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Sam Brownback, Governor

March 8, 2011

The Honorable Les Donovan, Chairperson
Senate Committee on Assessment and Taxation
Statehouse, Room 123-E
Topeka, Kansas 66612

Dear Senator Donovan:

SUBJECT: Fiscal Note for SB 98 by Senate Committee on Assessment and Taxation

In accordance with KSA 75-3715a, the following fiscal note concerning SB 98 is respectfully submitted to your committee.

SB 98 is a comprehensive tax proposal that would affect retail sales, individual income, and corporate income taxes. Specifically, the bill would make the following tax policy changes:

1. Begin collecting state and local retail sales taxes on digital products and most services, except for ambulatory healthcare and hospital services, on January 1, 2012;

2. Lower the individual income tax rates effective in tax year 2012;

3. Lower the corporate income tax rates in tax year 2011 and eliminate the corporate income tax in tax year 2012;

4. Lower the state retail sales tax rate to 5.3 percent effective January 1, 2012, and adjust the distribution of revenue between the State General Fund and the State Highway Fund;

5. Remove a number of specific sales tax exemptions that exist in current law. Some of the exemptions that would be removed include: coin operated laundry services; customized computer software; labor services for construction; residential and agricultural use utilities; bingo cards; charitable organizations that are listed by name; and purchases made by the federal government, State of Kansas, local governments, schools, and nonprofit hospitals; and

6. Provide a sales tax exemption for food and food ingredient products and repeal the food sales tax refund program.

The Department of Revenue estimates that SB 98 would have no fiscal effect on revenues to the State General Fund, State Highway Fund, or any other state fund in FY 2012 and FY 2013. The bill would be revenue neutral for the State General Fund, as additional revenue collections from specific tax sources would be offset by reduced collections from other specific tax sources in both FY 2012 and FY 2013. The redistribution of revenues and how the November 2, 2010 consensus revenue estimate for FY 2012 would be affected are shown in the following table:

Effect on FY 2012 Consensus Revenue Estimates
(Dollars in Thousands)

Receipt Description	Consensus Revenue Estimates (Nov. 2, 2010)	Change in Revenue FY 2012	Proposed Adjusted CRE FY 2012
Motor Carrier	$ 27,000	$ --	$ 27,000
Income Taxes:			
Individual	2,705,000	(87,000)	2,618,000
Corporate	275,000	(190,000)	85,000
Financial Institutions	21,000	--	21,000
Excise Taxes:			
Retail Sales	2,090,000	277,000	2,367,000
Compensating Use	295,000	--	295,000
Cigarette	97,000	--	97,000
Corporate Franchise	8,000	--	8,000
Severance	94,300	--	94,300
All Other Excise Taxes	96,400	--	96,400
Other Taxes	127,000	--	127,000
Total Taxes	$5,835,700	$ --	$5,835,700
Other Revenues:			
Interest	$ 11,800	$ --	$ 11,800
Transfers	(93,700)	--	(93,700)
Agency Earnings	56,800	--	56,800
Total Other Revenues	($ 25,100)	$ --	($ 25,100)
Total Receipts	$5,810,600	$ --	$5,810,600

To formulate these estimates, the Department of Revenue reviewed data on retail sales tax collections, sales tax exemptions, individual income tax collections, and corporate income tax collections. The Department of Revenue indicates that the bill would increase retail sales tax collections by $277.0 million in FY 2012 by collecting additional revenue from repealing certain sales tax exemptions, imposing the retail sales tax on certain services, and by reducing the state sales tax rate. Lowering the individual income tax rates is estimated to decrease revenues by $129.0 million in FY 2012, which would partially be offset by a $42.0 million increase in individual income tax revenue from eliminating the food sales tax rebate credits. Lowering the corporate income tax rate in FY 2012 is estimated to reduce receipts by $190.0 million. In FY 2013, the bill is estimated to increase retail sales tax collections by a total of $683.4 million, decrease individual income tax collections by $394.6 million, and decrease corporate income tax by $288.8 million.

The Department of Revenue indicates the bill would require $113,109 from the State General Fund in FY 2012 for administrative costs to implement the bill and to modify the automated tax system. The required programming for this bill by itself would be performed by existing staff of the Department of Revenue. However, if the combined effect of implementing this bill and other enacted legislation exceeds the Department's programming resources, or if the time for implementing the changes is too short, expenditures for outside contract programmer services beyond the Department's current budget may be required.

The Kansas Department of Transportation (KDOT) indicates the bill would reduce sales tax revenue dedicated to the State Highway Fund by $143.4 million in FY 2014 and by $162.0 million in FY 2015. It is estimated that sales tax revenue dedicated to the State Highway Fund would be reduced by a total of $1.2 billion between FY 2014 and FY 2020, and expenditures would also be reduced by the same amount over this time period. KDOT indicates the bill would not allow it to fully fund the new ten-year comprehensive transportation plan, known as T-WORKS, which was passed by the 2010 Legislature. The reduction in dedicated State Highway Fund revenue would also reduce current KDOT bonding authority by an estimated $200.0 million. KDOT also indicates the bill would remove a sales tax exemption that it currently uses when purchasing contractual services, commodities, capital outlay, and capital improvements. Removing this sales tax exemption would increase costs and would further reduce the number of projects that would be funded under T-WORKS. However, KDOT is unable to estimate the precise fiscal effect associated with the removal of its current sales tax exemptions.

The bill would increase costs for state agencies, local governments, schools, nonprofit hospitals, certain nonprofits groups, and other individuals and groups by removing current sales tax exemptions. The potential fiscal effect of requiring additional state expenditures to pay state and local retail sales taxes or providing reduced state services as a result of now being required to pay state and local retail sales taxes is not accounted for in this fiscal note. Any fiscal effect associated with SB 98 is not reflected in *The FY 2012 Governor's Budget Report*.

The Kansas Association of Counties and the League of Kansas Municipalities indicate that the bill would increase expenditures by local governments by removing the sales tax exemption on all purchases of property and services made by local governments. The bill would also increase local sales tax revenue by collecting local sales taxes on sales of certain property and services that under current law is exempt from paying state and local retail sales taxes. However, the Kansas Association of Counties and the League of Kansas Municipalities are unable to estimate the net fiscal effect of this bill on local governments.

Sincerely,

Steven J. Anderson, CPA, MBA
Director of the Budget

cc: Steve Neske, Revenue
Ben Cleeves, KDOT
Melissa Wangemann, KS Association of Counties
Larry Baer, League of KS Municipalities