the state's GDP growth rates going from lagging

to exceeding the national average when comparing the seven years prior to the 2013 reforms to the seven years following. In addition, over the past decade, North Carolina has seen the third-highest net in-migration after only Florida and Texas, two states that forgo individual income taxes altogether.”¹

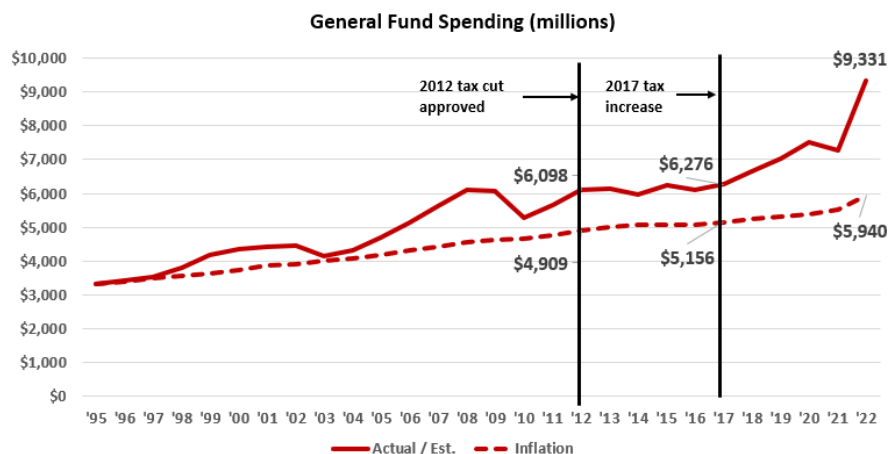
Tennessee improved its tax structure in 2022 when it completed the phaseout of the Hall Tax – the state’s income tax that was levied only on interest and dividends income.²

So what was different about the Kansas experience?

Many claims about Kansas are based on incomplete or inaccurate data, but Kansas did have serious budget challenges...and most of that was avoidable. There were a lot of mistakes made, and there were also other circumstances at play that created budget issues, including a very toxic political environment. A few examples of these issues follow.

Don’t cut taxes and increase spending

One of the major mistakes during the Brownback era was simultaneously implementing a large tax cut and spending increases. General Fund spending increased from about \$6.1 billion in FY 2012 to \$6.3 billion in FY 2017, when the Legislature imposed the largest tax increase in state history.



Source: Governor’s Budget Reports, KLRD, BLS Consumer Price Index Midwest Cities on fiscal basis

Claims that spending was drastically reduced simply are not accurate.

We encourage the Committee to examine a multi-year budget profile and adjust the implementation of HB 2457, if necessary, so that deficits are avoided.

Have a plan to balance the budget

Brownback’s original tax cut proposal was about \$350 million over five years, but it ballooned to \$3.5 billion by the time it left the Senate. Interviews with Governor Brownback revealed that there was never a plan to structurally balance the budget. Our analysis showed that small spending

reductions (2% to 3%) over three years would have balanced the budget and allowed spending to increase as revenues grew, and that could have been accomplished by enacting multiple efficiency opportunities. Unfortunately, Brownback, the Democrats, and some Republicans would not take advantage of those opportunities. Everyone knew the budget would go bust two years after tax cuts were implemented, but it was allowed to happen.

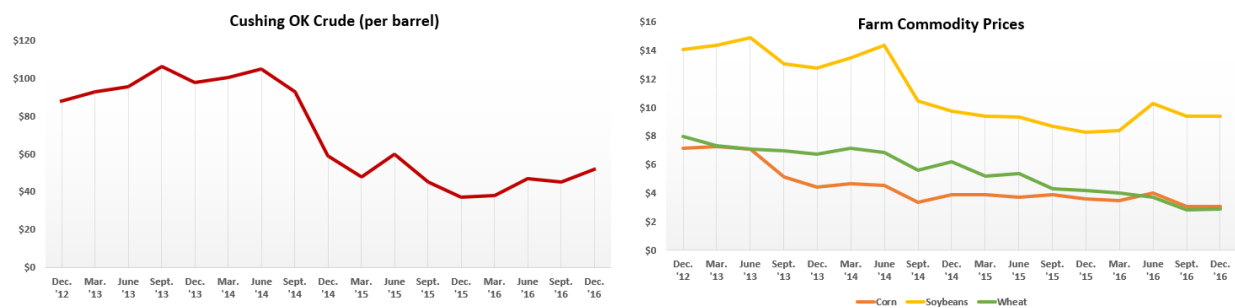
No promise that tax cuts will pay for themselves

Governor Brownback didn't say that tax cuts would pay for themselves, but that didn't stop the opposition from making the claim to discourage efforts in Kansas and other states.

His statement that tax cuts would be "a shot of adrenaline" to the economy may have given the impression that tax cuts would pay for themselves, but that was merely political exuberance, as politicians in both parties are known to do.

Oil and farm commodity prices plunged at the worst time

Just as the budget deficits were allowed to surface, prices on oil, corn, soybeans, and wheat dropped precipitously. That caused severe declines in severance tax and also sales and income tax related to agriculture.



Conclusion

The state has ample reserves to provide much-needed income tax relief now and use excess future revenue to trigger further tax cuts.

We encourage the committee to provide as much tax relief as possible and we thank you for your consideration.

¹ Loughead, Katherine, "North Carolina Reinforces Its Tax Reform Legacy," Tax Foundation, Dec. 3, 2021. <https://taxfoundation.org/north-carolina-tax-reform-2021/>

²Fritts, Janelle, "Tennessee Should Build on Success and Improve Corporate Taxes," Tax Foundation, Jan. 26, 2022. <https://taxfoundation.org/tennessee-tax-reform/>