Approved: 2-1-00
Date

MINUTES OF THE SENATE ASSESSMENT AND TAXATION COMMITTEE.

The meeting was called to order by Chairperson Senator Audrey Langworthy at 11:08 a.m. on January 31, 2000, in Room 519-S of the Capitol.

All members were present except:

Committee staff present: Chris Courtwright, Legislative Research Department
April Holman, Legislative Research Department
Don Hayward, Revisor of Statutes Office
Shirley Higgins, Committee Secretary

Conferees appearing before the committee: Shirley Sicilian, Kansas Department of Revenue

Others attending: See attached list.

The minutes of the meetings of January 25, 26, and 27, 2000, were approved.

Senator Langworthy began a brief review of two previously heard bills, **SB 378**, concerning refunds on sales tax paid upon food and **SB 379**, amending the homestead property refund act. She reminded the Committee that both bills were introduced by the interim Special Committee on Assessment and Taxation.

SB 378 would change the definition of income to include retirement benefits as well as dividends and interest from any source not included in the adjusted gross income. The only amendment by the Committee was technical.

Senator Hardenburger moved to recommend **SB 378** as favorable for passage as amended, seconded by Senator Steffes. The motion carried.

SB 379 would amend the homestead property tax refund act to exclude disability payments received under the federal social security act from the calculation of income. The only amendment by the Committee was to add a comma in one sentence for clarification purposes.

Senator Stephens moved to recommend **SB 379** as favorable for passage as amended, seconded by Senator Hardenburger. The motion carried.

SB 410–Taxation; providing benefits and incentives for statutory compliance by certain taxpayers

Shirley Sicilian, Kansas Department of Revenue, noted that **SB 410** was introduced at the request of the Department. She said the bill would create benefits and incentives that promote fairness, efficiency, and clarity in the tax laws. Ms. Sicilian discussed the six initiatives in the bill as follows (Attachment 1):

- Reduce interest for participants in a "Managed Sales Tax Audit Program"
  Ms. Sicilian explained that currently the Department relies heavily on voluntary compliance. Under the managed audit agreement, a taxpayer commits to performing a self-audit against an audit plan developed by the Director. Participation has been limited. **SB 410** would allow the Department to encourage participation by referencing the program in statute and allowing a 50 percent interest rate reduction on assessments identified by the eligible taxpayer and verified by the Director These taxpayers have been in compliance and are unlikely to be audited otherwise; therefore, the fiscal note on this provision of the bill is positive.

- Provide an electronic filing "coupon" for individual income taxpayers
  Ms. Sicilian noted that one of the Department's goals is to accelerate the increase in electronic filing because a significant and sustained increase in the percentage of taxpayers filing electronically will produce substantial long-term savings for the Department. The Department believes that the key to accelerating electronic filing is to get taxpayers to try it. The bill would encourage taxpayers to try electronic filing by providing them a $2.00 credit ("coupon") for doing so. Although the estimated fiscal impact for 2001 is $720,000, the savings in administrative costs would be approximately $700,000 in fiscal year 2002.

- Allow an "innocent spouse" finding at the state level
  Ms. Sicilian explained that the IRS relieves an "innocent spouse" from income tax liability and that relief automatically flows through to the state level. However, when there is only state liability, there can be no federal "innocent spouse" finding, and the state does not have any provision to grant this relief on its own. The bill would clarify the flow through of the federal funding and would allow the state to make its own "innocent spouse" finding where there is no outstanding federal liability. The fiscal note for this provision is minimal.

- Raise the threshold for filing estimated individual income tax returns
  Ms. Sicilian pointed out that the $200 threshold for determining whether individuals must file estimated individual income tax returns has been in place since 1989. The bill would move the threshold to $350. This increase will have a cash flow impact that will reduce fiscal year 2001 State General Fund revenues by $275,000. There would be some administrative cost savings since increasing the threshold should reduce the number of borderline cases wherein the tax penalty imposed is waived on appeal.

- Clarify certain provisions of the withholding tax law
  Ms. Sicilian noted that current Kansas withholding statutes do not address non-wage payments such as gambling winnings, taxable payments of Indian casino profits, and periodic pension payments. The main purpose of this amendment is to codify Kansas' adherence to the federal treatment of non-wage payments and to codify certain provisions currently found in Kansas regulations. Because these changes simply codify existing practice and rules, they have no fiscal impact.

- Allow tax penalties to be phased in at 1 percent a month, up to 24 percent
  Ms Sicilian explained, under current statute, if a taxpayer fails to file or pay by the due date, a 10 percent penalty must be assessed. Six months later, the penalty rises to 25 percent. The Secretary may waive the penalty for "reasonable causes." In the majority of cases, taxpayers request a waiver, and their requests are usually granted. The waiver process can be administratively expensive and time consuming. Under the proposed bill, penalties would be phased in at the rate of 1 percent a month up to a maximum of 24 percent. The lower starting rate and more gradual phase in will provide a reasonable penalty that can be uniformly applied. The fiscal note on this provision is minimal.

Ms. Sicilian also suggested an amendment to eliminate contractor registration fees. Current statute requires non-resident contractors to register and pay a fee of $10 for every Kansas contract with a price greater than $10,000. Ms. Sicilian noted that the fee produces very little revenue relative to the operational cost of building its collection into the Department's new system. The Department proposes continuing the registration requirement but eliminating the required fee.

The meeting was adjourned at 11:35 p.m.

The next meeting is scheduled for February 1, 2000.

SENATE ASSESSMENT AND TAXATION COMMITTEE
GUEST LIST

DATE: 1/31/00

NAME	REPRESENTING
Alex A. Kotoyantz	Ks. Academy of Sciences
GEORGE PETERSEN	Ks TAXPAYERS NETWORK
Mary Becker	Kansans Respond
Dave Holthaus	Western Resources
Tom Bruno	MGA
Marlee Bertholf	KCCI
Ann Durkes	DOB
Anne Spiess	Peterson Public Affairs Group

STATE OF KANSAS
Bill Graves, Governor

DEPARTMENT OF REVENUE
Karla Pierce, Secretary

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Office of Policy & Research

TESTIMONY

To:	Senator Audrey Langworthy, Chair, Senate Assessment and Taxation Committee
From:	Shirley K. Sicilian
Re:	**SB 410 – Taxpayer Benefits and Incentives**
Date:	January 31, 2000

Senator Langworthy and members of the Committee, thank you very much for the opportunity to testify today regarding senate bill 410. Senate bill 410 is a department of revenue bill. This bill would create taxpayer benefits and incentives that promote fairness, efficiency and clarity in the tax laws. The bill has six initiatives.

<u>The 6 initiatives contained in the bill.</u>

1. **Reduce Interest for Participants in a "Managed Sales Tax Audit Program" (§1 - §5).** The department generally employs sufficient sales tax audit staff to review approximately 2% to 3% of all Kansas sales tax filers' annually. This means that for any given tax year, less than 10% of sales tax payers will be audited within the 3 year statute of limitations. Clearly, our current system relies heavily on voluntary compliance, which the department fosters through a myriad of educational seminars and publications. The department also leverages both its education and its audit efforts to provide a third, middle approach to compliance. Under this middle approach, the department enters "managed-audit" agreements with certain eligible taxpayers that might not otherwise be audited for quite some time. Under the managed-audit agreement, a taxpayer commits to performing a self-audit against an audit plan developed by the director. The audit plan includes detailed educational materials and specifies: (1) the period to be audited, (2) the general scope of the audit, (3) records to be examined and the types of sampling techniques to be used, (4) specific procedures for determining liability, (5) deadline for completion of the audit, and (6) deadline for payment of the tax, penalty and interest assessed. Participation in our program has been limited. SB 410 would allow us to encourage participation by referencing the program in statute and allowing a 50% interest rate reduction on assessments identified by the eligible taxpayer and verified by the director. Because these are taxpayers that are unlikely to be audited otherwise, the fiscal note for this proposal is **positive**.

2. **Provide an electronic filing "coupon" for individual income taxpayers (§6).** One of the department's strategic goals is to accelerate the increase in electronic filing. A significant and sustained increase in the percentage of taxpayers filing electronically will produce substantial long-term cost savings for the department. We find those taxpayers that do try e-filing like it and intend to continue. Therefore, we believe the key to accelerating electronic filing is simply to get

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taxpayers to try it. This bill would encourage individual income taxpayers to try electronic filing by providing them a $2 credit, or "coupon," for doing so. The credit would be a short-term promotion, in place for tax years 2000 and 2001 only. We estimate the fiscal impact for 2001 would be **$720,000**. The administrative cost savings could be significant. Administrative cost savings for increased electronic filing of individual income tax returns would be realized through 1) elimination of the need to replace the departments intelligent character recognition software in 2002 , and 2) a reduction in the number of temporary employees needed during the 15 week tax season which usually begins the first week of February and ends about the third week of May. This amounts to a savings of approximately $700,000 (software, hardware, and temporaries) in FY 2002 and $250,000 (software maintenance and temporaries) in FY 2003 and thereafter. President Clinton has just announced a similar proposal ($10 credit) at the federal level.

3. **Allow an "Innocent Spouse" finding at the state level (§7).** The IRS Restructuring and Reform Act of 1998 requires the IRS to relieve an "innocent spouse" from income tax liability. This federal relief automatically flows through to the state level. But where there is no outstanding federal liability, only state liability, there can be no federal "innocent spouse" finding. And, the state does not have any provision to grant this relief on its own. This means that an "innocent spouse" who has not paid off the federal liability will be relieved from state liability. But if the federal liability was paid, there can be no relief at the state level. This bill would clarify the flow through of the federal finding, and would allow the state to make its own "innocent spouse" finding where there is no outstanding federal liability. We believe these changes would promote fairness and strengthen Kansas' conformity with the federal law. The fiscal note for this proposal is **minimal**.

4. **Raise the threshold for filing estimated individual income tax returns (§8).** There is a two-prong test for determining whether an individual must file estimated individual income tax returns. One of those two prongs is whether the individual can reasonably expect to owe $200 above withholding and credits. The $200 threshold has been in place since at least 1989. This bill would move that threshold to $350. Increasing the estimated filing threshold from $200 to $350 will have a "cash flow" impact that will reduce fiscal year 2001 state general fund revenues by **$275,000**. There would be some administrative cost savings since increasing the threshold should reduce the number of border-line cases where estimated tax penalty is imposed, and subsequently waived on appeal.

previous issue

5. **Clarify certain provisions of the withholding tax law (§9 - §18).** The current Kansas withholding statutes do not address non-wage payments, such as gambling winnings, taxable payments of Indian casino profits, or periodic pension payments. The state currently follows federal treatment, which subjects these payments to withholding requirements. The main purpose of these amendments is to codify Kansas' adherence to the federal treatment of non-wage payments. A second purpose of these amendments is to codify certain provisions currently found in our regulations. New Sections 12 and 13 are restatements of existing regulations that we feel would be more securely supportable if they were in statute. New Section 12 restates K.A.R. 92-11-15 captioned "Employer's liability for withheld taxes." The language is modified only to include "payors." New §13 restates K.A.R. 92-11-16 captioned "Employer's failure to withhold." Again, the language is modified only to include "payors."

New Section 14 deals with the rate of withholding. Subsections (a) and (b) are intended to restate the provisions deleted from 79-3297a. 79-3297a also has provisions regarding codification of withholding tables in regulations. The department does issue a publication containing the withholding tables at least annually. Two years ago, the tables needed to be published twice in one year. The frequency of withholding changes, and the time lag inherent in publication by regulation, makes publication by regulation impractical.

Because these changes simply codify existing practice and rules, they have **no fiscal impact**.

6. Allow tax penalties to be phased in at 1% a month, up to 24% (§19 - §22). Under current statute, if a taxpayer fails to file or pay by the due date, a 10% penalty must be assessed in addition to interest, even when the payment is only a day or two late. Six months later, the penalty rises to 25%. The secretary may waive penalty for "reasonable causes," and in the majority of cases, taxpayers do request a waiver. Because a 10% penalty in today's economic environment often seems excessive under the circumstances, their requests are usually granted. This putting on and taking off of penalty works in theory but can be administratively expensive and time consuming in practice - a poor use of government resources. The system also has the potential to create inequities between those who simply pay the penalty without question and those who know to ask for waiver. Under the proposed bill, penalties would be phased-in at the rate of 1% a month, up to a maximum of 24%. The lower starting rate and the more gradual phase-in will provide a penalty that is reasonable under most circumstances and can be uniformly applied. KDOR's old income tax processing systems would not have been able to calculate interest as required by this bill. However, our new system is able to. The fiscal note for this provision is **minimal**.

<u>Proposed amendment to eliminate contractor registration fees</u>

Since the time we introduced this bill, an operational issue came to our attention that we respectfully request be relieved through legislation. K.S.A. 79-1009 currently requires non-resident contractors to register and pay a fee of $10 for every Kansas contract with a price greater than $10,000. The fee produces very little revenue relative to the operational cost of building its collection into our new system. In fiscal year 1998, only $180.00 was remitted. We propose continuing the registration requirement, but eliminating the required fee:

> To the end that the state of Kansas and the political subdivisions thereof may receive all taxes due in every instance, including contributions due under the employment security law, contractors, who are nonresidents of this state, desiring to engage in, prosecute, follow or carry on the business of contracting as defined in this act shall register with the secretary of revenue or the secretary's designee for each contract where the total contract price or compensation to be received amounts to more than $10,000, except that a foreign corporation authorized to do business in this state shall not be required to register under the provisions of this act. ~~The secretary or the secretary's designee shall charge a fee for such registration in the amount of $10 for each such contract. All such fees received by the secretary or the secretary's designee shall be deposited on Monday of each week with the state treasurer. The state treasurer shall thereupon credit the amount of such fees to the state general fund.~~

<u>Summary of Fiscal Impact</u>

Only two of these initiatives, the electronic filing credit and the estimated threshold increase, have non-minimal fiscal impacts, for a total fiscal impact of $995,000. As mentioned above, that fiscal note would be offset by reduced administrative costs in the future of $700,000 in 2002, and $250,000 in 2003 and thereafter.