

MINUTES OF THE HOUSE TAXATION COMMITTEE

The meeting was called to order by Vice Chairman Richard Carlson at 9:00 A.M. on January 24, 2007 in Room 519-S of the Capitol.

All members were present except:
Representative Paul Davis
Representative Virgil Peck
Representative Kenny Wilk

Committee staff present:
Chris Courtwright, Legislative Research Department
Martha Dorsey, Legislative Research Department
Gordon Self, Office of Revisor of Statutes
Richard Cram, Department of Revenue
Rose Marie Glatt, Committee Secretary

Conferees appearing before the committee:
Stuart Little, Little Government Relations

Others attending:
See attached list.

The Vice Chairman called for bill introductions.

Stuart Little, appeared on behalf of the Johnson County Government, to requested a bill introduction regarding taxable convertible land in Johnson County. Representative Owens moved the introduction. Representative Worley seconded. The motion carried.

The Vice Chair called for the continuation of Interim Reports

2006 Interim Reports

“Truth Taxation” Local Budget Law

Chris Courtwright, Legislative Research Department, briefed the committee on the background of the Property Tax Lid, explaining its rationale and formula. He explained “Truth in Taxation Lid”, a new mechanism put in effect in 1999 whose provisions have not been modified since enacted.

He gave an overview of Committee activities, and reviewed their conclusions and recommendations. The Committee: 1) Finds that the decision made in 1999 to abolish the *Property Tax Lid* in favor of the *Truth in Taxation Lid* represented an appropriate choice of no longer seeking to micro-manage local units of governments; 2) Further notes that no report surfaced of any local unit having violated the *Truth in Taxation* provisions; 3) Encourages DOR to establish a comprehensive *Truth in Taxation* website with a variety of tax information available to taxpayers (Attachment 1).

State and Local Tax Policy

Chris Courtwright, Legislative Research Department, gave the background of the 2005 Special Committee on Assessment and Taxation, including their recommendations related to: State and local tax policy linkage; Long-run growth and the SGF; and Business taxes. He reviewed Committee activities and gave a brief overview of presentations by Dr. John Wong; Dr. Glenn Fisher, and Dr. Bart Hildreth. He summarized Secretary Wagnon’s recommendations, made at the October meeting, followed by suggestions expressed by conferees (Attachment 2).

He reviewed the Committee’s Conclusions and Recommendations: 1) Withholding tax, no longer be allowed to be diverted away from the SGF; 2) Specific questions relating to justification of any new exemptions must be answered by all parties before exemptions are given; 3) Leadership should develop rules that would prohibit advancement of any exemption until specific questions have been

CONTINUATION SHEET

MINUTES OF THE House Taxation Committee at 9:00 A.M. on January 24, 2006 in Room 519-S of the Capitol.

answered; 4) Encourage the 2007 legislature to consider multiple changes pertaining to corporation Income and Franchise taxes; 5) Recommended that PVD conduct a study of townships regarding property tax issues; 6) Repeal any statutory barriers and impediments to local government restructuring; 7) Develop tools and models to evaluate the possibility of multi-jurisdictional service-delivery systems by quantifying potential property tax savings and budget reductions associated with such entities.

Tax Incidence and Tax Base Erosion

Chris Courtwright, Legislative Research Department, explained this subject is closely related to the last topic, and called attention to page 2-31 in the Interim Report booklet (Attachment 3). He briefly described the studies of Dr. John Wong and Dr. Glenn Fisher on Tax Incidence and Tax Base Erosion. He reviewed Secretary Wagnon's criteria that she believed should be considered before any tax exemption be granted. He reviewed the Committee's Conclusions and Recommendations; 1) Specific questions relating to justification of any new exemptions must be answered by all parties before it is given; 2) Leadership should develop a set of rules that would prohibit advancement of any exemption until specific questions have been answered; 3) Standing Tax committees should consider tax incidence and progressivity-regressivity issues with respect to all major state and local tax policy changes.

Staff was requested to provide the dollar amounts of tax exemptions for profit, non-profit and not-for-profit groups and the lists of tax exemptions used by Dr. Wong and the Department of Revenue.

Richard Cram, Department of Revenue, returned to the podium to brief the Committee on the topic of the Individual Income Tax Structure. He distributed and explained a matrix summary on *State Sales Tax Exemptions* which addressed several of the Committee's previous questions (Attachment 4).

He explained the various areas where Kansas does and does not conform to the federal guidelines and explained Kansas deductions, tax brackets and credits (Attachment 5). He called attention to Schedule S in the Income Tax Booklet (copy on file in the Department of Revenue). He explained a memo from the Tax Expenditure Report, previously distributed, from KDOR's annual report regarding: 1) Individual Income Tax amount to the SGF after refunds for years 2001- 2006; 2) Income Tax by Adjusted Gross Income Bracket for 2004; 3) Individual Income Tax by County for 2004; and 4) Top twelve Kansas counties with highest average tax liability per return for 2004 (Attachment 6).

There was a request of staff to provide information on how Kansas income tax rates compare to those in surrounding states and how Kansas child credits compare to Federal credits.

The meeting was adjourned at 10:20 a.m. The next meeting is January 25, 2007.

Special Committee on Assessment and Taxation

“TRUTH IN TAXATION” LOCAL BUDGET LAW

CONCLUSIONS AND RECOMMENDATIONS

The Committee finds that the decision made in 1999 to abolish the tax lid in favor of the truth in taxation lid represented an appropriate choice of no longer seeking to micro-manage local units of government.

The Committee further notes that no report surfaced of any local unit having violated the truth in taxation provisions.

The Committee encourages the Department of Revenue to establish a comprehensive “truth in taxation” website that could make a variety of federal, state, and local tax information available to taxpayers.

Proposed Legislation: None.

BACKGROUND

Property Tax Lid: 1989-1999

The Legislature in 1985 enacted an aggregate property tax limitation (tax lid) that was effective beginning with tax year 1989 so as to coincide with the implementation of property tax reappraisal and classification (see KSA 79-5021 et seq). Because of the significant expansion in statewide assessed valuation anticipated as a result of reappraisal, the Legislature wanted a limitation on overall property taxes imposed by taxing subdivisions (many of whom otherwise could have received a windfall if mill levy rates were not rolled back). Numerous individual statutory fund levy limits, therefore, were suspended and replaced with the aggregate tax lid mechanism (see KSA 79-5022), which was applied to total property tax dollars levied in lieu of the mill levy rates.

The tax lid provided generally prohibited local units from levying property taxes in greater amounts than a “base” year (choice of either 1988 or 1989), subject to a number of exemptions and exceptions relative to

property taxes levied for special purposes. Property taxes levied as a result of new improvements to real estate and added personal property were exempt from the computation, as were taxes levied as a result of added territory or a service that had been transferred from another governmental unit. Other exemptions from the formula included property taxes levied for public building commissions; judgments, settlements and expenses for protection against liability; employer contributions for workers compensation, unemployment insurance, health care costs, employee benefit plans, and employee retirement and pension programs; district court operations; payment of out-district tuition to community colleges and Washburn; certain juvenile delinquency and crime prevention programs; rebates granted to property owners in conjunction with neighborhood revitalization programs; expenses necessary to interface with the state criminal justice information system; certain mental health services; and revenues to replace reductions in motor vehicle taxes.

Local units seeking to levy more in taxes beyond amounts not authorized by the aforementioned exemptions and exceptions

had authority pursuant to KSA 79-5036 to exempt themselves from all or a portion of the remaining restrictions of the tax lid by approving charter ordinances or resolutions. Such ordinances or resolutions were then subject to various publication and protest petition requirements, under which a certain percentage of the electorate could force an election on the question of the proposed tax lid exemptions (and efforts to increase property taxes beyond a certain point).

The tax lid was extended a number of times throughout the 1990s, with the last extension coming in 1997 (see 1997 SB 7). Under that legislation, the tax lid was extended for an additional two years -- until July 1, 1999—at which time it was allowed to expire (see KSA 79-5038). Local units of government traditionally opposed re-extension of the tax lid, generally arguing that local officials with authority to levy property taxes were elected just like members of the Legislature; that local units of government had a better idea of the demand for local services from the public and did not need to be micro-managed by statewide legislation; and that the tax lid appeared somewhat hypocritical in that its provisions did not apply to the state mill levies for building funds and school district general funds.

Truth in Taxation Lid: 1999-Present

Cognizant of the imminent expiration of the aggregate tax lid, the 1999 Legislature sought to replace it with a different mechanism known as “truth in taxation.” The legislation was crafted amid ongoing concerns over confusion regarding the extent to which local units may or may not have been increasing property taxes. The fact that mill levy rates in and of themselves did not necessarily represent an accurate measure for annual changes in property taxes (the other big variable being changes in assessed valuation) caused the legislation to be drafted with an emphasis on requiring local units to acknowledge to the press and the public when taxes were being increased.

The provisions of the truth in taxation lid, enacted in SB 45, provide that taxing subdivisions (defined more narrowly than the 1989 tax lid to exclude unified school districts and community colleges) are prohibited, absent adoption of a resolution or ordinance so acknowledging, from approving appropriations or budgets funded from property tax increases, except with regard to increases attributable to new improvements to real estate; certain added personal property valuation; property located within added jurisdictional territory; property which has changed in use; and for payment of principal and interest upon bonded indebtedness, temporary notes, and no-fund warrants (see KSA 79-2925b).

The acknowledgment resolutions and ordinances are not subject to protest petition but instead represent an official record for the benefit of the press and the public of certain property tax increases approved by local governing bodies, notwithstanding what may be happening with mill levies.

The legislation also finally repealed the many of hundreds of different statutory fund levy limits. (Absent this provision, the individual fund levy limits which had been suspended since 1989 would have been reactivated once the aggregate lid sunset on July 1, 1999.)

The truth in taxation provisions have not been modified since they were enacted in 1999.

2006 Interim Study

Because of ongoing concerns over increased property taxes, interim study requests were received from Rep. Wilk, Senator Allen, and Senator Brownlee to review the truth in taxation provisions and determine whether they were functioning adequately as a replacement mechanism for the old tax lid law.

The Legislative Coordinating Council subsequently approved the request and

charged the Special Committee to study the current "truth in taxation" property tax law that local governments have operated under since the late 1990's. The Committee is asked further to determine if local governments are complying with the "truth in taxation" provisions and if the provisions should be modified; or whether portions of the previous local government property tax lid law should be revived.

COMMITTEE ACTIVITIES

At the October meeting, staff briefed the Committee on the history of the property tax lid and the truth in taxation lid provisions.

No conferees appeared to advocate any changes in the current truth in taxation provisions or a restoration of the property tax lid. Representatives of the League of Kansas Municipalities and the Kansas Association of Counties appeared in opposition to restoration of the property tax lid. Both conferees said that the current truth in taxation provisions appeared to be working well.

During discussion, a number of Committee members noted that the public might be more aware of the acknowledgment resolutions passed by local governing bodies if they were posted on the Internet instead of being published in official newspapers. The Chair said that the Division of Property Valuation might be a logical agency to maintain a website that granted public access to information about local budgets and property tax increase resolutions.

The Committee also discussed asking Secretary Wagon to explore the feasibility of establishing a comprehensive "truth in taxation" website that could make a variety of federal, state, and local tax information available to taxpayers.

At the November meeting, the Committee reviewed its work at the previous two meetings and made final policy decisions.

CONCLUSIONS AND RECOMMENDATIONS

The Committee finds that the decision made in 1999 to abolish the tax lid in favor of the truth in taxation lid represented an appropriate choice of no longer seeking to micro-manage local units of government from the Statehouse.

The Committee further notes that no report surfaced of any local unit having violated the truth in taxation provisions over the past seven years.

The Committee makes no recommendation, at this time, regarding the issue of whether, as an alternative to, or in addition to, publication in official newspapers, local acknowledgment resolutions and ordinances should be published on the Internet.

Finally, the Committee encourages the Department of Revenue to establish a comprehensive "truth in taxation" website that could make a variety of federal, state, and local tax information available to taxpayers.

Special Committee on Assessment and Taxation

STATE AND LOCAL TAX POLICY

CONCLUSIONS AND RECOMMENDATIONS

The Committee expresses its concern about the recent trend of legislation that would earmark future sales, income, and property tax streams for funds other than the State General Fund (SGF). The Committee recommends that the withholding tax in particular no longer be allowed to be diverted away from the SGF, except as a last resort relative to retention of an existing business. The Committee further expresses its concern about the erosion of all major tax bases, especially the sales tax base. The Committee strongly recommends that certain specific questions relating to justification of any new exemptions be answered by all parties seeking sales tax exemption legislation. The Committee also strongly recommends that the leadership of the standing tax committees develop rules that would prohibit advancement of any sales tax exemption legislation until these questions have been answered satisfactorily by proponents.

The Committee notes that the top corporation income tax bracket may represent an economic development disincentive and encourages the 2007 Kansas Legislature to consider reducing that rate as part of a broader restructuring of the corporation income tax. That restructuring also should include simplification of the "high performance" income tax credit program be simplified; and the creation of broader availability for investment income tax credits in general. The Committee recommends the repeal of seldom-used income tax credits.

The Committee further recommends a corporation franchise tax exemption for certain assets of subsidiary corporations.

The Committee finds that one of the biggest future challenges involves local governmental service delivery systems and public angst over the property taxes associated therewith.

The Committee asks the Property Valuation Division to conduct a study of townships and report back to the tax and local government committees with respect to how many townships are actively levying property taxes and the range of activities being funded.

The Committee also recommends that the Legislature act as a facilitator to the discussion of local service delivery restructuring by enacting legislation that would repeal any and all statutory barriers to restructuring. The Secretary of Revenue should compile an exhaustive list of all such barriers and submit it to the tax and local government committees during the first week of the 2007 session.

The Committee further recommends that a tool be developed to evaluate the possibility of multi-jurisdictional service-delivery systems by quantifying potential property tax savings associated with such entities. This tool, which would be developed under the auspices of the KACIR, would be made available free-of-charge to local units of government wishing to explore realignment of certain services, including infrastructure maintenance, health, vehicle registration, reappraisal, elections, and deed registration. Access to such information would allow local units of government and their taxpayers to make well-informed decisions about how to proceed.

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ATTACHMENT 2

A second model should also be developed by KACIR that would help estimate the amount of property tax relief that could be provided if the funding of certain public safety functions were to be assumed by the state. One proposal would empower citizens within each of the 31 judicial districts to abolish county attorneys and replace that system with state-funded district attorneys. Data should continue to be compiled prior to the start of the session regarding county attorney budgets and mill levy equivalencies, and the tax and judiciary committees should jointly review the data. Legislation should subsequently be introduced that would allow citizens within the judicial districts to hold elections that would change their prosecutorial model. The model also should continue to be adapted to help quantify property tax relief associated with having additional state funding of other public safety functions, including corrections.

Proposed Legislation: None.

BACKGROUND

The 2005 Special Committee on Assessment and Taxation, as part of a broad topic entitled, "Analysis of State and Local Tax Policy," received a report from Secretary Wagoner on a number of studies that had been commissioned by the Department of Revenue and the Kansas Advisory Commission on Intergovernmental Relations (KACIR), including studies of sales and property tax base erosion; tax incidence; and the rapid expansion of state and local governmental debt. That Committee anticipated "the importance of the need to give these reports in-depth review and therefore requests that the Legislative Coordinating Council (LCC) again approve a Special Committee on Assessment and Taxation to study the same state and local tax policy topic during the summer and fall of 2006."

The LCC subsequently agreed to renew the broad-based state and local tax study, charging the 2006 Special Committee with studying and projecting the future of Kansas tax policy for the next 10 to 20 years. As a follow-up to a 2005 interim study, the 2006 Committee was further asked to review the current state and local tax structure, focusing on the shifts in reliance on sales, property, and income taxes since 1990. The Committee was asked to review which tax structure components would be most equitable to the taxpayers of Kansas; and

would improve Kansas' competitiveness with other states.

Other 2005 Recommendations

In addition to recommending that a new study be empaneled to receive the studies being prepared by the Department of Revenue and KACIR, the 2005 Special Committee made a number of other findings and recommendations in three areas – state and local tax policy linkage; long-run growth and the SGF; and business tax recommendations.

State and Local Tax Policy Linkage

- The Committee recommended that the context within which the Legislature views state tax policy and potential changes should always include consideration of the implications on local tax policy, especially property taxes.
- The Committee strongly encouraged the 2006 Legislature to provide property tax relief by authorizing the restoration of sales tax demand transfers to local units of government. If it was determined that the demand transfer program needed to be restructured, the Committee recommended that special emphasis be placed on providing additional funds for local units in rural areas.

- The Committee also asked that the standing tax committees monitor the implications of the growing regional differences in local sales tax rates.

Long-Run Growth and the SGF

- The Committee made a finding that the overall elasticity of tax receipts, especially SGF tax receipts, appeared to be declining to the point that the ability of the state to fund ongoing and necessary expenditures without periodic tax increases has been imperilled. The Committee expressed its concern about the recent trend of legislation to earmark future sales, income, and property tax revenue streams from specific industries or businesses, including legislation associated with the development of sales-tax-and revenue bonds and the neighborhood revitalization program.
- The Committee, therefore, recommended that a more rigorous fiscal review be applied to future legislation seeking to earmark revenues historically placed in the SGF and asked that all such bills be referred to the standing tax committees.
- Because of the proliferation of legislation associated with the diversion of revenues, the Committee asked that the standing tax and appropriations committees' work with staff at the Division of Budget and the Legislative Research Department to develop a new monthly receipts report that disaggregates taxes and other receipts relative to the amount placed in the SGF compared to the amount placed in all other funds.
- Also because of the concern over long-run state revenue growth issues, the Committee further recommended that the 2006 Legislature memorialize Congress to minimize all federal preemption of state taxing authority.

Business Tax Recommendations

- The Committee expressed its concern about the volatility of corporation income tax receipts over the last decade. The Committee therefore recommended that the Department of Revenue report to the standing tax committees on policy options regarding modernization and structural changes to the tax that would help assure that it continues to be a viable revenue source well into the future.
- The Committee recommended that the Legislature attempt to provide a property tax exemption for commercial and industrial machinery and equipment and notes that options under consideration would include a full statutory exemption; expansion of the existing income tax credit to 100 percent; or a constitutional amendment authorizing the Legislature to phase in a full exemption over a period of years.

COMMITTEE ACTIVITIES

At the September meeting, the Committee received the KACIR studies, which were conducted by the Kansas Public Finance Center, a part of the Hugo Wall School of Urban and Public Affairs at Wichita State University.

Dr. John Wong presented a study on tax incidence. Among the principal findings was a conclusion that the Kansas individual income tax is modestly progressive; and that such progressivity does not completely offset the regressivity of the other major tax sources.

Dr. Wong then presented a study on sales tax base erosion, noting that economic and technological changes in recent years had joined legislatively enacted exemptions as the major sources of erosion. He said that one study had estimated that extending the tax to all "readily taxable" services could

increase revenue by over \$500 million. He added that the main arguments for inclusion of additional services in the sales tax base included:

- the sales tax should be as broadly applicable to consumer expenditures as possible;
- taxation of services would reduce the regressivity of the sales tax;
- revenues would be more responsive to rising levels of personal income; and
- administration of the tax would be simplified if the tax were extended to those services entered in conjunction with the sales of tangible personal property.

Dr. Glenn Fisher presented a study on property tax base erosion, stating that the Kansas property tax is evolving largely into a real estate tax, due at least in part to the increased propensity of the Legislature to exempt personal property. He said that given the importance of the tax for local government revenue, any major changes in the property tax system would likely be controversial and potentially painful.

Dr. Bart Hildreth presented a study on the extent to which Kansas local government debt has been increasing over the last 15 years. He said that policy choices for those concerned about the mounting local debt burden included enacting tighter limits; promoting debt coordination; and enhancing transparency to enable taxpayer "comparison" shopping.

The Chair subsequently offered an invitation to all communities across Kansas to attend the October meeting and outline their service deliveries and revenue needs in their respective regions. Communities were invited to determine how an ideal local funding package might look and to bring any and all innovative approaches forward to the Committee.

At the October meeting, Secretary Wagon delivered her perspective on the past, present, and future of Kansas state and local tax policy. She said that if the Legislature continued to allow erosion of the major tax bases, there would be higher tax rates; less equity among various groups of taxpayers; less competitiveness and more taxpayer discontent; and more special interest groups' requesting exemptions – creating a vicious cycle.

She said that the KACIR studies had indicated that Kansas state and local tax policy faces a number of serious challenges in addition to tax base erosion, including over-reliance on the property tax; declining elasticity of major tax sources; and increasing demands on state and local governmental services.

Secretary Wagon said that tax base erosion had been occurring because of the enactment of a number of exemptions and tax credits; and because of economic shifts in consumption and business practices, many relating to new technologies. She also said that the authorization of sales tax and revenue (STAR) bonds and the propensity of the Legislature to earmark future revenue streams threatened the elasticity of tax receipts relative to the State General Fund (SGF). She said that once a special practice or tax treatment had been established, it was often difficult for the Legislature to backtrack and stop that process. Faced with a similar situation more than three decades ago, the "Hodge Committee" in the early 1970s formed a special commission to review tax policies and make decisions on which special exemptions, exceptions, and credits should be restructured or totally eliminated.

The Secretary said that she hoped the Committee would strongly recommend that the Legislature, in the future, protect the withholding tax and not allow any other circumstances wherein major tax sources could be diverted from the SGF. The Secretary subsequently outlined a variety of

policy options for the Committee to consider, including modernizing the corporation income tax structure by adjusting the rate structure and the apportionment formula; simplifying various business-related tax credits and repealing those which are seldom used; developing criteria for evaluating future sales tax exemption requests; eliminating the franchise tax imposed on the assets of certain subsidiary corporations; and continuing the discussion about restructuring local government finance.

Conferees representing AARP and Kansas Action for Children said that Kansas should consider a number of equity issues, including the ability to pay, when looking at major tax structure issues.

The Executive Director of the League of Kansas Municipalities said that cities could reduce reliance on property taxes if they were granted additional authority to levy local income, earnings, motor fuel, and excise taxes. He also said that the Legislature could remove impediments that discourage local units from combining for the purpose of streamlining the delivery of local governmental services.

A conferee representing the Kansas Association of Counties agreed, stating that all levels of government needed to nurture a culture of cross-jurisdictional collaboration.

A representative of the Unified Government of Wyandotte County and Kansas City, Kansas, said that the entity strongly supported a local option earnings tax which could be used to further reduce property taxes.

A conferee representing the Kansas Chamber of Commerce and Industry stated that the business machinery and equipment property tax exemption was extremely helpful to many Kansas businesses; and that some form of corporation franchise tax relief would continue to help those businesses stimulate the economy.

Following a discussion of local revenue needs, the Committee began an extensive discussion of local and regional service delivery structures. The Chair stated that the number of local units of government in Kansas was the highest in the nation in per capita terms and wondered aloud whether the more than 4,000 taxing entities in the state represented the most efficient structure for delivering services. Representative Jerry Henry suggested that one of the universities or the KACIR attempt to build a model for analyzing a multi-county service delivery system with an emphasis on efficiency and not on politics. The Chair said that he would try to have Secretary Wagon, prior to the November meeting, coordinate discussions about that idea with local units of government and other stakeholders. Secretary Wagon said that she would bring the topic up for discussion on November 1 at the KACIR summit in Salina. Senator Derek Schmidt and Senator Greta Goodwin also volunteered to establish a working group that would explore the possibility of relieving local property taxpayers of the burden of supporting most public safety functions by moving most funding for such functions to the state level.

At the November meeting, the Committee reviewed its work at the previous two meetings and made final policy decisions.

CONCLUSIONS AND RECOMMENDATIONS

Long-Run Growth and SGF Receipts

The Committee again expresses its concern (just as it did in 2005) about the recent trend of legislation that would earmark future sales, income, and property tax streams for funds other than the SGF.

The Committee recommends that the withholding tax, in particular, no longer be allowed to be diverted away from the SGF, except as a last resort relative to retention of an existing business. The Committee

encourages the Legislature to first attempt to utilize any and all other tools at its disposal in business retention or business attraction efforts.

The Committee further expresses its concern about the erosion of all major tax bases, especially the sales tax base. The Committee strongly recommends that certain specific questions relating to justification of any new exemptions be answered by all parties seeking sales tax exemption legislation (see Tax Incidence and Tax Base Erosion topic for more details).

The Committee also strongly recommends that the leadership of the standing tax committees develop rules that would prohibit advancement of any sales tax exemption legislation until these questions have been answered satisfactorily by proponents.

Business Tax Recommendations

The Committee notes that the top corporation income tax bracket of 7.35 percent may well represent an economic development disincentive and, therefore, encourages the 2007 Kansas Legislature to consider reducing that rate as part of a broader restructuring of the corporation income tax. As part of that restructuring, the Committee also recommends that the "high performance" income tax credit program be simplified; and that the availability of investment income tax credits in general be broadened. The Committee recommends the repeal of seldom-used income tax credits.

The Committee further recommends a corporation franchise tax exemption for certain assets of subsidiary corporations which have been subject to taxation previously as assets of parent corporations.

Local Governmental Service Delivery and Property Taxes

The Committee finds that one of the biggest challenges facing policymakers over

the next decade involves local and regional governmental service delivery systems and public angst over the property taxes associated with those services and systems.

The Committee notes that townships by far appear to represent the largest number of taxing subdivisions in the state. The Committee asks the Property Valuation Division to conduct a study of townships and report back to the tax and local government committees with respect to how many townships are actively levying property taxes and how many are not; and what are the range of activities being funded by the townships.

The Committee also recommends that the debate regarding potential restructuring of local service delivery systems be driven by local needs and local issues and not by state mandates. The Legislature may best act as a facilitator to this discussion by enacting legislation that would repeal any and all statutory barriers and impediments to local governmental service restructuring. The Secretary of Revenue, in conjunction with the League of Kansas Municipalities and Kansas Association of Counties, should compile an exhaustive list of all such statutory impediments and submit it to the tax and local government committees during the first week of the 2007 Legislative Session.

The Committee further recommends that a tool be developed to evaluate the possibility of multi-jurisdictional service-delivery systems by quantifying potential property tax savings and budget reductions associated with such entities. This tool, which would be developed under the auspices of the KACIR by the Hugo Wall School of Urban and Public Affairs at Wichita State University in conjunction with input from the Kansas Association of Counties and League of Kansas Municipalities, would be made available free-of-charge to local units of government wishing to explore realignment of certain local services.

As part of the development of the aforementioned tool, the KACIR should seek the capacity to compare and contrast potential changes in Kansas with other successful examples of local service realignments from around the nation.

Local services and functions that potentially could be reviewed would include infrastructure maintenance, health, vehicle registration, reappraisal, elections, and deed registration. Access to such information would allow local units of government and their taxpayers to make their own well-informed decisions about how to proceed with the discussion.

A second model also should be developed by KACIR and the Hugo Wall School of Urban and Public Affairs that would help estimate the amount of property tax relief that could be provided if the

funding of certain public safety functions were to be assumed by the state. One proposal discussed during the interim would empower citizens within each of the 31 judicial districts to abolish county attorneys and replace that system with state-funded district attorneys. Data should continue to be compiled prior to the start of the 2007 session regarding county attorney budgets and mill levy equivalencies, and the tax and judiciary committees should jointly review the data. Legislation should subsequently be introduced that would allow citizens within the judicial districts to hold elections that would change their prosecutorial model in this manner. The model also should continue to be adapted to help quantify the potential property tax relief associated with having additional state funding of other public safety functions, including corrections.

Special Committee on Assessment and Taxation

TAX INCIDENCE AND TAX BASE EROSION

CONCLUSIONS AND RECOMMENDATIONS

The Committee expresses its concern about the erosion of all major tax bases, especially the sales tax base. The Committee strongly recommends that certain specific questions relating to justification of any new exemptions be answered by all parties seeking sales tax exemption legislation.

The Committee further strongly recommends that the leadership of the standing tax committees develop rules that would prohibit advancement of any sales tax exemption legislation until these questions have been answered satisfactorily by proponents.

Finally, the Committee recommends that the standing committees consider tax incidence and progressivity-regressivity issues with respect to all major state and local tax policy changes.

Proposed Legislation: None.

BACKGROUND

The 2005 Special Committee on Assessment and Taxation, as part of a broad topic entitled, "Analysis of State and Local Tax Policy," received a report from Secretary Wagnon on a number of studies that had been commissioned by the Department of Revenue and the Kansas Advisory Commission on Intergovernmental Relations (KACIR), including studies of sales and property tax base erosion; and on tax incidence. That Committee anticipated "the importance of the need to give these reports in-depth review" and requested that the reports be submitted and reviewed by another Special Committee established by the Legislative Coordinating Council (LCC) during the summer and fall of 2006.

The LCC subsequently agreed and charged the 2006 Special Committee with reviewing the latest research on tax incidence of the major tax sources, including the policy considerations of moving to a flat-rate income tax. The Committee also was asked to study erosion of sales and property tax bases as part of the review of tax incidence.

COMMITTEE ACTIVITIES

At the September meeting, the Committee received the KACIR studies, which were conducted by the Kansas Public Finance Center, a part of the Hugo Wall School of Urban and Public Affairs at Wichita State University.

Dr. John Wong presented a study on tax incidence. Among the principal findings was a conclusion that the Kansas individual income tax is modestly progressive; and that such progressivity does not completely offset the regressivity of the other major tax sources.

Dr. Wong then presented a study on sales tax base erosion, noting that economic and technological changes in recent years had joined legislatively enacted exemptions as the major sources of erosion. He said that one study had estimated that extending the tax to all "readily taxable" services could increase revenue by over \$500 million. He added that the main arguments for inclusion of additional services in the sales tax base included:

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ATTACHMENT 3**

- the sales tax should be as broadly applicable to consumer expenditures as possible;
- taxation of services would reduce the regressivity of the sales tax;
- revenues would be more responsive to rising levels of personal income; and
- administration of the tax would be simplified if the tax were extended to those services rendered in conjunction with the sales of tangible personal property.

Dr. Glenn Fisher presented a study on property tax base erosion, stating that the Kansas property tax is evolving largely into a real estate tax, due at least in part to the increased propensity of the Legislature to exempt personal property. He said that given the importance of the tax for local government revenue, any major changes in the property tax system would likely be controversial and potentially painful.

At the October meeting, Secretary Wagnon made a number of comments with respect to tax base erosion. She said that if the Legislature continued to allow erosion of the major tax bases, there would be higher tax rates; less equity among various groups of taxpayers; less competitiveness and more taxpayer discontent; and more special interest groups' requesting exemptions—creating a vicious cycle.

She also said that tax base erosion had been occurring because of the enactment of a number of exemptions and tax credits; and because of economic shifts in consumption and business practices, many relating to new technologies. She also said that the authorization of sales tax and revenue (STAR) bonds and the propensity of the Legislature to earmark future revenue streams threatened the elasticity of tax receipts relative to the State General Fund

(SGF). She said that once a special practice or tax treatment had been established, it was often difficult for the Legislature to backtrack and stop that process. Faced with a similar situation more than three decades ago, the "Hodge Committee" in the early 1970s formed a special commission to review tax policies and make decisions on which special exemptions, exceptions, and credits should be restructured or totally eliminated.

The Secretary suggested that the following criteria be considered when evaluating future sales tax exemption requests:

- (1) Does this exemption help maintain the sales tax as a final tax on consumption?
- (2) Does this exemption help make the tax more easily administered, or would it lead to confusion over why one organization or entity is taxed while another is not?
- (3) Who is the principal beneficiary? What would be lost if the exemption were not to be granted?
- (4) Does this exemption establish an unfair competitive advantage for one entity over another?
- (5) Is this exemption targeted to a broad class of taxpayers or a narrow group? If the latter, why should all members of the broad class not be included? If the exemption were to be granted, what other groups would look at the precedent and asked to be added to the exemption?
- (6) What is the public benefit for granting the exemption? Does it outweigh the loss of revenue for the general activities of the state?

Conferees representing AARP and Kansas Action for Children agreed that erosion of the major tax bases needed to stop; and said that a number of exemptions

enacted in recent years had made the overall state and local tax structure more regressive.

Also at the October meeting, the Committee received information from the Department of Revenue on the potential impact on certain taxpayers of moving to a revenue-neutral single income tax ("flat") rate income tax structure. Replacing the current individual income tax rates with a 5.10 percent rate would in the aggregate be revenue-neutral, according to the information. The following table summarizes the average impact per return for taxpayers in various Kansas adjusted gross income (KAGI) brackets:

		Average	
		<u>KAGI Brackets</u>	<u>Dollar Change</u>
\$	0 \$	10,000 \$	15.39
	10,000	20,000	83.26
	20,000	30,000	126.29
	30,000	50,000	206.89
	50,000	75,000	166.19
	75,000	100,000	(45.84)
	100,000	200,000	(562.79)
\$	200,000	Over \$	(3,915.13)

At the November meeting, the Committee reviewed its work at the previous two meetings and made final policy decisions.

CONCLUSIONS AND RECOMMENDATIONS

The Committee expresses its concern about the erosion of all major tax bases, especially the sales tax base. The Committee strongly recommends that the following questions be asked of and answered by all parties seeking sales tax exemption legislation:

- (1) Does this exemption help maintain the sales tax as a final tax on consumption?
- (2) Does this exemption help make the tax more easily administered, or would it lead to confusion over why one organization or entity is taxed while another is not?
- (3) Who is the principal beneficiary? What would be lost if the exemption were not to be granted?
- (4) Does this exemption establish an unfair competitive advantage for one entity over another?
- (5) Is this exemption targeted to a broad class of taxpayers or a narrow group? If the latter, why should all members of the broad class not be included? If the exemption were to be granted, what other groups would look at the precedent and asked to be added to the exemption?
- (6) What is the public benefit for granting the exemption? Does it outweigh the loss of revenue for the general activities of the state?

The Committee further recommends that the leadership of the Senate Assessment and Taxation Committee and the House Taxation Committee develop committee rules that would prohibit advancement of any sales tax exemption legislation until these questions have been answered satisfactorily by proponents of such legislation.

Finally, the Committee recommends that the standing tax committees consider tax incidence and progressivity-regressivity issues with respect to all major state and local tax policy changes.

State Sales Tax Exemptions Summary

Statute	Description of Exemption or Exclusion	Recent Revision	FY2006 (\$ in Millions)	FY2007 (\$ in Millions)	FY2008 (\$ in Millions)	FY2009 (\$ in Millions)	2010 (\$ in Millions)
Tax Rate			5.3%	5.3%	5.3%	5.3%	5.3%
Annual Rate of Increase			3.50%	3.5%	3.5%	3.5%	3.5%
3602 (e)	Definition of retail sales, exempting wholesale sales and sales for resale		\$ -	\$ -	\$ -	\$ -	\$ -
3602 (ii)	Modified definition of sales or selling price to not include cash rebates granted by a manufacturer to a purchaser or lessee of a new motor vehicle if paid indirectly to the retailer as a result of the original sale. The exemption is granted from July 1, 2006 and ending June 30, 2009.	Rev 2006 SB 404		\$ 9.940	\$ 10.288	\$ 10.648	\$ 11.021
3603 (b)	Taxes telephone and telegraph services except creation WATS and private data lines. Bundling of services added in 2001. Modified pre-paid calling cards - revolved phrase dealing with sold in minutes (no fiscal impact).	Rev 2001 SB 1, Rev 2002 SB 39,	\$ 1.304	\$ 1.349	\$ 1.397	\$ 1.445	\$ 1.496
3603 (e)	Admission to any cultural and historical event which occurs triennially	Revised 1994	Minimal	Minimal	Minimal	Minimal	Minimal
3603 (f)	Coin operated Laundry Services		\$ 0.331	\$ 0.342	\$ 0.354	\$ 0.367	\$ 0.380
3603 (g)	Service of renting of rooms by holds or accommodation brokers to federal government or any federal employee in performance of official government duties.	2002 SB39	\$ 0.108	\$ 0.111	\$ 0.115	\$ 0.119	\$ 0.123
3603 (h)	Service of leasing or renting machinery and equipment owned by city purchased with industrial revenue bonds prior to July 1, 1973		\$ -	\$ -	\$ -	\$ -	\$ -
3603 (m)	Fees and charges by any political subdivision, youth recreation organization exclusively providing services to persons 18 or younger organized as a 501(c)(3) for sports, games and other recreational activities and entry fees and charges for participation.	Revised 1994 1998 SB493	\$ 0.816	\$ 0.845	\$ 0.874	\$ 0.905	\$ 0.936
3603 (n)	Dues charged by any organization pursuant to paragraph 8 and 9 of 79-201 (veteran & humanitarian organizations) and zoos	1998 SB493	\$ 0.301	\$ 0.311	\$ 0.322	\$ 0.333	\$ 0.345
3603 (o)	Motor vehicles exchanged for corporate stock, corporate transfer to itself and immediate family member sales.		\$ 0.189	\$ 0.195	\$ 0.202	\$ 0.209	\$ 0.216
3603 (o)	In 2004, changed the way sales tax computed on isolated and occasional sales of vehicles. Estimated to generate \$2 million annually	2004 SB 147					
3603 (p)	Labor services of installing or applying property in original construction of a building or facility or the construction reconstruction, restoration, replacement or repair of a residence, bridge or highway	1998 SB493	\$ 163.982	\$ 169.721	\$ 175.661	\$ 181.809	\$ 188.173
3603 (q)	Exemption for Service of repairing, servicing, maintaining custom computer software as described in section 3603 (e)	1988 Amended 2002 SB39	\$ -	\$ -	\$ -	\$ -	\$ -
3603 (s)	Customized computer software and services for modifying software for single end use and billed as a separate invoiced item. In 2004, amended to tax only prewritten software. Custom software is exempt	1988 Amended 2002 SB39, 2004SB 147	\$ 4.658	\$ 4.821	\$ 4.989	\$ 5.164	\$ 5.345
3603 (v)	Sales of bingo cards, bingo faces and instant bingo tickets. Tax rate 2.5 on July 1, 2001 to June 30, 2002; exempt on July 1, 2002	2000 HB 2013	\$ 2.464	\$ 2.551	\$ 2.640	\$ 2.732	\$ 2.828
3606 (a)	Motor fuels and items taxed by sales or excise tax	1999	\$ 209.721	\$ 217.061	\$ 224.659	\$ 232.522	\$ 240.660
3606 (b)	Property or services purchases by State of Kansas, political subdivision, nonprofit hospital or blood /donor bank. In 2001, deleted sales of water to make purchases for water suppliers exempt. (Neutral FN due to Clean Water Fee)	2001 SB 332	\$ 298.440	\$ 308.885	\$ 319.696	\$ 330.886	\$ 342.467
3606 (c)	Property or services purchased and leasing by elementary or secondary schools and educational institutions		\$ 52.738	\$ 54.584	\$ 56.495	\$ 58.472	\$ 60.518
3606 (d)	Property or services purchased by contractor for building or repair of buildings for nonprofit hospital, elementary or secondary schools or nonprofit educational institutions		\$ 107.288	\$ 111.043	\$ 114.930	\$ 118.952	\$ 123.115
3606 (e)	Property or services purchases by federal government, its agencies or instrumentality's		\$ 4.993	\$ 5.168	\$ 5.349	\$ 5.536	\$ 5.730
3606 (f)	Property purchased by railroad or public utility for use in the movement of interstate commerce		\$ 14.009	\$ 14.500	\$ 15.007	\$ 15.532	\$ 16.076
3606 (g)	Sales, repair or modification of aircraft sold for interstate commerce directly through an authorized agent. IN 2004, expanded aircraft exemption for repair, modification plus parts and labor	1998 SB493, 2004 SB 147	\$ 6.582	\$ 6.812	\$ 7.050	\$ 7.297	\$ 7.552
3606 (h)	Rental of nonsectarian textbooks by elementary or secondary schools		\$ 0.863	\$ 0.893	\$ 0.924	\$ 0.956	\$ 0.990
3606 (i)	Lease or rental of films, records, tapes, etc. by motion picture exhibitors		\$ 1.540	\$ 1.594	\$ 1.650	\$ 1.708	\$ 1.767
3606 (j)	Meals served without charge to employees if duties include furnishing or sale of such meals or drinks		\$ 3.413	\$ 3.533	\$ 3.656	\$ 3.784	\$ 3.917
3606 (k)	Vehicles, trailers or aircraft purchased and delivered out of state to a nonresident		\$ 13.924	\$ 14.411	\$ 14.916	\$ 15.438	\$ 15.978
3606 (l)	Isolated or occasional sales, except motor vehicles		\$ -	\$ -	\$ -	\$ -	\$ -
3606 (m)	Property which becomes an ingredient or component part of property or services produced or manufactured for ultimate sale at retail		\$ 2,027.664	\$ 2,098.633	\$ 2,172.085	\$ 2,248.108	\$ 2,326.791
3606 (n)	Property consumed in the production, manufacturing, processing, mining, drilling, refining or compounding of property; or irrigation of crops for ultimate sale at retail. In 2000, added provision to eliminate refunds from the Johnson County Water case sav		\$ 266.039	\$ 275.351	\$ 284.988	\$ 294.962	\$ 305.286
3606 (o)	Sales of animals, fowl, aquatic plants, and animals used in agriculture or aquaculture, for production of food for human consumption, the production of animal, dairy, poultry, or aquatic products, fiber or fur or the production of offspring.		\$ 149.737	\$ 154.978	\$ 160.402	\$ 166.017	\$ 171.827
3606 (p)	Sales for prescription drugs	1999 SB 45	\$ 63.459	\$ 65.680	\$ 67.978	\$ 70.358	\$ 72.820
3606 (q)	Sales of insulin dispensed by pharmacist for treatment of diabetes		\$ 0.490	\$ 0.507	\$ 0.525	\$ 0.543	\$ 0.562

State Sales Tax Exemptions Summary

Statute	Description of Exemption or Exclusion	Recent Revision	FY2006 (\$ in Millions)	FY2007 (\$ in Millions)	FY2008 (\$ in Millions)	FY2009 (\$ in Millions)	FY2010 (\$ in Millions)
Tax Rate			5.3%	5.3%	5.3%	5.3%	5.3%
Annual Rate of Increase			3.50%	3.5%	3.5%	3.5%	3.5%
3606 (r)	Sales of prosthetic or orthopedic appliances prescribed by a doctor. IN 2004, exempted all hearing aids, prats and batteries by licensed providers	Amended 1997, 2004 SB 147	\$ 7.462	\$ 7.724	\$ 7.994	\$ 8.274	\$ 8.563
3606 (s)	Sales of property or services purchased by a groundwater management district		\$ 0.038	\$ 0.039	\$ 0.041	\$ 0.042	\$ 0.044
3606 (t)	Sales of farm or aquaculture machinery and equipment, parts and services for repair and replacement. In 2006, added work-site utility vehicle as exempt	2006 SB 76	\$ 43.170	\$ 45.118	\$ 47.134	\$ 49.221	\$ 51.381
3606 (u)	Leases or rentals of property used as a dwelling for more than 28 consecutive days.		\$ 0.657	\$ 0.680	\$ 0.704	\$ 0.729	\$ 0.754
3606 (v)	Sales of food products purchased by contractor for use in preparing meals for delivery to homebound elderly persons. In 2004, expanded exemption to all personal property purchased by contractor and sales of food products by or on behalf of contractor or organization	2004 SB 147	\$ 0.750	\$ 0.777	\$ 0.804	\$ 0.832	\$ 0.861
3606 (w)	Sales of natural gas, electricity, heat, & water delivered through mains, lines or pipes to residential premises for noncommercial use, for agricultural use (to include propane gas),for use in severing oil and any property exempt from property taxation. (Updated Oct 06 based on return/stat data)		\$ 97.627	\$ 101.044	\$ 104.580	\$ 108.241	\$ 112.029
3606 (x)	Sales of propane, gas, LP-gas, coal, wood, and other fuel sources for the production of heat or lighting for noncommercial use in a residential premise		\$ 14.727	\$ 15.243	\$ 15.776	\$ 16.328	\$ 16.900
3606 (y)	Sales of materials and services used in repairing, maintaining, etc., of railroad rolling stock used in interstate commerce		\$ 0.845	\$ 0.874	\$ 0.905	\$ 0.936	\$ 0.969
3606 (z)	Property and services purchased directly by a port authority or a contractor therefor.		Minimal	Minimal	Minimal	Minimal	Minimal
3606 (aa)	Materials and services brought into Kansas for usage outside of Kansas for repair, services, alteration, maintenance, etc. used for the transmission of liquids or national gas by a pipeline in interstate commerce		Minimal	Minimal	Minimal	Minimal	Minimal
3606 (bb)	Used mobile and manufactured homes		\$ 3.999	\$ 4.139	\$ 4.284	\$ 4.433	\$ 4.589
3606 (cc)	Property or services purchased for constructing, reconstructing, enlarging or remodeling a business; sale and installation of machinery and equipment purchased for installation in such business. (Enterprise Zone Exemption)		\$ 59.146	\$ 61.216	\$ 63.358	\$ 65.576	\$ 67.871
3606 (dd)	Property purchased with food stamps issued by US Department of Agriculture		\$ 6.839	\$ 7.078	\$ 7.326	\$ 7.582	\$ 7.848
3606 (ee)	Lottery tickets and shares made as part of a lottery operated by the State of Kansas		\$ 12.729	\$ 13.174	\$ 13.636	\$ 14.113	\$ 14.607
3606 (ff)	New mobile or manufactured homes to the extent of 40% of the gross receipts		\$ 2.932	\$ 3.035	\$ 3.141	\$ 3.251	\$ 3.365
3606 (gg)	Property purchased with vouchers issued pursuant to the federal special supplemental food program for women, infants and children		n/a	n/a	n/a	n/a	n/a
3606 (hh)	Medical supplies and equipment purchased by nonprofit skilled nursing home or intermediate nursing care home for providing medical services to residents		\$ 0.939	\$ 0.972	\$ 1.006	\$ 1.041	\$ 1.077
3606 (ii)	Property purchased by nonprofit organization for nonsectarian comprehensive multidiscipline youth development programs and activities and sales of property by or on behalf of such organization	1998 SB493	\$ 2.369	\$ 2.452	\$ 2.538	\$ 2.627	\$ 2.719
3606 (jj)	Property and services, includes leasing of property, purchased for community-based mental retardation facility or mental health center.	2004 SB 147	\$ 2.176	\$ 2.252	\$ 2.331	\$ 2.413	\$ 2.497
3606(kk)	Machinery and equipment used directly and primarily in the manufacture, assemblage, processing, finishing, storing, warehousing or distributing of property for resale by the plant or facility. In 2004, added exemption for building new facility in Riverton Ks (minimal impact)	1998 HB2584	\$ 104.453	\$ 108.109	\$ 111.893	\$ 115.809	\$ 119.862
3606 (ll)	Educational materials purchased for distribution to the public at no charge by a nonprofit public health corporation		\$ 0.073	\$ 0.076	\$ 0.078	\$ 0.081	\$ 0.084
3606 (mm)	Seeds, tree seedlings, fertilizers, insecticides, etc., and services purchased and used for producing plants to prevent soil erosion on land devoted to agricultural use.	1988 HB2626	\$ 0.862	\$ 0.892	\$ 0.924	\$ 0.956	\$ 0.989
3606 (nn)	Services rendered by advertising agency or broadcast station		\$ 3.820	\$ 3.954	\$ 4.092	\$ 4.235	\$ 4.383
3606 (oo)	Property purchased by a community action group or agency to repair or weatherize housing occupied by low income individuals.		Minimal	Minimal	Minimal	Minimal	Minimal
3606 (pp)	Drill bits and explosives used in the exploration and production of oil or gas		\$ 0.363	\$ 0.376	\$ 0.389	\$ 0.403	\$ 0.417
3606 (qq)	Property and services purchased by a nonprofit museum or historical society which is organized under the federal income taxation code as a 501 (c)(3)		\$ 0.356	\$ 0.369	\$ 0.382	\$ 0.395	\$ 0.409
3606 (rr)	Property which will admit purchases to an annual event sponsored by a nonprofit organization organized under the federal income taxation code as a 501 (c)(3)		\$ 0.030	\$ 0.031	\$ 0.032	\$ 0.033	\$ 0.034
3606 (ss)	Property and services purchased by a public broadcasting station licensed by FCC as a noncommercial educational television or radio station.		Minimal	Minimal	Minimal	Minimal	Minimal
3606 (tt)	Property and services purchased by not-for-profit corporation for the sole purpose of constructing a Kansas Korean War memorial and is organized under the federal income taxation code as a 501 (c)(3)	1996 HB2656	\$ -	\$ -	\$ -	\$ -	\$ -
3606 (uu)	Property and services purchased by rural fire fighting organization	1997 SB184	Minimal	Minimal	Minimal	Minimal	Minimal

State Sales Tax Exemptions Summary

Statute	Description of Exemption or Exclusion	Recent Revision	FY2006 (\$ in Millions)	FY2007 (\$ in Millions)	FY2008 (\$ in Millions)	FY2009 (\$ in Millions)	/2010 (\$ in Millions)
Tax Rate			5.3%	5.3%	5.3%	5.3%	5.3%
Annual Rate of Increase			3.50%	3.5%	3.5%	3.5%	3.5%
3606 (vv)	Property purchased by the following organizations who are organized under the federal income taxation code as a 501 (c)(3): American Heart Association, Kansas Affiliate; Kansas Alliance for the Mentally Ill, Inc.; Kansas Mental Illness Awareness Council; in 2004 added: Heartstrings Community Foundation, Cystic Fibrosis, Spina Bifida Assn, CHWC, Inc., Cross-lines Cooperative Council, Dreams Work, Inc., KSDS, Inc., Lyme Association of Grater Kansas City, Inc	1997 SB184, 2001 HB 2029, 2004 SB 147, 2006 SB 404	\$ 0.084	\$ 0.169	\$ 0.257	\$ 0.348	\$ 0.443
3606 (ww)	Property purchased by the Habitat for Humanity for use within a housing project	1997 SB184	\$ 0.103	\$ 0.107	\$ 0.111	\$ 0.115	\$ 0.119
3606 (xx)	Property and services purchases by nonprofit zoo or on behalf of a zoo by an entity that is a 501(c)(3)	1998 SB493	\$ 0.544	\$ 0.563	\$ 0.583	\$ 0.603	\$ 0.624
3606 (yy)	Property and services purchased by a parent-teach association or organizations and all sales of tangible personal property by or on behalf of such association	1998 SB493	\$ 0.511	\$ 0.529	\$ 0.547	\$ 0.567	\$ 0.586
3606 (zz)	Machinery and equipment purchased by over-the-air free access radio or television station used directly and primarily for producing signal or the electricity essential for producing the signal.	1998 SB493	\$ 0.859	\$ 0.889	\$ 0.920	\$ 0.952	\$ 0.985
3606(aaa)	Property and services purchased by religious organizations and used exclusively for religious purposes	1998 SB493	\$ 15.649	\$ 16.197	\$ 16.764	\$ 17.350	\$ 17.958
3606 (bbb)	Sales of food for human consumption by organizations exempt by 501(c)(3) pursuant to food distribution programs which offers such food at a price below cost in exchange for the performance of community service by the purchaser.	1998 SB493		\$ -	\$ -	\$ -	\$ -
3606 (ccc)	Property and services purchases by health care centers and clinics who are serving the medically underserved.	1999 SB 45	\$ 0.341	\$ 0.353	\$ 0.365	\$ 0.378	\$ 0.391
3606 (ddd)	Property and services purchases by any class II or III railroad (shortline) for track and facilities used directly in interstate commerce. Only for calendar year 1999.	1999 SB 45	n/a	n/a	n/a	n/a	n/a
3606 (eee)	Property and services purchases for reconstruction, reconstruction, renovation, repair of grain storage facilities or railroad sidings. Only for calendar year 1999 and 2000.	1999 SB 45, 2000 SB 59	n/a	n/a	n/a	n/a	n/a
3606 (fff)	Material handling equipment, racking systems & other related machinery & equipment used for the handling, movement or storage of tangible personal property in a warehouse or distribution facility; installation, repair, maintenance services, and replacement parts.	2000 HB 2011	\$ 5.656	\$ 5.854	\$ 6.059	\$ 6.271	\$ 6.490
3606 (ggg)	Property and services purchased by or on behalf of the Kansas Academy of Science.	2000 SB 59	Minimal	Minimal	Minimal	Minimal	Minimal
3606 (hhh)	Property and services purchased by or on behalf of Domestic Violence Shelters as members of the Kansas coalition against Sexual and Domestic Violence	2004 SB 147	\$ 0.052	\$ 0.054	\$ 0.055	\$ 0.057	\$ 0.059
3606 (iii)	Property and services purchased by orgnaizations distributing food without charge to other nonprofit food distribution programs. Includes taxes paid on and after July 1, 2005 and prior to July 1, 2006.	2006 SB 404	\$ -	\$ 0.222	\$ 0.230	\$ 0.238	\$ 0.246
3606 (jjj)	Sales of dietary supplements dispensed by prescription order by a licensed practitioner or mid-level prectitioner.	2006 SB 404		Minimal	Minimal	Minimal	Minimal
3606 (kkk)							
3606 (lll)	Property and services purchased by Special Olympics Kansas, Inc., and sales made by or on behalf of Special Olympics.	2006 SB 404		\$ 0.025	\$ 0.026	\$ 0.027	\$ 0.028
3606 (mmm)	Property and services purchased by Marillac Center, Inc. and sales made by or on behalf of the Marillac Center.	2006 SB 404		\$ 0.050	\$ 0.052	\$ 0.054	\$ 0.055
3606 (nnn)	Property and services purchased by West Sedgwick County - Sunrise Rotary Club for consturcting boundless playground.	2006 SB 404		\$ 0.020	\$ 0.021	\$ 0.021	\$ 0.022
3606 (ooo)	Sales made by or on behalf of a public library	2006 SB 404		\$ 0.010	\$ 0.010	\$ 0.011	\$ 0.011
3606 (ppp)	Property and services purchased by non-profit Homeless Shelters, and sales made by or on behalf of these organizations.	2006 SB 404		\$ 0.100	\$ 0.104	\$ 0.107	\$ 0.111
3606 (qqq)	Property and services purchased by TLC for Children and Families, Inc. and sales made by or on behalf of TLC	2006 SB 404		\$ 0.160	\$ 0.166	\$ 0.171	\$ 0.177
3606 (rrr)	Property and services purchased by county law library, and sales made by or on behalf of these organizations.	2006 SB 404		\$ 0.100	\$ 0.104	\$ 0.107	\$ 0.111
3606 (sss)	Property and services purchased by catholic charities or youthville and sales made by or on behalf of catholic charities or youthville	2006 SB 404		\$ 0.600	\$ 0.621	\$ 0.643	\$ 0.665
3606 (ttt)	Property and services purchased a contractor for a purpose of restoring, consturcting, equipping, reconstructing, maintaining, repairing, enlarging, furnishing or remodeling a home or facility owned by a nonprofit museum which is a qualified under the governor hometown heritage act (KSA 75-5071)	2006 SB 404		\$ 0.100	\$ 0.104	\$ 0.107	\$ 0.111
3606 (uuu)	Property and services purchased by Kansas Children's Service League and sales made by or on behalf of the KC SL	2006 SB 404		\$ 0.140	\$ 0.145	\$ 0.150	\$ 0.155
	Total		\$ 3,767.081	\$ 3,931.934	\$ 4,070.071	\$ 4,213.043	\$ 4,361.018

Updated through 2006 Legislative changes.

Kansas Department of Revenue

Individual Income Tax Structure

January 17, 2007

Kansas conforms to the federal definition of adjusted gross income and the federal definition of itemized deductions. Kansas also piggyback's the federal earned income credit, which is 15% of the amount claimed on the federal return, child care credit and adoption expense credit, which are equal to 25% of the amount claimed on the federal return. Kansas does not conform to federal standard deduction or personal exemption amounts or any other federal income tax credits. Kansas does not allow federal income tax liability to be deducted, so any increase or decrease in federal income tax liability will have no impact on Kansas income tax revenues.

Any changes made by the federal government which modify adjusted gross income or itemized deductions will cause either a positive or negative impact to the state. Any changes in the federal earned income credit, child care credit and the adoption expense credit will flow through to Kansas with either a positive or negative impact.

Federal Adjusted Gross Income

Wages
Interest
Dividends
Taxable Refunds
Alimony
Business Income
Capital Gains
Other Gains
IRA Distributions
Pensions and Annuities
Rental Real Estate, Royalties, Partnerships, S Corporations, Trusts, etc.
Farm Income
Unemployment Compensation
Social Security Benefits
Other Income

Less:

Educator Expenses
IRA Deduction
Student Loan Interest deduction
Tuition and Fees Deduction
Moving Expenses
One-Half of Self-Employment Tax
Self-Employed Health Insurance Deduction
Self-Employed SEP, SIMPLE, and Qualified Plans
Penalty on early withdrawal of Savings

Alimony Paid

Federal Itemized Deductions

Medical and Dental Expenses (to the extent they exceed 7.5% of FAGI)
State and Local Taxes Paid
Interest Paid
Gifts to Charity
Casualty and Theft Losses
Job Expenses and Miscellaneous Deductions (to the extent they exceed 2% of FAGI)
Other Miscellaneous Deductions

Kansas Adjusted Gross Income

Federal Adjusted Gross Income

Plus:

State and Municipal Bond Interest (Kansas State and Municipal bonds issued after December 31, 1987 are exempt)
Contributions to KPERs
Federal Net Operation Loss Carry Forward
Other Additions

Less:

Interest on U.S. Obligations
Kansas Net Operating Loss Carry Forward
Exempt Retirement Benefits
Military Compensation of a Nonresident Servicemember
Learning Quest Education Saving Program
Other Subtractions

Kansas Deductions

Itemized Deductions – Federal Itemized Deductions less State Income Taxes
Or
Standard Deductions
Married Filing Joint \$6,000
Single/Married Filing Separate \$3,000
Head of Household \$4,500
Exemption Allowance \$2,250

Kansas Tax Rates and Brackets

Tax Year 1998 to Present

Taxable income Brackets

Single				Married			
\$ -	-	\$ 15,000	3.50%	\$ -	-	\$ 30,000	3.50%
\$ 15,000	-	\$ 30,000	6.25%	\$ 30,000	-	\$ 60,000	6.25%
\$ 30,000	-	Over	6.45%	\$ 60,000	-	Over	6.45%

Kansas Credits

Non-Refundable:


- Credit for Taxes Paid to Other States
- Child and Dependent Care Credit
- Adoption Credit
- Agricultural Loan Interest Reduction Credit
- Agritourism Liability Insurance Credit
- Angel Investor Credit
- Alternative Fuel Credit
- Assistive Technology Contribution Credit
- Business and Job Development Credit
- Cellulosic Plant Credit
- Center for Entrepreneurship Credit
- High Performance Incentive Program Credit
- Historic Preservation Credit
- Integrated Coal Gasification Credit
- Law Enforcement Training Center Credit
- Mathematics and Science Teacher Employment Credit
- National Guard & Reserve Employer Credit
- Nitrogen Fertilizer Plant Credit
- Petroleum Refinery Credit
- Plugging an Abandoned Gas or Oil Well Credit
- Qualifying Pipeline Credit
- Research and Development Credit
- Swine Facility Improvement Credit
- Temporary Assistance to Families Contribution Credit
- Venture and Local Seed Capital Credit

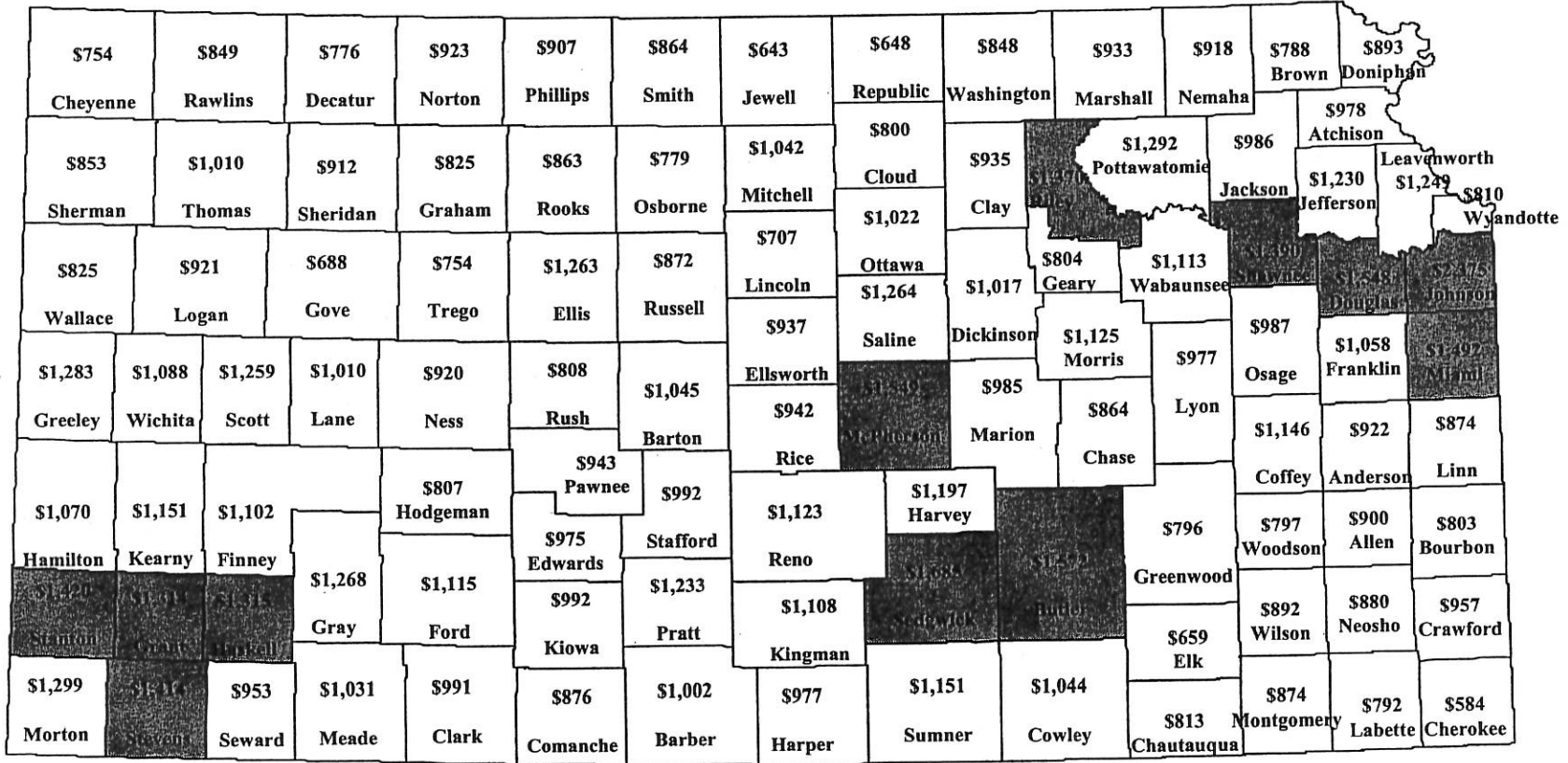
Refundable:

- Earned Income Credit
- Food Sales Tax Refund
- Business Machinery and Equipment Credit
- Child Day Care Assistance Credit
- Community Service Contribution Credit
- Disabled Access Credit
- Individual Development Account Credit
- Regional Foundation Credit
- Single City Port Authority Credit
- Small Employer Health Insurance Contribution Credit
- Telecommunications & Railroad Credit

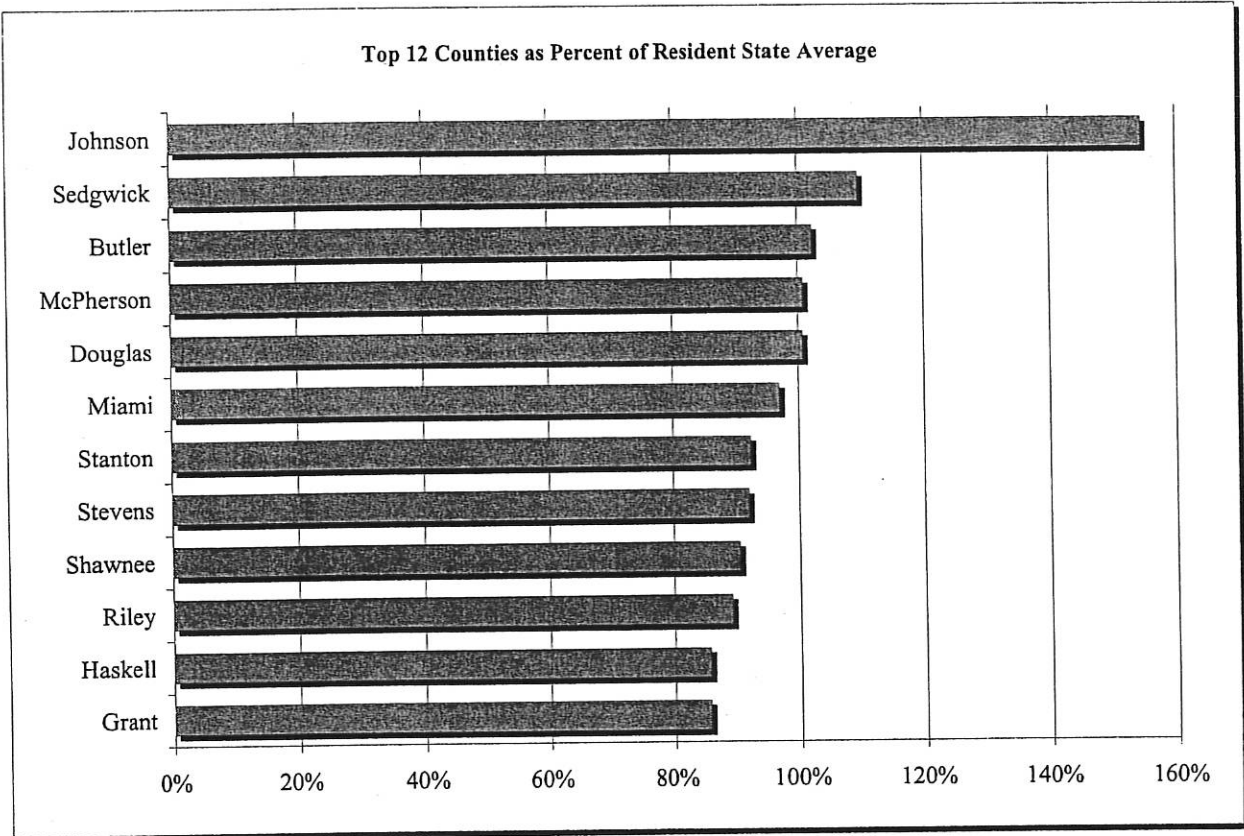
Individual Income Tax Liability Tax Year 2004

The map below shows each county's average tax liability per return. The twelve shaded areas display the counties with the highest average tax liability per return.

 Top 12 counties with highest average tax liability per return



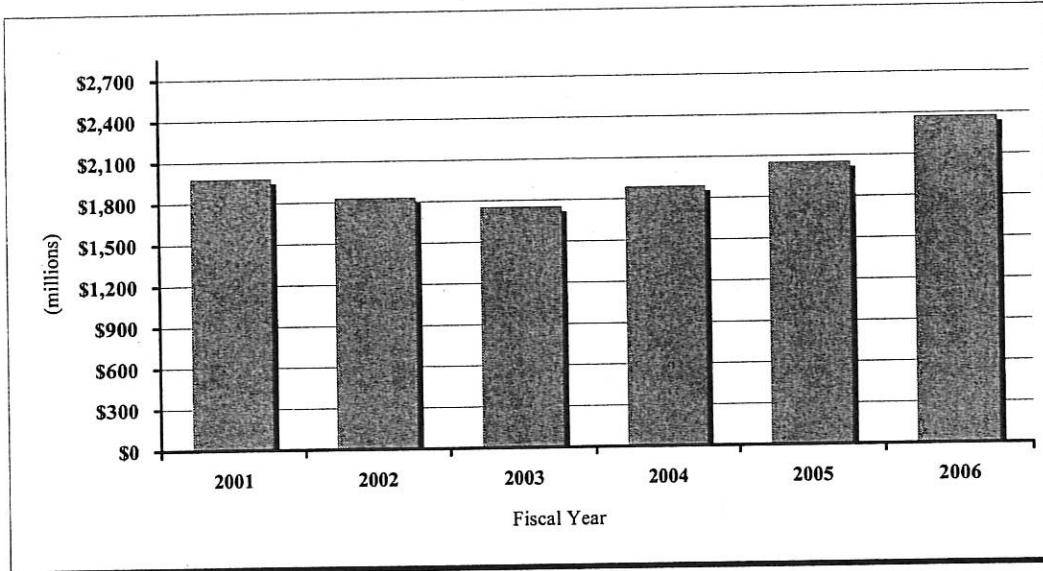
Top Twelve Kansas Counties with Highest Average Tax Liability per Return Tax Year 2004



<u>Top 12 Counties</u>	<u>Average Tax Liability</u>	<u>Rank</u>	<u>Top 12 Counties as a Percent of Resident Average</u>
Johnson	\$2,375	1	155%
Sedgwick	\$1,685	2	110%
Butler	\$1,572	3	102%
McPherson	\$1,549	4	101%
Douglas	\$1,548	5	101%
Miami	\$1,492	6	97%
Stanton	\$1,420	7	92%
Stevens	\$1,414	8	92%
Shawnee	\$1,390	9	90%
Riley	\$1,370	10	89%
Haskell	\$1,315	11	86%
Grant	\$1,314	12	85%
Average Kansas Residents (top 12 counties)			100%
			\$1,537

Individual Income Tax Amount to the State General Fund after Refunds

Kansas individual income tax rates by income brackets and filing status can be found on the Tax Rates table in this Annual Report.

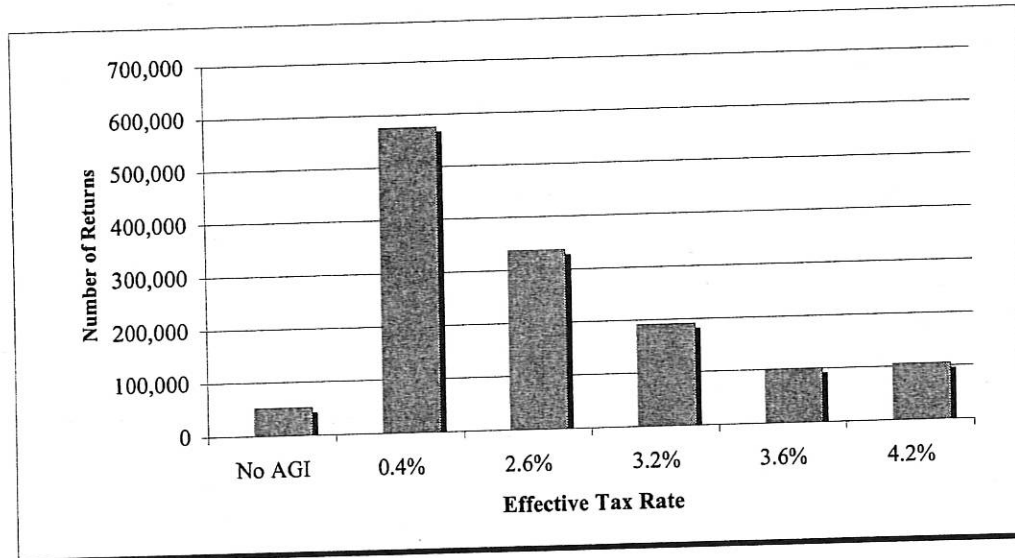


<u>Fiscal Year</u>	<u>Amount Collected</u>	<u>Percent Change</u>
2001	\$1,977,341,638	6.6%
2002	\$1,829,611,161	(7.5%)
2003	\$1,750,054,137	-4.3%
2004	\$1,888,431,039	7.9%
2005	\$2,050,562,199	8.6%
2006	\$2,371,252,554	15.6%

Kansas Individual Income Tax by Adjusted Gross Income Bracket

Resident Taxpayers, Tax Year 2004

Number of Returns Within Each Effective Tax Rate



<u>Effective Tax Rate on Adjusted Gross Income *</u>	<u>Kansas Adjusted Gross Income Brackets</u>	<u>Number of Returns</u>	<u>Kansas Adjusted Gross Income</u>	<u>Tax Liability After All Credits</u>
	No AGI -	52,195	(\$1,322,008,271)	(\$4,701,766)
0.40%	\$0 - \$25,000	575,628	\$6,702,903,385	\$26,657,825
2.61%	\$25,000 - \$50,000	337,012	\$12,186,827,297	\$318,521,833
3.23%	\$50,000 - \$75,000	191,579	\$11,748,068,656	\$379,477,814
3.65%	\$75,000 - \$100,000	100,467	\$8,622,101,793	\$314,419,536
4.23%	\$100,000 - Over	<u>104,822</u>	<u>\$22,422,521,495</u>	<u>\$949,340,661</u>
3.29%	Total Kansas Residents	1,361,703	\$60,360,414,355	\$1,983,715,903

* Effective rate is the tax liability (after all credits) divided by the adjusted gross income.

Individual Income Tax for Tax Year 2004 by County

Resident Taxpayers Only

County	Number Returns	Kansas Adjusted Gross Income	Tax Year Liability	Percent of Total Liability	Per Return Average	
					Tax Liability	Rank
Allen	7,112	219,269,425	6,399,476	0.3%	\$900	69
Anderson	4,116	130,481,414	3,795,426	0.2%	\$922	63
Atchison	7,856	266,933,562	7,684,130	0.4%	\$978	51
Barber	2,519	80,969,921	2,524,460	0.1%	\$1,002	44
Barton	13,564	451,783,668	14,178,091	0.7%	\$1,045	36
Bourbon	7,001	208,859,386	5,621,446	0.3%	\$803	90
Brown	5,245	149,559,219	4,130,803	0.2%	\$788	95
Butler	29,119	1,303,650,095	45,765,727	2.4%	\$1,572	3
Chase	1,347	39,167,593	1,163,450	0.1%	\$864	78
Chautauqua	1,786	53,278,509	1,451,778	0.1%	\$813	85
Cherokee	9,704	284,537,436	5,663,454	0.3%	\$584	105
Cheyenne	1,454	24,923,073	1,096,849	0.1%	\$754	98
Clark	1,086	35,441,112	1,076,088	0.1%	\$991	47
Clay	4,137	127,273,845	3,867,618	0.2%	\$935	60
Cloud	4,814	136,303,061	3,849,477	0.2%	\$800	91
Coffey	4,400	157,341,151	5,040,979	0.3%	\$1,146	26
Comanche	986	30,610,350	864,111	0.0%	\$876	73
Cowley	16,822	583,060,680	17,569,296	0.9%	\$1,044	37
Crawford	17,698	580,065,450	16,933,560	0.9%	\$957	55
Decatur	1,610	42,078,986	1,248,852	0.1%	\$776	97
Dickinson	9,773	316,028,354	9,938,318	0.5%	\$1,017	41
Doniphan	4,258	168,828,286	3,804,353	0.2%	\$893	70
Douglas	47,450	2,094,767,169	73,447,572	3.8%	\$1,548	5
Edwards	1,581	47,971,692	1,542,149	0.1%	\$975	54
Elk	1,563	39,901,420	1,030,565	0.1%	\$659	102
Ellis	13,471	497,893,704	17,007,280	0.9%	\$1,263	18
Ellsworth	2,947	91,881,727	2,762,182	0.1%	\$937	59
Finney	17,317	618,334,325	19,088,744	1.0%	\$1,102	32
Ford	13,832	508,622,486	15,424,962	0.8%	\$1,115	29
Franklin	12,614	450,984,387	13,350,894	0.7%	\$1,058	35
Geary	10,793	316,639,743	8,672,962	0.4%	\$804	89
Gove	1,554	38,657,007	1,069,198	0.1%	\$688	101
Graham	1,349	37,261,907	1,112,783	0.1%	\$825	83
Grant	3,513	136,169,388	4,615,209	0.2%	\$1,314	12
Gray	3,048	114,071,821	3,863,411	0.2%	\$1,268	16
Greeley	699	25,107,486	896,965	0.0%	\$1,283	15
Greenwood	3,593	100,294,753	2,860,053	0.1%	\$796	93
Hamilton	1,138	34,606,348	1,217,794	0.1%	\$1,070	34
Harper	3,263	104,035,783	3,189,228	0.2%	\$977	52
Harvey	16,827	626,785,769	20,146,007	1.0%	\$1,197	23
Haskell	1,828	70,913,609	2,403,420	0.1%	\$1,315	11
Hodgeman	943	26,810,203	761,254	0.0%	\$807	88
Jackson	6,661	217,861,209	6,568,434	0.3%	\$986	49
Jefferson	9,403	368,327,484	11,562,818	0.6%	\$1,230	22
Jewell	1,745	43,041,648	1,121,494	0.1%	\$643	104
Johnson	251,129	17,594,855,091	596,464,985	30.7%	\$2,375	1
Kearny	1,841	65,824,338	2,118,723	0.1%	\$1,151	24
Kingman	3,978	137,976,156	4,407,132	0.2%	\$1,108	31
Kiowa	1,552	48,911,972	1,539,945	0.1%	\$992	45
Labette	10,642	305,561,227	8,431,686	0.4%	\$792	94
Lane	977	31,720,740	986,347	0.1%	\$1,010	43
Leavenworth	28,391	1,171,464,509	35,473,172	1.8%	\$1,249	20
Lincoln	1,673	43,550,363	1,183,050	0.1%	\$707	100
Linn	4,593	147,085,966	4,013,334	0.2%	\$874	75
Logan	1,590	48,121,262	1,464,889	0.1%	\$921	64
Lyon	17,136	558,152,697	16,743,105	0.9%	\$977	53
Marion	6,127	198,704,957	6,033,236	0.3%	\$985	50
Marshall	5,590	172,652,505	5,216,883	0.3%	\$933	61

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Individual Income Tax for Tax Year 2004 by County

Resident Taxpayers Only

County	Number Returns	Kansas Adjusted Gross Income	Tax Year Liability	Percent of Total Liability	Per Return Average	
					Tax Liability	Rank
McPherson	14,833	658,963,518	22,981,031	1.2%	\$1,549	4
Meade	1,971	65,531,157	2,031,149	0.1%	\$1,031	39
Miami	13,659	639,634,243	20,376,370	1.0%	\$1,492	6
Mitchell	3,460	114,594,937	3,606,158	0.2%	\$1,042	38
Montgomery	17,503	544,841,889	15,297,676	0.8%	\$874	74
Morris	2,805	96,079,363	3,156,699	0.2%	\$1,125	27
Morton	1,579	61,194,000	2,051,554	0.1%	\$1,299	13
Nemaha	5,302	169,252,773	4,867,865	0.3%	\$918	66
Neosho	8,310	253,428,216	7,311,954	0.4%	\$880	72
Ness	1,649	49,901,428	1,516,517	0.1%	\$920	65
Norton	2,588	76,628,292	2,389,781	0.1%	\$923	62
Osage	8,523	286,906,050	8,409,831	0.4%	\$987	48
Osborne	2,062	56,366,289	1,605,314	0.1%	\$779	96
Ottawa	3,176	106,744,771	3,246,374	0.2%	\$1,022	40
Pawnee	3,273	100,166,159	3,086,725	0.2%	\$943	57
Phillips	2,931	84,597,315	2,658,644	0.1%	\$907	68
Pottawatomie	8,956	366,509,757	11,574,486	0.6%	\$1,292	14
Pratt	4,709	165,987,252	5,806,214	0.3%	\$1,233	21
Rawlins	1,378	38,251,429	1,169,385	0.1%	\$849	81
Reno	31,059	1,095,102,083	34,866,541	1.8%	\$1,123	28
Republic	2,730	70,270,159	1,768,001	0.1%	\$648	103
Rice	4,880	157,346,033	4,594,653	0.2%	\$942	58
Riley	21,581	842,610,436	29,564,438	1.5%	\$1,370	10
Rooks	2,655	77,229,828	2,291,231	0.1%	\$863	79
Rush	1,810	50,242,415	1,462,002	0.1%	\$808	87
Russell	3,744	108,101,017	3,265,049	0.2%	\$872	76
Saline	28,305	1,098,636,104	35,787,964	1.8%	\$1,264	17
Scott	2,462	89,169,522	3,098,795	0.2%	\$1,259	19
Sedgwick	232,748	10,784,715,269	392,104,915	20.2%	\$1,685	2
Seward	9,960	341,780,822	9,490,475	0.5%	\$953	56
Shawnee	94,432	3,810,789,711	131,236,509	6.8%	\$1,390	9
Sheridan	1,355	39,828,893	1,236,163	0.1%	\$912	67
Sherman	3,195	92,306,259	2,723,795	0.1%	\$853	80
Smith	2,226	61,801,581	1,923,160	0.1%	\$864	77
Stafford	2,248	72,409,745	2,229,306	0.1%	\$992	46
Stanton	1,101	44,282,405	1,563,376	0.1%	\$1,420	7
Stevens	2,411	98,014,112	3,409,911	0.2%	\$1,414	8
Sumner	10,864	396,372,425	12,502,668	0.6%	\$1,151	25
Thomas	3,876	123,053,967	3,915,625	0.2%	\$1,010	42
Trego	1,589	41,215,707	1,198,603	0.1%	\$754	99
Wabaunsee	3,308	118,392,161	3,681,249	0.2%	\$1,113	30
Wallace	830	24,353,195	684,645	0.0%	\$825	84
Washington	3,274	94,270,757	2,775,867	0.1%	\$848	82
Wichita	1,400	47,760,247	1,523,327	0.1%	\$1,088	33
Wilson	4,977	147,976,354	4,437,934	0.2%	\$892	71
Woodson	1,759	45,916,222	1,401,583	0.1%	\$797	92
Wyandotte	78,193	2,633,881,325	63,297,887	3.3%	\$810	86
KS Residents with county indicator	1,336,397	\$59,069,375,019	\$1,942,639,006		\$1,454	
KS Residents with no county indicator	<u>25,306</u>	<u>\$1,291,039,336</u>	<u>\$41,076,897</u>		\$1,623	
Total Residents	1,361,703	\$60,360,414,355	\$1,983,715,903	87.6%	\$1,457	
Non-Residents	<u>238,788</u>	<u>\$44,717,346,552</u>	<u>\$280,398,296</u>	<u>12.4%</u>	\$1,174	
All Taxpayers	1,600,491	\$105,077,760,907	\$2,264,114,199	100.0%	\$1,415	

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