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Testimony Before the
Senate Committee on Assessment and Taxation
on
SB 316 Tax Limits

by
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Mr. Chairman, Members of the Committee:

Thank you for the opportunity to testify on SB 316.

For 34 years I have worked as an investment banker in the field of public finance. Most of that time has been spent in Kansas My areas of expertise include long term planning for capital improvements, budgeting, debt issuance, municipal credit analysis and rating agency presentations and bond issuance and marketing. Over the years, my clients have included municipalities from all corners of Kansas. I am here presenting my own views on this legislation. I do not represent any other city, county, association or company.

First I'd like to make a general comment about revenue limits.
Property taxes are the cornerstone of local government finance. Some cities are blessed with economies which produce significant sales taxes and other fee incomes. For others, particularly smaller, rural governments property taxes comprise nearly all revenues. While property taxes are the most predictable and dependable revenues available, tax collections are adversely affected by economic downturns while sales taxes and fee incomes are even more dramatically impacted by those same events. The effects on an economic downturn on a city are complex and are not accurately reflected in CPI. When the will of the public is to provide a service revenue limits negatively impact bond ratings, increase borrowing costs and cause expensive workarounds. In the long run, revenue limits are destructive to credit quality.

My next comments relate to the deletion of certain exemptions contained in the original legislation.
The first of these relates to the existing exemption for road construction costs. Kansas has a good highway system. KDOT initiatives have proven to be popular because voters understand that our highway systems are the economic lifelines of the cities in our state. When KDOT makes road improvements cities and counties are asked to share the cost of those improvements. Intersection improvements, traffic lighting, curb cuts and entry and exit lanes just a few examples. These improvements are often required for important economic development projects where commitments must be made quickly. If cities don't have the ability to provide that cost sharing it will compromise KDOT's efforts to stretch it's budget and the local and state economy could suffer. For this reason I believe the exemption for road construction costs in existing legislation should be protected.

Second, the exemption for losses of valuation due to legislative or judicial action. Over the years we have seen changes in assessment ratios and exemptions from taxation. These changes often occur to promote economic growth. Two not too distant examples are the exemption of merchants and manufacturing inventories and the exemption of farm machinery and equipment. Without debating merits what we know is that these changes caused sudden and abrupt changes in assessed values as well as the distribution of property tax collections. Some cities and some regions are always harder hit than others. Our local governments have responded to these events in the past. Creating a condition where municipalities are unable to respond to abrupt changes in tax base will create a hardship the next time we see this kind of an event. I believe the exemption for legislative and judicial action contained in the original legislation is warranted and I encourage you not to remove it.

My third comment deals with the exemption for expenditures mandated by federal or state law. There are very few examples of a federal or state agency asking a city or county to do something and the local government simply agreeing. When mandates occur the issue at stake is nearly always public health, public safety or the environment. EPA tactics are what I typically call "carrot and stick". They will offer a subsidized loan followed quickly by the threat of an enforcement action. Enforcement actions occur because public health or the environment are at risk. The level of health risk can be debatable or very real and clear. In a situation where remediation is necessary to protect public health from a clear and present danger, rapid response is necessary. Requiring an election to be held could be a real problem. I have always felt lawmakers in Kansas understood this as our statutes have allowed municipal governments to work with regulators when forced to do so. I encourage the committee not to remove the exemption for mandated expenditures in the existing legislation.

My last comments deal with the change in the effective date of this legislation.
The challenges cities face are significant. While balancing the efficient provision of public services which often compete with one another for scarce tax dollars, local governments must also protect critical contingency reserves and maintain the budget flexibility to deal with recessions and extraordinary events. They must do all this while keeping the overall levels of taxation defendable and tolerable to their most vocal critics. At the local level these officials know very clearly that they will not be reelected if they can't achieve these goals.

Real property assessment procedures vary and assessments are not perfectly reflective of market prices. When we follow other measures of economic growth such as sales tax receipts we see patterns of growth which are anything but smooth during times of economic growth and contraction.

During the great recession it became very clear to me that local government would be among the last sectors of the overall economy to recover. Property tax revenues lagged economic activity. Spending initiatives and needed bond issues were delayed or scrapped because unemployment was high and consumer confidence low. In the healthiest areas property tax revenues did not begin climbing until 2015 even though real property values as reflected in the price of home sales began to gradually improve two years earlier. In other areas property values are still flat. None of this is captured in CPI.

Local fiscal health has not yet fully returned to pre-recession levels as economic activity clambers back. While tax revenues have begun to improve they have been more than offset by increases in service costs, long-term infrastructure needs, employee wages, and pension and healthcare obligations, along with decreased levels of state and federal aid. All of these costs have risen faster than the level of inflation and continue to constrain municipal budgets.

The reason I am framing all this out is to point out that local governments have been dealing with dynamic complex challenges. Needed projects were delayed and fund balances drawn down to deal with challenges and only now are we getting to a point where real progress is being made to catch up and to protect against the next challenge.

Large portions of our state are now dealing with yet another recession. The decline in oil and gas prices has caused the assessed valuations of some counties to drop by as much as 30% from 2014 to 2015 (source: KS Dept of Revenue). This occurred abruptly, in a single year. While we initially hoped this would be a single year dislocation, it is now clear that energy prices will remain depressed for longer than expected and these same jurisdictions could be facing further reductions in tax base this year.

Even though the proposed legislation anticipates declines in valuation, it does not in my opinion address the reality of this event. Even without this legislation the Counties facing the most significant drops can't simply reallocate all lost taxes onto the backs of other property owners. The shift in tax burden onto those constituents would be too dramatic and a hardship. Important services have been cut and fund balances have been drawn down in order to ease the pain. The three year average of past valuations which this legislation allows will not address what has happened in a single year. If revenue limits are initiated this year these local governments will not be given the time they need for oil and gas prices to improve. Needed public services can't be resumed and contingency reserves replenished until this happens. Immediate implementation of the revenue limits in this legislation will create an even greater financial hardship.

January 1, 2018 will be here soon enough. Moving the effective date of this legislation forward will create hardship for our cities and counties and the citizens they serve and is unnecessary. This legislation will be viewed as credit negative by bond rating agencies and investors and I ask members of the committee to vote no.