

Approved: 1-31-96
Date

MINUTES OF THE HOUSE COMMITTEE ON TAXATION..

The meeting was called to order by Chairperson Phill Kline at 9:07 a.m. on January 25, 1996 in Room 519-S of the Capitol.

All members were present except: Rep. Lawrence
Rep. Powell

Committee staff present: Chris Courtwright, Legislative Research Department
Tom Severn, Legislative Research Department
Don Hayward, Revisor of Statutes
Shirley Sicilian, Department of Revenue
Ann McMorris, Committee Secretary

Conferees appearing before the committee: none

Others attending: See attached list

Chair introduced Rep. Rocky Nichols who explained a proposed House Concurrent Resolution to amend the constitution of the state of Kansas relating to the taxation of property. This amendment would provide for tax year 1997 and all tax years thereafter on the aggregate of property tax levied on property used for residential and commercial purposes.

Moved by Rep. Larkin, seconded by Rep. Mays, the committee introduce a resolution to amend the constitution of the State of Kansas to impose property tax caps on residential and commercial and industrial real property. Motion carried.

Chair called on Chairman August Bogina for an update on the operation and function of the Kansas Board of Tax Appeals. (Attachment 1)

Chair called on Shirley Sicilian of the Department of Revenue for a review of the various flat tax proposals before Congress. (Attachment 2)

Chair asked for committee bill introductions. None were made.

The next meeting is scheduled for Janaury 31, 1996.

Adjournment 10:20 a.m.

Attachments - 2

COMMENTS TO
HOUSE TAXATION COMMITTEE
JANUARY 25, 1996

Mister Chairman and Members of the Committee, I welcome the opportunity of discussing with you the operation and function of the Board of Tax Appeals. During my appearance before the interim committee on November 7, 1995, I presented those members with information that indicated a sampling of the types of decisions that the Board encounters. Also included therewith was a tabulation of the case load that existed at that point in time. Since the majority of your members did not serve on that interim committee, I am enclosing copies of those same documents. With your indulgence, this will be a duplication for those members who served on the interim committee. Also included in your packet is an updated report of the case filings/case workload measures of the Board.

As an update, I would note that the Governor's budget recommendations for the Board do reflect that we have reduced our appropriations for fiscal year 1996 by 1 1/2% and reduced our FTE by 2%. We have also reduced our FTE by 3% for the next fiscal year with the appropriations reflecting those adjustments.

I believe we have fulfilled our intention to bring a more timely closure to the appeals process, especially the non-represented residential requests for relief. All of the residential appeals that were not represented by an attorney and/or a tax representative that were filed in 1995 were heard in 1995. We accomplished this goal by assigning a Board member as a hearing officer and holding hearings in the taxpayer's locality. Through this process we were able to schedule as many as four different hearings in different cities to accommodate the taxpayer/appellee. Each of these hearings was audio-recorded with a staff attorney present. The Board, as a

whole, then was able to review the case by using the file, audio-recording, and notes prepared by the hearing officer and the attorney. Although every participant may not have been totally pleased by the results of those hearings, I believe the process was well accepted. We will continue this format to resolve the residential appeals of taxpayers.

Hearings of appeals of commercial properties are heard in Topeka by the entire board. Occasionally, we do have hearings simultaneously in each of our two hearing rooms with our five member board split numerically between those proceedings. A record of all of the commercial and industrial hearings is prepared by a certified court reporter member of our staff. I have enclosed herewith a copy of our calendars through April, 1996, which indicate the commercial (Comm), Director of Taxation (DT) and represented residential hearings (HRGS).

I am not, at this time, prepared to furnish recommendations to you for statutory changes to improve the operation of our Board. I would submit, however, in response to the interim committee's request, a tabulation of a survey of the "Arbitration of Classification or Valuation Grievances." The result of that survey is as follows:

ARBITRATION OF
CLASSIFICATION OR VALUATION GRIEVANCES
KSA 79-1494 (as per County officials)

Ellis County - one appeal
Shawnee County - zero appeals
Lyon County - four appeals ('95 Condo project, 124 separate parcels)
Saline County - seventeen appeals

Comments:

- ◆ The process was a waste of time.
- ◆ Each party had only a "one shot deal."
- ◆ Total failure because of lack of documentation of the method used to determine value.

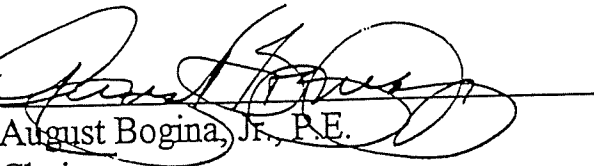
- ◆ The Arbitrator is not required to determine fair market value.
- ◆ The Arbitrator believed their task was to seek a middle ground.
- ◆ The taxpayer always had due process opportunities (their choice to choose normal appeal or arbitration).
- ◆ The county is denied due process because they have no choice if the taxpayer requests arbitration of the appeal.

I and members of the Board, as well as our staff, are committed to providing the best service possible consistent with real values, legislative intent, case law, the statutes, our Constitution, and common sense. That commitment, I believe, is real and a worthy goal for our agency.

I thank you and welcome the opportunity to appear before you at any time to discuss the Board of Tax Appeals' role in our state government.

Respectfully submitted,

BOARD OF TAX APPEALS

BY 
August Bogina, Jr., P.E.
Chairman

Attachments

Fiscal Reports for FY96 Case Filings/Case Workload Measures

Dec 31, 1995

1-4

	<u>Fiscal Year</u>									
	<u>87</u>	<u>88</u>	<u>89</u>	<u>90</u>	<u>91</u>	<u>92</u>	<u>93</u>	<u>94</u>	<u>95</u>	<u>96</u>
<u>Special Appeals</u>										
Protests	0	1,053	1,242	15,468	3,831	3,619	6,035	3,652	2,344	326
Exemptions	1,403	3,691	4,023	3,635	4,263	6,562	8,899	5,267	5,038	1,631
Grievances	<u>6,867</u>	<u>1,056</u>	<u>1,620</u>	<u>1,607</u>	<u>2,093</u>	<u>2,734</u>	<u>3,026</u>	<u>2,661</u>	<u>2,396</u>	<u>1,512</u>
Subtotal Special Appeals	8,270	5,800	6,885	20,710	10,187	12,915	17,960	11,580	9,778	3,469
<u>Other Appeals</u>										
Co Bd of EQ	74	55	361	1,769	1,058	2,309	1,524	1,870	1,780	1,918
Dir of Tax	44	29	32	54	66	69	111	131	130	64
Dir of PV	28	0	3	20	26	28	17	35	12	5
No-fund Warrants	37	27	27	48	43	23	21	36	22	9
School Dist	5	9	44	72	0	0	0	2	1	0
Ind Rev Bond Exempt	148	28	41	47	22	34	45	38	39	16
Eco-Dev Exempt	0	27	46	76	71	71	37	45	73	40
Other	0	0	4	1	0	0	6	12	18	3
Subtotal Other Appeals	336	175	558	2,087	1,286	2,534	1,761	2,169	2,075	2,055
Subtotal All Appeals	8,606	5,975	7,443	22,797	11,473	15,449	19,721	13,749	11,853	5,524
Informal Review Results	0	10	11	51,611	13,197	12,619	8,494	6,929	213	0
Total Findings	8,606	5,985	7,454	74,408	24,670	28,068	28,215	20,678	12,066	5,524
Hearings @ BOTA by Case Filing		1,342	1,045	2,286	4,945	3,441	3,134	2,878	2,154	2,172
Pre-hearing by Case Filing		0	0	0	0	0	0	2,103	2,319	902
Orders Written by Case Filing		<u>6,097</u>	<u>7,099</u>	<u>7,470</u>	<u>21,239</u>	<u>16,832</u>	<u>21,332</u>	<u>16,426</u>	<u>22,742</u>	<u>7,653</u>
Cases Closed by Case Filing		6,071	6,978	7,231	21,224	16,716	21,187	14,391	15,696	6,586
Open Cases by Case Filing		7,748	8,213	23,779	14,028	12,761	11,295	10,653	6,810	5,748
School Levy Cases/Pending Crt Dec.		0	0	0	0	0	2,801	375	24	0
School Levy Cases Closed									-3200	0
Contaminated Cases/Pending Crt Dec.				1	72	85	175	79	112	0
Contaminated Cases Closed										-319
Crt Cases Status 24/28 '87 to Present		<u>23</u>	<u>59</u>	<u>195</u>	<u>80</u>	<u>203</u>	<u>420</u>	<u>453</u>	<u>565</u>	<u>137</u>
Subtotal Crt Case/Pending Crt Cases		23	59	196	152	288	3,396	907	-2,499	-182
Accumulative Crt/Pending Crt Cases		23	82	278	430	718	4,114	5,021	2,522	2
Current Active Cases		7,725	8,131	23,501	13,598	12,043	7,181	5,632	4,288	3,635

Presentation to
the House Taxation Committee
Regarding Federal Tax Proposals

Presented by
Shirley Sicilian, Director of Research and Revenue Analysis
Kansas Department of Revenue

- I. A variety of tax reform proposals have been put forward on the federal level. Among them:
 - A. Unlimited Savings Allowance or USA Tax: Sens. Nunn (D-Ga.) and Domenici (R-N.M.)
 - B. National Retail Sales Tax: Sen. Lugar (R-Ind.)
 - C. Flat Taxes: Rep. Armey (R-Tex.), Sen. Specter (R-Pa.)
 - D. Modified Flat Rate Income Tax: Rep. Gephardt (D-Mo.)
- II. While the proposals vary considerably, they share at least two basic characteristics; which in comparison to the current structure, make them more similar than they may first appear.
 - A. The first similarity is that the proposals move toward fewer tax rates, in some cases, to a single rate, or "flat" tax. The objective is to promote simplicity and reduce compliance and administration costs at the federal level.
 - B. Second, the proposals shift the base away from income, towards consumption in an effort to increase incentives for saving and investment.
- III. In this presentation, I'd like to do four things:
 - A. first, very briefly overview the existing federal tax structure;
 - B. second, identify and explain a few of the distinguishing characteristics to look for in comparing the proposed structures to the existing system, and to each other;
 - C. third, provide a bullet outline of the key flat tax proposals; and
 - D. fourth, identify a few of the implications for states if one of the new proposals is adopted;
- IV. The Current Federal Tax Structure
 - A. The current federal tax base consists primarily of the income of individuals and corporations. In the case of individuals, the rate depends on the individual's filing status (i.e. single, head of household, married filing joint return, and married filing a separate return) and the individual's income. The marginal rates are 15 percent, 28 percent, 31 percent and, in the case of income over \$256,000, 39.6 percent. Capital gains are subject to a maximum rate of 28 percent.
 - B. The federal tax system also includes employment taxes (which are used to finance social security benefits, Medicare, and unemployment compensation), an estate and gift tax, and excise taxes on selected goods and services.

- C. Currently, there is no federal broad-based consumption tax. Of course, most states, and many state and local subdivisions, impose general sales taxes. Most state and local governments also impose property taxes.
 - D. The composition of tax receipts varies substantially across countries. Among the countries in the Organization for Economic Cooperation and Development, Canada relies most heavily on the individual income tax, followed by the United States. Japan is the most reliant on the corporate income tax. The United States and Japan generate the smallest proportion of their revenue from taxes directly on goods and services (consumption taxes or excise taxes).
- V. Primary Characteristics of the Proposed Tax Structures: Rates and Base
- A. Slope of the Rates
 1. One major objective of the proposals is to simplify the current federal income tax.
 2. In general, the simplest system would be a "flat tax", which is a system with only one marginal tax rate. In practice, even the flat tax proposals have some "zero bracket", a threshold level of income, below which no tax is owed. But, beyond this base level, some proposals would apply just one marginal rate.
 3. The Arney and Specter flat tax proposals would impose a single rate equal to 20%.¹ In the case of Arney's proposal, the rate is reduced to 17% for taxable years beginning after December 31, 1996. Both proposals include generous standard deductions.²
 4. The Gephardt plan is identified as a "modified flat tax." Under this plan, a family of four would pay 10% on income to \$60,000, and a single taxpayer would pay 10% on income to \$32,000. Otherwise, the "proposal retains current progressivity."

¹ Many features of the Arney and Specter bills are identical. Both bills are based upon a proposal by Professors Robert E. Hall and Alvin Rabushka, described in *Low Tax, Simple Tax, Flat Tax*, (New York: McGraw Hill), 1983.

² Standard deductions under the Arney and Specter bills would include the following basic standard deduction (compared to current law):

Filing Status	Arney	Specter	Current Law
Joint Return	\$24,700	\$16,500	\$6,550
Head of Household	\$16,200	\$14,000	\$5,750
Married filing sep.	\$12,350	\$9,500	\$3,275
Single	\$12,350	\$9,500	\$3,900

plus the "additional standard deduction." The "additional standard deduction" is equal to \$5,000 under Arney's bill, \$4,500 under Specter's bill, times the number of dependents of the taxpayer. Under present law, a \$2,500 exemption amount is allowed for calendar year 1995 for the taxpayer, his or her spouse, and each dependent of the taxpayer.

B. Definition of the Tax Base

1. Many of the flat tax proposals do more than simply apply one rate to the current individual income tax base, they, along with most of the other proposals, redefine the base of the tax as well. There are two main approaches: a consumption base and an income base.
2. The gross income of a taxpayer in any year is simply the sum of the taxpayer's consumption and gross saving. Thus, the difference between these two bases is in the treatment of saving. An income-based tax includes the return to saving in the tax base; a consumption-based tax does not.
3. Sen. Lugar's National Retail Sales tax is perhaps the easiest to view as a tax on consumption.
4. The USA tax proposed by Nunn and Domenici is also a consumption based tax. This bill would replace the current individual income tax with a "savings-exempt income tax," a broader-based individual income tax with an unlimited deduction for net new saving. Individuals would be taxed on income from wages, interest and dividends minus additions to savings made during the year. (This tax is progressively graduated with three brackets from 8% - 40%)
5. Certain types of Value Added Taxes (VATs) can also provide consumption based taxation.
 - a) A value-added tax generally is a tax imposed and collected on only the "value added" at every stage in the production and distribution process. The value added is the difference in the value of sales (outputs) and the value of purchases (inputs).
 - b) Although they are administered differently, a VAT and a general sales tax can accomplish identical results: the VAT is levied incrementally, to a portion of the value of the sale, at each stage of production; while the sales tax is levied once on the full value of the retail sale.
 - c) The value-added tax minimizes the problems of "cascading" sales tax, i.e. the potential for double counting intermediate goods and services, yet it does not require an identification of the final (retail) use of a good or service.³

³ Take the example of a logger, selling to a furniture maker, selling to a furniture retailer:

- d) A VAT is generally thought of as a consumption tax, not because it uses value added as a base, but because it uses cash-flow accounting principles to measure value added.
- 6. The Arney and Specter flat taxes are also a form of consumption based tax,
 - a) At the personal income level, the rate is applied to "taxable earned income", while income from savings and investment (i.e. interest, dividends and capital gains) would be exempt. Taxable business income under these two bills means income other than investment income.
 - b) In fact the business activities taxes proposed by Arney and Specter resemble a subtraction-method VAT. The difference between the bills' business activities taxes and a subtraction-method VAT is that the bills would allow businesses to deduct compensation expense, while VATs generally do not allow compensation deductions. However, under the bills, the receipt of such compensation is subject to tax at the individual level at the same flat rate applicable to businesses. The total effect from the combination of the business activities tax and the individual tax, is roughly equivalent to a VAT.

VI. Quick Outline of Key Flat Tax Proposals

A. Arney and Specter Flat Tax

1. Individual tax

- a) Applies to wages, salaries, and pensions; not dividends, interest or gains (business profit is taxed only once)
- b) Initial 20% rate
- c) Long-run rate of 17% after Dec., 1996 (Specter remains at 20%)
- d) Generous personal allowances
- e) No deductions for mortgage, charitable contributions. (Allowed under Specter)
- f) Repeal wage withholding and require a monthly payment by all wage and salary taxpayers. (Specter would not repeal)

Firm	Price	Value-Added	Tax 10% VAT	Tax 10% Sales
Logger	\$20	\$20	\$2	\$0
Furniture Maker	\$70	\$50	\$5	\$0
Retailer	\$100	\$30	\$3	\$10
TOTALS		\$100	\$10	\$10

2. Business tax
 - a) Business receipts less purchases from other businesses, and less wages, salaries, and pensions (wage income is taxed only once)
 - b) Expense new investment
 - c) Deduction for interest expense
 - d) No deduction for employee fringe benefits
 - e) Not border adjustable (imports deductible as "inputs")
 3. Replaces individual and corporate income and estate taxes
- B. Gephardt Modified Flat Tax
1. Individual tax
 - a) 10% marginal rate on \$0 - \$40,200 (Married)
 - b) Eliminates the 28% maximum on capital gain
 - c) Current progressivity of the tax code retained (total of 5 brackets with highest at 34%)
 - d) Broadens base by eliminating many deductions, credits, exclusions and adjustments. Mortgage interest deduction is allowed.
 - e) Income based. Tax exempt interest, fringe benefits (health insurance), and employer pension contributions included; state and local tax refunds excluded

VII. Implications for States

- A. The implication for the states from adoption of an alternative plan will vary depending upon the specifics of the proposal adopted.
- B. However, compared to current circumstances, some of the proposals could leave the states with fewer tax policy choices. This is because the current structure of federal and state tax systems combines consumption taxes - state sales taxes - with "ability to pay" taxes - federal, state and local income taxes. If the federal government moves towards a consumption tax, it may restrict a states option to maintain "ability to pay" income taxes in their mix.
- C. For example, Kansas personal and corporate income taxes begin with the federal determination of AGI. As that definition is dramatically changed, or even eliminated, Kansas must decide if it wishes to continue to utilize the federal determinant, or draft, administer, and enforce its own definition of income.
- D. Some commentator's suggest that replacing the federal income tax with a single retail sales tax, as under Sen. Lugar's NST, would have the most dramatic impact.
 1. It would be very difficult for states to effectively maintain and administer an income tax entirely absence a federal counterpart.

2. Yet, it may also be difficult to follow the federal direction and revert our income tax to a state sales tax which would then be in addition to the new federal tax as well as the existing state and local sales taxes.
3. On the other hand, the loss of autonomy in tax policy may be offset to some degree by the efficiency benefits to the national economy arising from a broad, commonly administered sales tax.

VIII. Notes

- A. One area of controversy for all of the proposals is the degree of revenue impact.
- B. Another, related controversy is the degree of distributional impacts.
- C. The relevance of border adjustment and transfer pricing issues is debated.
- D. There is controversy regarding the degree to which the current system creates a disincentive for savings and investment (future, as opposed to current, consumption).