

MINUTES OF THE HOUSE TAXATION COMMITTEE

The meeting was called to order by Chairman Kenny Wilk at 9:00 A.M. on February 13, 2007 in Room 519-S of the Capitol.

All members were present except:  
Representative Kinzer

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:  
Hon. Maurice P. McTigue, Q.S.O., Mercatus Center, George Mason University

Others attending:  
See attached list.

The Chairman called for bill introductions.

Whitney Damron, on behalf of ONEOK, Inc. requested a bill introduction regarding filing exemption for publicly traded partnerships. Representative Owens moved the introduction. Representative Carlson seconded the motion. The motion carried.

Representative Menghini made a motion to introduce a bill regarding a majority vote required for a three member county commission for a special benefit district. Representative Owens seconded the motion. The motion carried.

Vice-Chair Carlson introduced the Honorable Maurice P. McTigue, from the Mercatus Center at George Mason University in Washington D.C. He is a former Legislator, serving in the Parliament of New Zealand, during 1984-1994, when they accomplished major revenue systems (tax) and economic reforms for their government.

Mr. McTigue, said the Mercatus Center is a resource organization, privately funded, attached to George Washington University. They look at how one can convert academic thought into strategies that can be used by legislators as a means of doing the work of government in a better way. He explained the philosophy behind the changes was centered around shifting risk away from government, and moving it back to communities, industries, and in some cases taken away from taxpayers, paying for them at all.

He gave a power point presentation on *Gathering the Revenue*, explaining the process used in New Zealand's economic reform (Attachment 1). Two other documents were distributed during his presentation, 1) a memorandum from Richard W. Rahn, Director General of the Center for Global Economic Growth, a project of the Freedom Works Foundation, entitled *Economic literacy test....and advice*, and 2) a simplified process and structure used by the New Zealand government when it considering the introduction of "a value added tax" (Attachment 2).

He provided demographics on New Zealand and answered Committee member's questions regarding their experience.

The Chairman thanked Mr. McTigue for his presentation. The meeting was adjourned at 10:25 a.m. The next meeting is February 14, 2007.

# TAXATION COMMITTEE

DATE: FEBRUARY 13

NAME	REPRESENTING
Whitney Jansen	ONCOR, Inc.
ALAN COBB	America for Prosperity
Trent Sebitts	Americans for Prosperity
TERRY FORSYTH	KNEA
Carolyn Gaston	EMBARQ
Dan Karber	Kansas, Inc
Michelle Peterson	Capitol Strategies

# Gathering the Revenue

HS TAXATION COMMITTEE  
2-13-07  
Attachment 1

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MERCATUS CENTER  
AT GEORGE MASON UNIVERSITY

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[www.mercatus.org](http://www.mercatus.org)

**Kansas State Legislature**  
**House Taxation**  
**Committee**

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Hon. Maurice McTigue

Director,

Government Accountability  
Project, Mercatus Center

February 13<sup>th</sup>, 2007

# **The New Zealand Experience**

Shifting Risk Away From Government

# What's the problem?

- What is wrong with the current system?
- The importance of “selling” the problem.
- The nature of the problem should have a significant impact on the design of the reform.

# **How much should be changed?**

- What should drive the scale of the reform?

# **What Should Drive Change Decisions?**

- The change should fix the problem!
- Policy positions should be based on clearly articulated principles.
- The validity of each decision should be checked against these principles.
- Long term solutions are superior to short term fixes.
- The best results come from fixing everything at the same time.



# Developing a Strategy

- What goals are to be achieved?
- Is the program politically achievable?
- Are the changes proposed politically sustainable in the long term?

# **What is the Purpose of the Revenue System?**

- To fund the governments activities?
- To change behavior?
- To deliver social policy?
- To redistribute wealth?

# Building a Revenue System

- To raise sufficient revenue to meet the essential expenditures of the Government by the most efficient means possible, while encouraging economic growth, business investment and employment.
- The revenue system should advance the economic and social objectives of the Government and be judged to be fair by the majority of the people.

# Goals for Tax Reform in New Zealand

- A broad tax base with low rates
- A mix of income and consumption taxes
- Seen to be fair by the majority of the public
- Secure against leakage & evasion
- Raises as much revenue as the old system
- Must improve international competitiveness
- Ease of compliance
- No double taxes

# New Zealand Results

- Tax rates were halved.
- Revenue increased 20%.
- Everyone pays some tax.
- Eliminated capital gains, death, excise, sales, payroll taxes & tariffs.
- Eliminated double taxation.
- Eliminated tax breaks.
- Social policy delivered by direct payment.
- 67% of taxpayers don't have to file tax returns.
- 20 years with no major change.



# Incentives Matter

- Perceived unfairness promotes system abuse.
- High tax rates encourage avoidance and evasion.
- Bad tax systems chase investors away.
- Good tax systems attract investors and jobs.

# The Collection System

- Gather all the revenue owed at the least cost and with the least disruption to peoples' lives.
- So what instructions would you give to the IRS equivalent?

# Internal Revenue Service

- Maximize the revenue gathered by voluntary compliance.
- Minimize the opportunity for errors.
- Resolve disputes expeditiously.
- Prosecute crooks.
- ***Prosecute only crooks.***



# The Inland Revenue Service

1-15

- Mission: To collect the revenue owed.
- Appropriation: \$117.430 million
- Output class – Audits & Investigations
  
- Contract: 137,000 investigations and verification checks,  
58,000 GST audits and checks,  
20,000 payroll audits

Tax assessed per dollar spent:

\$14.00 per investigation

\$4.00 per verification

\$6.00 per GST audit

\$5.00 per payroll audit

All audits and checks must meet 100% of the standards and timeframes outlined in the National Quality Statements.

# IRELAND

- The only poor developed country
- Tax rates in 1985: top 65%, bottom 35%
- 2000 rates: top 40%, bottom 20%
- GDP growth: from 0.4% to 10% pa
- Unemployment: from 15.7% to 3.7%
- Corporate tax: from 50% to 12.5%
- Capital gains tax: from 40% to 27%
- Debt: from 118% of GDP to 39%

# IRELAND RESULTS

- Revenue results
- Personal income tax revenue up 5-fold
- Corporate tax revenue up 600%
- Capital gains tax revenue up 40%
- Deficit of 14% of GDP
- Surplus of 5% of GDP
- Unemployment down from 23% to 4%

# **Anecdotes on Laffer Curve**

- Russia: Instituted 13% flat tax in 2001.  
by 2005 revenue increased 100%.
- India: Reduced income tax from 65% to 50%.  
Revenue increased 40%.
- New Zealand: Halved tax rates.  
Revenue increased 20% in first year.

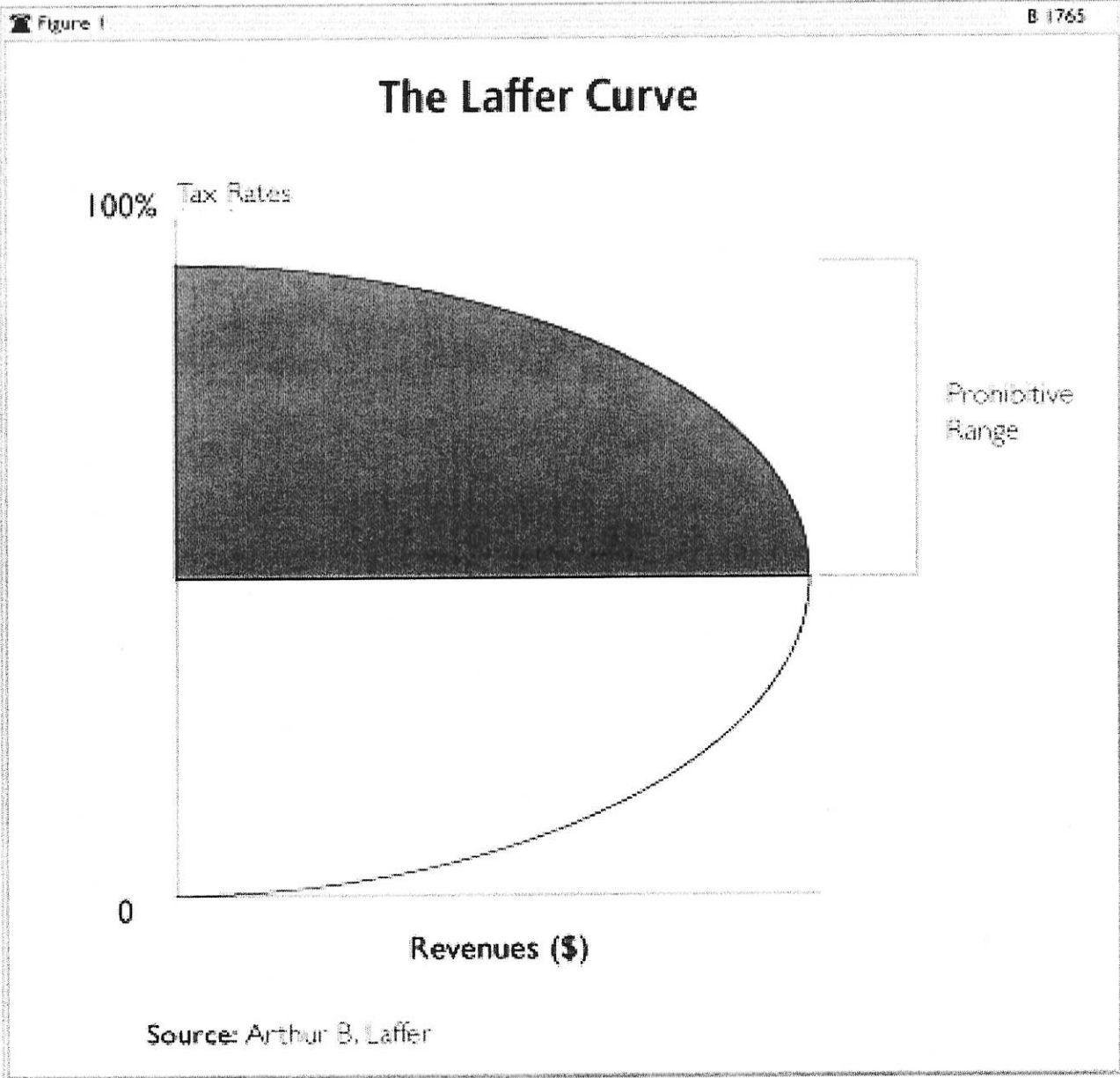
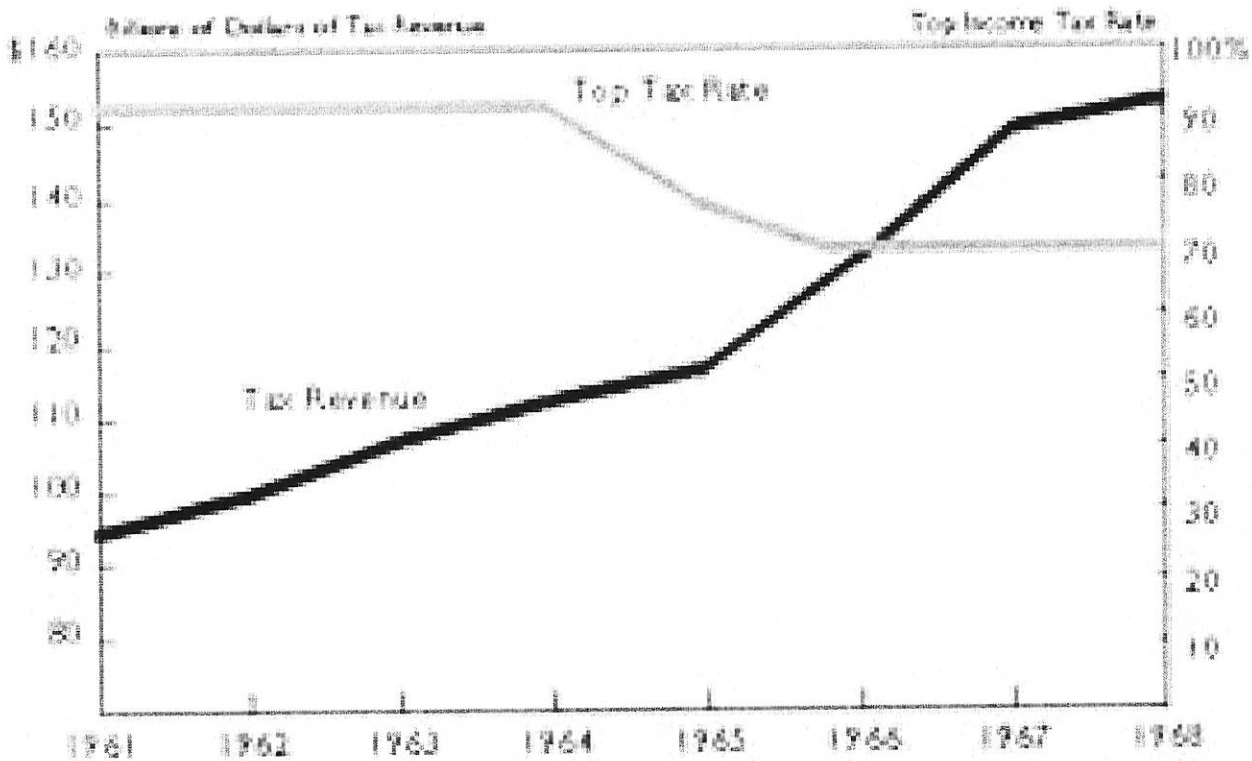


Chart 6

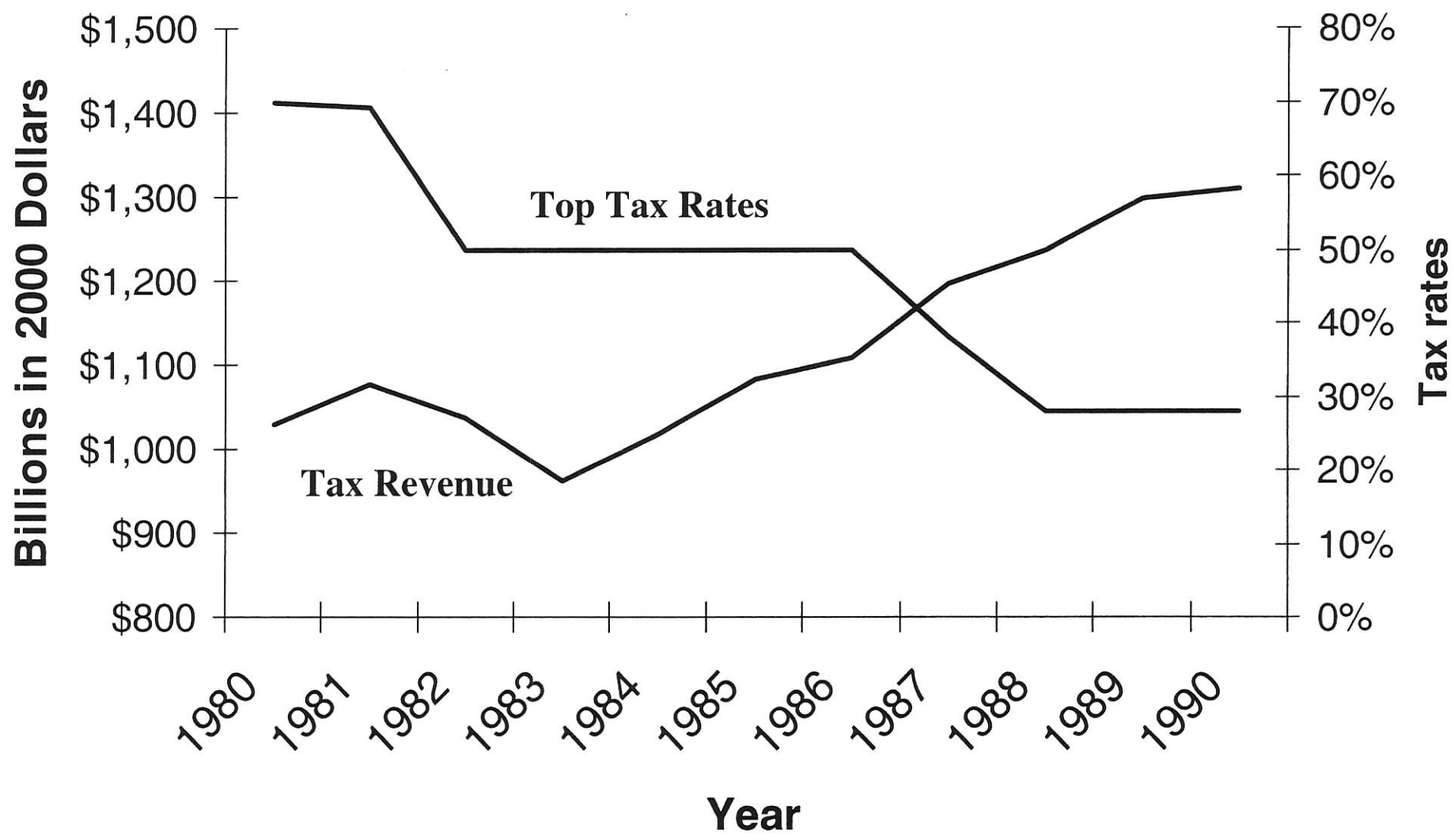


### Kennedy Tax Cuts Boosted Revenue



Sources: Tax Foundation; Budget of the U.S. Government, FY 1997; Office of Management and Budget.

# Reagan's Tax Cuts Increased Revenue





# Who Should Pay?

- Move cost away from taxpayer.
- User pays.
- Is this a fair and reasonable charge against the taxpayer?
- Is this a cost of consumption?
- Is this a cost of doing business?

# Examples

- Transportation
- Tobacco
- Alcohol
- Services
- Farm advisory services
- Applied Research
- DMV

# Does the Government Need to Own?

- Ownership
- Owning assets versus “acquiring capability.”
- Leasing: uses someone else’s capital.
- Purchasing services: e.g. hi tech, saves capital, someone else takes the risk.
- Roads: contract financing and construction, gives future benefits now, smoothes cost over time

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## Economic literacy test . . . and advice

By Richard W. Rahn

Published December 12, 2005

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Before members of Congress leave for the Christmas and New Year's holidays, they are to take a test in economic literacy: their vote on extending the tax cuts President Bush proposed and Congress voted for in 2003, including the current maximum 15 percent long-term capital gains tax rate.

The tax cuts worked very well in revitalizing the economy, which has been growing almost 4 percent yearly. Millions of new jobs were created, resulting in nearly full employment. This has been particularly remarkable given the unprecedented economic battering from the hurricanes.

Now, many Democrats and some Republicans want to repeal the tax cuts -- which means increasing tax rates, like "The Grinch that stole Christmas." They argue we must increase tax rates to bring down the deficit. But tax revenues have been growing much faster than the economy (even with the tax rate cuts), and much faster than the Congressional Budget Office forecast. In fact, the deficit has been falling despite the reckless spending by Congress.

To understand the particular foolishness of increasing the capital-gains tax rate, a brief review of its history is in order. (Remember, a capital gain is the difference between the purchase and sales prices of an asset, such as a corporate stock or a home.) For several decades before 1967, the maximum capital-gains rate remained 25 percent. Beginning in the late 1960s, the maximum rate was raised several times until it reached 49 percent in 1976. Because of this very high rate, many people had an effective rate of more than 100 percent because asset purchase prices were not adjusted for inflation. These high tax rates almost killed venture capital in the U.S. and greatly diminished investment, causing fewer new jobs to be created and a fall in economic growth.

In 1978, Congress wisely reduced the maximum capital gains rate to 28 percent. As a result, capital-gains tax revenues rose (almost 40 percent) rather than declining as the CBO forecast.

In 1981, Congress again cut the capital gains tax rate to a maximum 20 percent. This time, capital-gains revenues again soared by more than 100 percent, despite contrary CBO forecasts. In 1987, Congress foolishly raised the maximum capital-gains tax rate to 28 percent and capital-gains tax receipts fell, despite CBO forecasts they would increase. (The CBO forecast of capital-gains realizations was off by more than 100 percent for the 1987-1993 period.)

Realizing its mistake, Congress cut the capital-gains tax rate to 21 percent in 1996, and again capital-gains tax revenue soared by an average of more than 100 percent as contrasted with the period of the 28 percent rate (and surprise, surprise -- again the CBO had it all wrong).

In 2003, Congress cut the maximum capital gains rate to 15 percent at the urging of President Bush. The final capital-gains receipt numbers for 2004 and 2005 will not be in for some time, but given the surge in tax revenue (and real estate and stock prices), it is a very safe bet capital-gains tax receipts will again be up despite the lower rate. (We also know from the 2003 realization data that the CBO was wrong again.)

If it seems counterintuitive that lower rates lead to higher revenues and vice versa, remember that capital gains taxes are somewhat voluntary. If the rate is seen as too high, people will neither sell nor invest in productive assets.

People have a choice with their savings; they can put them into savings accounts or even tax-free municipal bonds -- they need not put them into assets subject to the capital-gains tax. And if tax rates are perceived as too high on all savings, people can just spend their money.

In sum, we know every time capital gains rates fell in the last 30 years revenues went up and vice versa.

Members of Congress have a choice. They can vote for a higher capital-gains tax rate based on the projections of a CBO model that has been wrong for 27 consecutive years (both in magnitude and direction), or they can vote to continue the lower rate supported by the data and recommendations of economists (including a number of Nobel Prize-winners) who have been right in their projections over the decades.

Those members of Congress who vote for a higher capital-gains tax rate will prove to their constituents that they are dim or mean-spirited or both. And you can bet many representatives will do so, thus failing the test in economic literacy.

*Richard W. Rahn is director general of the Center for Global Economic Growth, a project of the FreedomWorks Foundation.*

# Consumption Tax Decision Hierarchy

The following is a simplification of a process used by the New Zealand government when it was considering the introduction of a “value added tax” and how to structure it. The framework is a valuable tool for legislators because it clarifies the often conflicting claims for one approach as opposed to another.

## **1) What is the purpose of the tax?**

Option 1: Solely to raise revenue and spread the tax base.

Option 2: To change incentives (e.g., luxury taxes, to exempt education, to reduce gasoline consumption, etc.).

*Questions to consider:*

*Will this tax system provide superior incentives to other tax systems?*

*Will providing incentives through this tax system accomplish goals more effectively than alternative government policies?*

*Is the desire for special rates or exemptions a sign that this tax system creates undesirable incentives across the board?*

Option 3: To accomplish social goals (e.g., lower burden on certain groups, redistribute income).

*Questions to consider:*

*Will this tax system accomplish social goals more effectively than other tax systems?*

*Will this tax system accomplish social goals more effectively than alternative government policies?*

## **2) How will the tax be structured to accomplish social goals?**

Option 1: Rebates to favored groups.

Option 2: Point of sale exemptions or discounts to favored groups.

*Questions to consider:*

*How will each option affect administrative costs, transparency, and potential for fraud?*

*How will the public perceive the fairness of each option?*

### **3) How much revenue is to be raised?**

*Questions to consider:*

*Is this tax capable of delivering the desired quantity of revenue?*

*How large are the collection/enforcement costs to deliver the desired revenue?*

*How large are the economic disincentives at this level of revenue?*

### **4) Will it be single or multiple rates?**

Option 1: Single rates

*Advantages to consider:*

- *Low cost of compliance*
- *Simplicity for the taxpayer*
- *Ease of enforcement*
- *No border disputes*
- *Perception of fairness*

*Disadvantages to consider:*

- *Taxes everyone the same rate*
- *Taxes all consumption the same*
- *Perception of unfairness*

Option 2: Multiple rates

*Advantages to consider:*

- *Taxes certain consumption more than others*
- *Perception of fairness*
- *Higher revenues in certain circumstances*
- *Minimal economic distortion in certain circumstances*

*Disadvantages to consider:*

- *Higher cost of compliance*
- *Complexity requires invasive audits*
- *May raise less revenue*
- *May create significant distortions*
- *Significant border disputes*
- *Significant public confusion/anger*

Option 3: Exemptions (Zero rate for some items)

*Advantages to consider:*

- *Encourages the zero rated activity (exports, education, health, charity)*

*Disadvantages to consider:*

- *Cost of compliance*
- *Difficult border definition*
- *Complex rules, difficult policing*
- *Forces rates up on other consumption*

## **5) What will the rate(s) be?**

*Questions to consider:*

*At what point do revenues fall because people curtail consumption?*

*At what point does the tax have destructive economic effects?*

*At what point does consumption move offshore?*

*At what point does the tax generate significant outright cheating?*

*How do enforcement costs change as the tax rates change?*

## **6) What type of collection system will be used?**

Option 1: Point of consumption collection.

Option 2: Collection on non-saved income.

*Questions to consider in choosing the collection option:*

- *Ease of cost/collection*
- *Risk of theft/fraud*
- *Transparency/visibility of tax to voters*
- *Perceived fairness*

## **7) How acceptable will the tax be to the public?**

*Questions to consider:*

*Will the tax lose elections?*

*Will the public accept the tax once passed or will there be continual pressures for change?*

*Will both political parties buy into the tax or will it be subject to change as*



*control of the legislature changes?*

*What changes would be required to get political acceptance?*