

TESTIMONY BEFORE THE HOUSE TAXATION COMMITTEE

ARGUMENTS FOR THE REPEAL FOR THE SALES
TAX ON CONSTRUCTION SERVICES USED IN
COMMERCIAL REMODELING - HB 2585
BY GUS RAU MEYER
RAU CONSTRUCTION COMPANY
FEBRUARY 7, 2024

My name is Gus Rau Meyer, I live in Prairie Village, Kansas and am President of Rau Construction Company. Rau is a mid-sized construction company founded in 1870, and has been doing business in the Kansas City Metropolitan area since the early 1900's. Our main focus is on commercial, retail, and historic rehabilitation projects in the private sector.

Our customers are both the owner or developer who builds a new building or owns an existing structure, as well as the tenant who is renting a space and finishing it for their own use. The "Remodel Tax" impacts our customers in many ways. The first way is in the renovation of an existing space whether it is a commercial tenant finish, or a repurposing of a building or portions of a building to a new use. The second way is the new finishes in a previously unfinished space in a recently completed project. The second way in my personal opinion is the most insidious. When a space has never been finished out and has its first finishes installed whether it is 1 day or 2 years after the building was built and calling it a "remodel" that will have a significant tax collected upon that work since it was not part of the "Original Construction" is rather unfair.

Then we add on another layer of burden this tax causes. Although economic times have been good in the Eastern portion of Kansas, the economic demands on remodel construction have become more severe. With the high cost of construction, increase in on-line retail sales, work-from-home transition after COVID, and other factors; new construction in the sectors we work in has fallen in the past decade. When companies look to relocate, they are often looking at moving to an existing building.

The competition between local jurisdictions, on both sides of the state line (Kansas and Missouri) makes the decision as to where to relocate or renovate very intense. When our clients are comparing equal designs, the two major items which will determine the ultimate location of a project are based on the economics of construction costs. The biggest variable we typically see in construction costs is Sales Tax on Construction Services, known as the Kansas Remodel Tax.

This is a significant economic development issue for the commercial real estate industry. We are asked by clients to determine for them what the impact of the Kansas Remodel Tax is on their project. Each project is different in the makeup of the scope of work, but the analysis typically shows that cost of the Kansas Remodel Tax as 2.4% to 3.0% of the overall cost of the project. In a business where a fraction of a percent in cost or rental rate may cause a tenant to choose a Missouri site over a Kansas site, a 2 ½% difference in the project cost due to the Kansas Remodel Tax can be a significant difference.

Then there is another layer of burden this tax causes. That is the difficulty in administering this tax. This is from the standpoint as a remitter; and I feel I am safe to say it is also difficult from a collection perspective. As a company who prides itself on exceptional accounting practices, we have found we always have a problem in this area during sales tax audits. The interpretation on what constitutes remodeling appears to be subject to change depending on the person making the audit.

As an example, we recently completed a large historic renovation in Kansas. The building was initially built as a hotel in the middle of the last century. The project was a major economic and social win for this town. It was clear that the bulk of the project did not have the "Remodel Tax" as it created over 100 units of housing, which is exempt from this tax. The question then becomes what about the work to the old Ballroom? This was not going to be apartments. Was it going to be ancillary space for the apartments, which is a little "grey" about if "Remodel Tax" should be collected. Was it going to be some other public or commercial space, which would then have "Remodel Tax" collected on it. What if the use of the space was not determined would rebuilding the infrastructure of the building for future finishes require "Remodel Tax" to be collected. And, if "Remodel Tax" is required for this portion of the work, how do you determine where to start and stop with the cost of the exempt work and the non-exempt work. This is one example of what we go through on almost every remodel project in Kansas. Ask 5 auditors from the State and you will probably get 5 different answers.

Finally, there is the practical problem. When working in the eastern quarter of Kansas and we are competing on a renovation and/or remodel project, we come across many contractors that are bidding to us, or we are bidding against, that are not paying the "Remodel Tax". It is not well publicized, it is not fully enforced due to the difficulty to enforce, and we suspect that enforcing this tax will probably cost more than the money collected from that enforcement.

We urge your support of HB 2585. It is time to join our neighboring states in how they tax commercial construction. Repeal the "Remodel Tax on Commercial Construction".

Per the attached analysis of 2 recent remodel projects in Kansas, approximately 2.56% of the total cost of the project goes to pay this tax. In an industry where a fraction of a percent in a rental rate may cause a tenant to choose a Missouri site over a Kansas site, a 2.56% difference in the remodel cost can be a significant difference.

TESTIMONY BEFORE THE HOUSE ASSESSMENT AND TAXATION COMMITTEE
ARGUMENTS FOR THE REPEAL FOR THE SALES TAX ON CONSTRUCTION SERVICES
USED IN COMMERCIAL REMODELING - HB 2059
BY GUS RAU MEYER
FEBRUARY 3, 1999

As I mentioned before, I am submitting with this testimony an analysis of the effect of the Sales Tax on Construction Services concerning Remodeling has on two recent projects in Kansas. On a hypothetical \$500,000 remodel project. The Sales Tax on Construction Services, paid by all Contractors on this hypothetical project would amount to \$13,100 or 2.62% of the cost of the project. Examples of a project of this size would be a 15,000 to 30,000 square foot tenant finish, or a renovation of a small to average size downtown building. This "hypothetical" project could be found in any area of the state, especially the renovation of an older building. This is in addition to the Sales Tax on Materials.

Although I am not an economist or an actuary, my own analysis of this issue is every project which chooses another state to locate in or is not done because of these economics, are far more of a loss to the State than the loss of sales tax revenue. I feel the elimination of the Sales Tax on Construction Services could result in an increase in revenues from other tax revenues (Sales Tax on Materials, Property Tax, Income Tax, etc.) due to an increase in projects being done in the State of Kansas. These are projects that would not have been constructed or would have been done in other states if this Tax was still in place. This increase in these other tax revenues, coupled with the other economic benefits of more business and jobs, far outweigh the income realized by the State from this Sales Tax on Construction Services.

In conclusion, as a lifelong resident of Kansas, and a backer of its high quality of life and standard of living, I feel this Tax is a burden upon me and my State as it relates to its difficulty to administer and subsequent enforcement, and restriction to economic development as it effects small businesspeople to real estate developers. It is hurting the people who live and work inside the state boundaries and do not have a choice as to where to build their business by significantly increasing their cost. It also, and more importantly, drives people who have a choice around the perimeter of the state, away from Kansas.

I thank you Mister Chairman and members of this committee for allowing me to appear before you today. I appreciate your consideration and ask for your support in repealing this Tax as outlined in HB 2059. If you have any questions, I would be glad to address them.