Approved: March 8, 2007
Date

MINUTES OF THE SENATE ASSESSMENT AND TAXATION COMMITTEE

The meeting was called to order by Chairman Barbara Allen at 10:30 A.M. on March 6, 2007, in Room 519-S of the Capitol.

All members were present except:
Terry Bruce- excused

Committee staff present:
Chris Courtwright, Kansas Legislative Research Department
Martha Dorsey, Kansas Legislative Research Department
Gordon Self, Office of Revisor of Statutes
Judy Swanson, Committee Assistant

Conferees appearing before the committee:
Joan Wagnon, KDOR
April Holman, Kansas Action for Children
Don Moler, League of Municipalities
mark Desett, KNEA
Aaron Catlin, Kansas Livestock Association
Mark Tallman, KASB

Others attending:
See attached list.

Hearing on confirmation of appointment of Bruce Larkin to State Board of Tax Appeals was opened with Mr. Larkin making a brief statement concerning his qualifications. He introduced his wife, Judy Larkin, and said he served as a State Representative for 19 years. He was a member of the House Tax Committee for 13 years, and has been employed by Kansas Department of Revenue for the past 14 months.

Joan Wagnon, Secretary of KDOR, said she would like to give reference to Mr. Larkin as her good friend, her former colleague and her current employee. He is a person of great character and good judgement. He has shown excellent judgement working with the tax appeals process.

Bill Reardon, former State Representative, gave Mr. Larkin a reference for his appointment to BOTA. (Attachment 1) He said Mr. Larkin was a person of high integrity, and one of the most knowledgeable legislators on tax issues he served with during his time in the legislature.

Senator Goodwin said Mr. Larkin was one of the fairest and highest quality people she knew, and he had every qualification necessary for this appointment.

Senator Lee moved to confirm the appointment of Bruce Larkin to the State Board of Tax Appeals. Senator Goodwin seconded the motion, and the motion carried.

Hearing on SB 305–Establishing the tax modernization commission

Joan Wagnon, Secretary of KDOR, testified in support of **SB 305**. (Attachment 2) Studies show trends point to the narrowing of the tax base in Kansas. Secretary Wagnon suggested members of the Tax Modernization Commission should represent a diverse group of Kansas citizens from a variety of geographical areas, vocations and perspectives. She further suggested the Governor appoint the chair and the vice-chair of the commission. The important thing is to get the Commission started.

April Holman, Kansas Action for Children, testified there are three key principles of good tax policy: diversity, sufficiency and equity. (Attachment 3) Currently there are 72 sales tax exemptions in Kansas. The current strong economy will not last forever, and further erosion of the tax base is inevitable. The poorest Kansans pay 32.7% of their income in taxes as opposed to the wealthiest Kansans, who pay a rate equal to 7.7% of their income. A comprehensive modernization of the Kansas tax system is long overdue.

Ms. Holman said the study should also include local units of government. She is not convinced dynamic

MINUTES OF THE Senate Assessment and Taxation Committee at 10:30 A.M. on in Room 519-S of the Capitol.

scoring would be realistic. Senator Jordan said it is a mistake to only look at tax credits, without also looking at the return from granting tax credits. Ms. Holman said she had a problem with finding a means to accomplish unskewed information concerning tax credits vs. tax benefits.

Don Moler, Kansas League of Municipalities, testified all taxes should be examined, and a conclusion drawn from the information found. (Attachment 4)

Mark Desetti, KNEA, said KNEA supports a comprehensive examination of the entire tax system in Kansas. (Attachment 5) The Kansas tax system has lost vertical equity. There is a lack of progressivity in the system. He said a tax system can have vertical equity and be progressive. Mr. Desetti shared statistical information from the Institute on Taxation and Economic Policy (ITEP).

Aaron Catlin, Kansas Livestock Association, testified KLA is supportive of **SB 305**. (Attachment 6) Kansas' geographical location and topography make it ideal for agricultural production, but it is difficult to attract additional industries necessary to diversify and protect the tax base. Population shifts from rural to urban areas have taken a toll on many rural communities and counties. One member of the Commission should be from the agriculture production community.

Mark Tallman, KASB, said KASB members are concerned over recent trends in tax and funding policies, particularly in the area of school finance. (Attachment 7) The shift to property and sales tax to fund schools and other public programs has made the tax system more regressive. Left unchecked, the trend will erode the tax base; then eventually erode the quality of public services. Only a high-level independent review of the entire tax system can lead to a comprehensive solution.

During committee discussion, Senator Schmidt expressed surprise KLA would want a tax commission to take a closer look at closing some of the loopholes which currently exist for agriculture production. Senator Donovan said the percentages in the ITEP study quoted by Mr. Desetti could not be correct. Senator Jordan said Kansas is more reliant on property tax, but Mr. Tallman's remarks show since '89 the amount has gone down. Mr. Tallman said his remarks were made from Kansas Tax Facts booklet, not from the ITEP study. The hearing on **SB 305** was closed.

Chairman Allen requested April Holman prepare balloon amendments for **SB 305** for further Committee consideration.

Senator Goodwin moved to approve the February 28 and March 1 Committee minutes. Senator Apple seconded the motion, and the motion carried.

Being no further business, the meeting adjourned at 11:35 AM. The next meeting will be March 7.

SENATE
ASSESSMENT & TAXATION COMMITTEE

GUEST LIST

DATE: 3-6-07

NAME	REPRESENTING
David R. Corbin	KDOR
Richard Cram	"
Don Moler	LKM
Ben Cleeves	DOB
Joshua Lewis	Sen. Schmidt
Trevor Wohlford	BOTA
[illegible]	BOTA
[illegible]	KDOR
[illegible]	KDOR
Trisha Schmuck	KDOR
[illegible]	BOTA
Joan Wagnon	KDOR
Dan Murray	Federico Consulting
Ted Warner	KS Govt Consulting
Shawnel Stepp	KDOR
Becky Hastings	KDOR
Marketa Walden	KDOR
MIKE TAYLOR	UNIFIED GOVERNMENT/KCK

SENATE
ASSESSMENT & TAXATION COMMITTEE

GUEST LIST

DATE: 3-6-07

NAME	REPRESENTING
[illegible]	LGR
Marlee Carpenter	KS Chamber
ROBYN HORTON	KS MOTOR CARRIERS ASSOC.
Ashley Sherard	Lenexa Chamber of Commerce
Caleb Hensl	Arkansas City HS - Page for Greta Goodwin
Mark Desetti	KNEA
April Holman	Kansas Action for Children
Mark Tallman	KASB
Tony A. Scott	KSCPA
BRANDON BOHNING	WHITNEY DAMRON P.A.
Emily Geier	Hein Law Firm, Chartered
Aaron Cathin	KS Livestock Assoc.

Testimony Before Senate Tax Committee
Bruce Larkin Confirmation Hearing
Bill Reardon
March 6, 2007

Madam Chair and Members of the Senate Tax Committee:

Since I retired from the Kansas House in 2004, I have worked as a lobbyist for the Kansas City Public School District. I wanted to clarify that today, I am representing myself, not my school district.

I have known Bruce Larkin since he was first elected to the House in 1986. While we are both members of the same political party, our legislative districts could not have been more disparate. I represented an urban core district and Bruce represented, arguably, the most rural district in the Kansas House. Despite our different backgrounds, I grew to genuinely like and deeply respect Bruce.

I would like to briefly touch upon a couple reasons why I believe Bruce Larkin is an ideal choice to serve on the Kansas Board of Tax Appeals.

First, Bruce was one of the most knowledgeable legislators on tax issues that I served with during my three decades in the House. During my tenure, Bruce Larkin, Joan Wagnon and former Speaker Jim Braden were the three legislators whose knowledge and expertise on tax issues I most respected.

Second, and equally important, Bruce Larkin's integrity as a legislator and as a person was respected by many, many colleagues on both sides of the isle and by both Democrat and Republican Governors, as well as past and present Secretaries of Revenue. Bruce Larkin is a man of conviction and yet he is open to view points that conflict with his own. I strongly believe that personal integrity is the single most important character trait for anyone serving on a quasi-judicial body such as the Board of Tax Appeals.

I have know Bruce Larkin for over 20 years and I am convinced that he possesses the knowledge, expertise and personal character to serve with distinction as a member or the Kansas State Board of Tax Appeals.

K A N S A S

JOAN WAGNON, SECRETARY

DEPARTMENT OF REVENUE
OFFICE OF THE SECRETARY

KATHLEEN SEBELIUS, GOVERNOR

March 6, 2007
Testimony on S305
Tax Modernization Commission

I appear in support of S305 today. I have often suggested, most recently in the 2006 Interim Taxation committees, that we need to modernize our tax systems. Studies which have been completed recently under the auspices of the Kansas Advisory Council on Intergovernmental Relations and the Department of Revenue have pointed out the potentially devastating trends in tax policy in recent years. Those trends point to the narrowing of the tax base, the accelerating use of exemptions and credits which contribute to that base erosion, and the changes in the economy which make provisions in our tax code outmoded and outdated. I have previously presented some of those studies to this committee and to the Interim committees.

The two major initiatives of this administration with regard to improving the business tax climate have resulted from consultation with citizen and business groups across the state. There is value in "taking a step back" occasionally, and thoughtfully and completely examining the tax climate in a state, and recommending changes. The most complete and far reaching such examination was in the 1970's when the Hodge Commission promulgated sweeping changes which the legislature enacted. It has taken nearly 35 years to undo some of their fine work.

The 1995 Tax Equity Task Force, created by Executive Order of Governor Graves, produced scholarly work and useful ideas, but failed to produce a legislative champion to see their ideas and strategies enacted into law. I have personally referred to that work when looking for information, or ways to solve problems. This report provided impetus for the removal of the business and machinery tax, along with a study group of business executives the department assembled to advise it on tax policy.

DOCKING STATE OFFICE BUILDING, 915 SW HARRISON ST., TOPEKA, KS 66612-1588
Voice 785-296-3041 Fax 785-296-7928 http://www.ksrevenue.org/

I do have a suggestion for the way in which the commission is created. Rather than the 9 members appointed by the Governor coming from such designated areas, as seen on lines 19-30, I would recommend you use the following language instead:

Nine members shall be appointed by the Governor to represent a diverse group of Kansas citizens from a variety of geographical areas, vocations, and perspectives, including those of private citizens of all ages, business people, property owners, finance professionals, educators and local governments.

Further, it is not clear if the appointees of the House and Senate leadership (lines 32-40) can be private citizens or legislators. Perhaps you should consider making this clear if the intent is to have 10 legislators (including the House and Senate tax committee chairs) plus 9 citizens and the Secretary of Revenue.

I would further suggest that the Governor appoint the chair and vice-chair of the commission in order to be able to recruit leadership willing to serve and commit the time. I have seen commissions formed with no appointed leaders, and they don't necessarily select the best leaders from among their membership when they don't know each other.

While there are many ways to organize and construct such a commission, the important thing seems to be first, to get it started, and second, with the right people and sufficient resources for it to work effectively, and finally, with some commitment to following through on the recommendations if they are worthy.

Joan Wagnon

Assessment & Taxation
Date 3-6-07
Attachment # 2-2

FISCAL FOCUS

Budget and Tax Policy in Perspective

April Holman
Legislative Testimony
Senate Bill 305
Senate Committee on Assessment and Taxation
March 6, 2007

Good morning Madam Chair and members of the Committee. On behalf of Kansas Action for Children (KAC), I would like to thank you for this opportunity to testify in favor of Senate Bill 305.

KAC is a not-for-profit child advocacy organization that has been in existence since 1979. KAC promotes policies that aid family economic stability because instability creates stress and the potential for harm to children through less consistent medical care, fewer opportunities for early learning and the potential for lower performance in school.

We have stood before the committee several times this session testifying in opposition to bills that would further erode the Kansas tax base. We believe that Senate Bill 305 is a better way to address the issues that we all know exist with the Kansas tax structure.

Key Principles of Good Tax Policy

We think of good tax policy is in terms of three key principles: diversity, sufficiency and equity. ***Diversity*** of revenue sources is important to protect against economic downturns in certain areas of the economy and to ensure that no single group of taxpayers is responsible for paying the majority of taxes. ***Sufficiency*** of revenues is vital for funding of government and the services it provides and ***equity*** ensures the integrity of the system and its long-term viability.

Pragmatic Policy and the Erosion of the Tax Base

Tax policy in Kansas has developed in a series of policy decisions designed to address issues arising for various groups at various times. This has been done with the best of intentions and in a very pragmatic way. However, the result over time has been a narrowing of the tax base and unintended consequences threatening the principles of good tax policy.

In 2004, Kansas Action for Children published a report entitled, "Erosion of the Kansas Tax Base." At that time we noted that the number of exemptions to the Kansas sales tax increased from 36 to over 60 during the previous decade. Currently there are 72 sales tax exemptions with over a dozen more making their way through the legislative process this year.

720 SW Jackson, Suite 201 Topeka, KS 66603 • Telephone: (785)232-0550 •Fax: (785)232-0699 • kac@kac.org • www.kac.org

Assessment & Taxation
Date 3-6-07
Attachment # 3

Although the number of income tax credits is not as large as the number of sales tax exemptions, the trend in this area is the same. In 1994 there were 9 income tax credits in Kansas law. Today there are 29 credits available. In addition to this the income tax rate structure has changed to equalize the rates for married and single taxpayers and standard deduction and personal exemption amounts have also been increased.

While the dollar impact of the tax breaks vary, the cumulative effect is significant. The Department of Revenue estimates that tax reductions enacted since 1995 totaled about $920 million in FY 2005, with a cumulative total of about $6.7 billion since 1995.

The state may be able to sustain lost revenues due to tax further erosion of the tax base this year. However, the current strong economy will not last forever. When the Kansas economy reaches the next downturn this source of revenue will no longer be available to the state. As recently as the late 1990's a similar erosion of the Kansas tax base took place during times of a strong economy only to result in revenue shortfalls in the early 2000's when the economy slowed down. At that time policymakers responded to revenue shortfalls by increasing sales tax, cigarette tax and franchise tax rates for those taxpayers not fortunate enough to have an exemption.

Erosion of the tax base threatens all three of the key principles of good tax policy. Diversity is an issue because the weakening of the income tax has resulted in more reliance on sales and property tax revenues. Sufficiency of revenues is a significant issue, especially in light of increasing funding commitments in the areas of education and Medicaid and the knowledge that our current strong economy can't last forever. Finally, a tax incidence analysis published by the Kansas Department of Revenue and the Kansas Public Finance Center of the Hugo Wall School of Urban and Public Affairs at Wichita State University last year emphasized inequities in the Kansas tax system, noting that the poorest Kansans pay a combined (sales, income, and property) effective tax rate equal to 32.7% of their income as opposed to the wealthiest Kansans who pay a combined effective tax rate equal to 7.7% of their income.

Senate Bill 305

It is our belief that a comprehensive modernization of the Kansas tax system is long overdue. Recent reports from the Kansas Department of Revenue show that Kansas taxes disproportionately impact the poor and that both the sales tax and property tax bases have been eroded significantly in recent years. This has resulted in tax shifts as well as revenue shortfalls and the need in some years to increase tax rates. In order to address these issues as well as the changing nature of the Kansas economy a comprehensive plan should be created for modernizing Kansas taxes. If we can update and improve the efficiency of our tax system, the need for exemptions will not longer be an issue. For this reason we respectfully request your support of Senate Bill 305.

LKM
League of Kansas Municipalities

300 SW 8th . .ue
Topeka, Kansas 66603-3912
Phone: (785) 354-9565
Fax: (785) 354-4186

To: Senate Assessment and Taxation Committee

From: Don Moler, Executive Director

Re: Support for SB 305

Date: March 6, 2007

First, I would like to thank the Committee for allowing the League to testify concerning this very important matter. For a number of years the League has been concerned about the funding of Kansas Local Governments in the 21st Century. With an ever increasing dependence of local government revenue sources on the local property tax and the local sales tax, we believe the time has come for a comprehensive review of the tax structure of the State of Kansas.

Historically, there has been a three-legged stool upon which local services have been financed, with the three legs of the stool being: the local property tax; the local sales tax; and the state-provided demand transfers. The demand transfers stopped being provided approximately four years ago, although we are hopeful that we will see their return in the very near future. Without the demand transfers, city and county operations have become increasingly dependent upon the local property tax and the local sales tax. This has the effect of making the reliance on these two taxes evermore difficult, and puts local government finances in a precarious position. As a result it also puts an ever increasing strain upon the local property tax base and our local property taxpayers.

For these reasons we fully support the creation of the tax modernization commission, and would urge the adoption of SB 305 by the Committee. Thank you for allowing the League to testify today. We would be more than happy to answer any questions you may have.

Assessment & Taxation
Date 3-6-07
Attachment # 4

KANSAS NATIONAL EDUCATION ASSOCIATION / 715 SW 10TH AVENUE / TOPEKA, KANSAS 66612-1686

Mark Desetti, Written Testimony
Senate Assessment and Taxation Committee
March 6, 2007

Senate Bill 305

Madame Chair, members of the committee, thank you for the opportunity to provide testimony today on Senate Bill 305, a proposal to create a Tax Modernization Commission.

I have been before this Committee and the House Taxation Committee this year on a variety of bills and every time I ended my testimony the same way. We at KNEA believe that the legislature should make a comprehensive examination of the entire tax system to ensure that our many provisions result in a system that will provide stable funding for all state services and that is fair to both citizens and business.

Senate Bill 305, we believe, does just that.

One of the reasons we think the Legislature should take a step back and examine the system is the impact that the current way of enacting tax policy has had on Kansans.

Our system of taxes should be based on a stable three-legged stool with one leg being property tax, another being sales tax, and the third being income tax. We also believe that the tax system should be elastic in providing for stability over good and bad economic times and that it should have both vertical and horizontal equity.

I would like to focus the rest of my comments on vertical equity.

Evidence shows that the Kansas tax system has lost vertical equity. Today low income Kansans pay a considerably higher percentage of their income in taxes than do wealthy Kansans. There is a lack of progressivity in our system.

What evidence do we have of a lack of vertical equity or progressivity in the Kansas tax system? I went to two sources that have analyzed the Kansas system for help. The first is the Hugo Wall School of Urban and Public Affairs at Wichita State University. In a tax incidence review study authored by John D. Wong and published in March of 2006, Wong came to this conclusion in examining the effective tax rate (ETR) paid by households within income groupings:

> Out of the ten income groupings, the highest effective tax rate paid is by households that earn less than $10,000 (32.7 percent), while the lowest effective rate paid is for households with $200,000 or more of income (7.7 percent). Again, it should be kept in

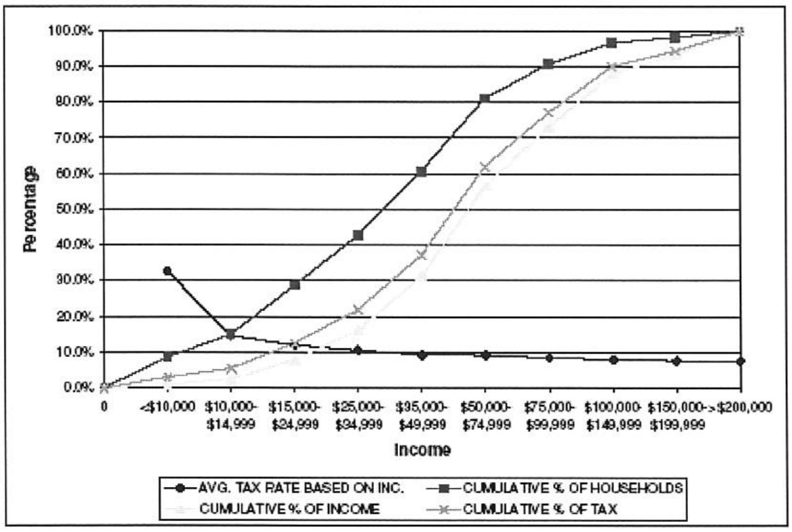
Assessment & Taxation
Date 3-6-07
Attachment # 5

Telephone: (785) 232-8271 FAX: (785) 232-6012 Web Page: www.knea.org

mind that the ETRs are computed as a percentage of Kansas adjusted gross income. The average effective tax rate for the state as a whole is 9.2 percent.[1]

Exhibit 62: Combined Tax Incidence by Income Class

2003 TOTAL TAXES KANSAS	<$10,000	$10,000-$14,999	$15,000-$24,999	$25,000-$34,999	$35,000-$49,999	$50,000-$74,999	$75,000-$99,999	$100,000-$149,999	$150,000-$199,999	>$200,000	Total
AVG. TAX RATE BASED ON INC.	32.7%	14.6%	12.0%	10.5%	9.3%	9.1%	8.4%	8.0%	7.6%	7.7%	9.2%
CUMULATIVE % OF HOUSEHOLDS	8.6%	14.9%	28.7%	42.7%	60.8%	81.1%	90.7%	96.8%	98.3%	100.0%	
CUMULATIVE % OF INCOME	0.8%	2.4%	7.9%	16.2%	31.4%	56.4%	73.1%	88.0%	93.4%	100.0%	
CUMULATIVE % OF TAX	3.0%	5.5%	12.6%	22.0%	37.3%	62.1%	77.2%	90.1%	94.5%	100.0%	
KAKWANI INDEX	(0.0009)	(0.0017)	(0.0053)	(0.0074)	(0.0107)	(0.0118)	(0.0047)	(0.0019)	(0.0002)	(0.0001)	(0.0892)
SUITS INDEX	(0.0001)	(0.0004)	(0.0021)	(0.0044)	(0.0089)	(0.0145)	(0.0081)	(0.0046)	(0.0009)	(0.0004)	(0.0888)



Tax policy in Kansas clearly makes the poor even more so. You will note on the graph provided in Wong's exhibit 62 (above)[2], as Kansans increase in income, the percentage of income paid in taxes steadily declines after a sharp change from those earning below $10,000/year to those earning between $10,000 and $14,999/year.

As a comparison, Wong provides findings from the 2005 Minnesota Tax Incidence Study and the 2001 Oregon Tax Incidence Study. These studies both found tax systems that had vertical equity. In Minnesota, the effective tax rate ranged from 10.2% on the lowest income group to 9.1% on the highest income group. In Oregon, the system was progressive with low income tax payers paying an ETR of 5.9% and high income taxpayers paying an ETR of 8.9%.[3]

Clearly a tax system can have vertical equity and can be progressive.

I have attached to my testimony pages 69 and 70 of the Kansas Tax Incidence Study for your review.

---

[1] Wong, John D., Kansas Tax Incidence Study: Who Pays Kansas Individual Income, Residential Property, and Retail Sales Taxes, Kansas Public Finance Center, Hugo Wall School of Urban and Public Affairs, Wichita State University, March, 2006, p 69.

[2] Ibid., p 70.

[3] Ibid., p 69.

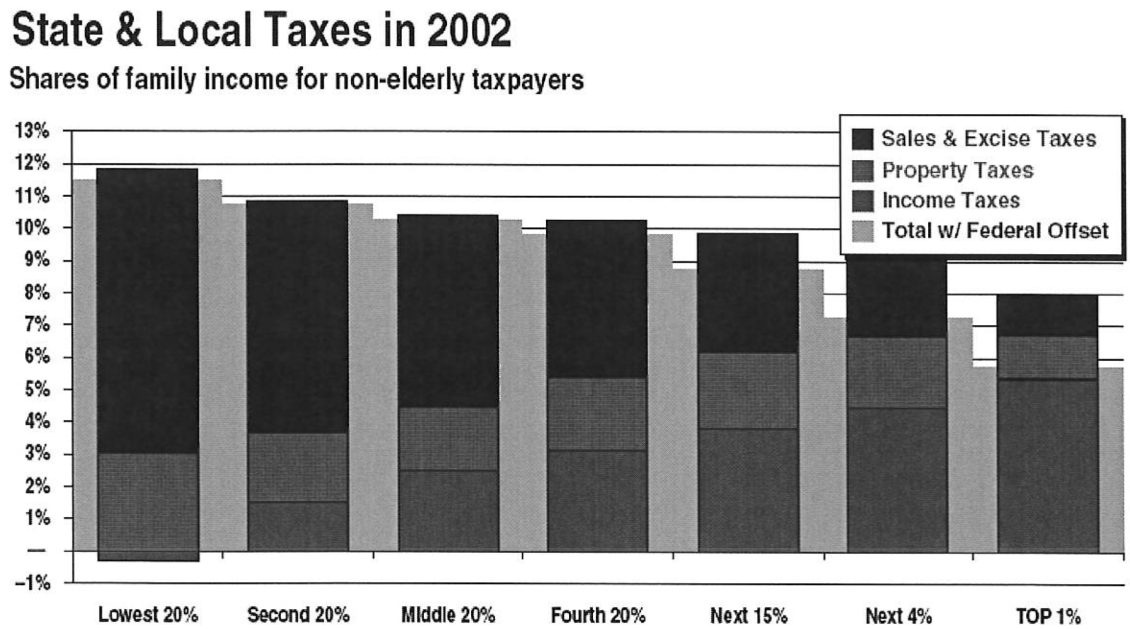
Assessment & Taxation
Date 3-6-07
Attachment # 5-2

The second source I examined is the 2003 publication Who Pays? A Distributional Analysis of the Tax Systems in All 50 States from the Institute on Taxation and Economic Policy.
The ITEP study came to two fundamental conclusions. First, that the tax system in Kansas lacks vertical equity – low income Kansans pay a greater percentage of their income in taxes than upper income Kansans. Secondly, they found that between 1989 and 2003, the system had become worse for low income earners.

On the issue of vertical equity, ITEP found that:

- The state and local tax rate on the best off one percent of Kansas families – with average incomes of $781,000 – is 8.0% before accounting for the tax savings from federal itemized deductions. After the federal offset, the effective tax rate is only 5.7%.
- The average tax rate on families in the middle of the income distribution – those earning between $27,000 and $44,000 – is 10.4% before the federal offset and about the same after, nearly double the effective rate on the best-off one percent.
- But the tax rate on the poorest Kansas families – those earning less than $14,000 – is the highest of all. At 11.5% it is more than double the effective rate on the very wealthy.[4]

The graph below represents the effective tax rate by income level as found by ITEP.[5]



When examining the changes in the tax system between 1989 and 2003, the ITEP report found that, for Kansas citizens, "effective tax burdens rose across the board, but they increased far more heavily on the low- and middle-incomes than on those with the highest incomes."[6] In addition, "substantial increases in the state and local sales taxes and rises in excise taxes drove up tax burdens on the poor and middle class."[7]

---

[4] ITEP press release, Kansas Taxes Hit Poor & Middle Class Much Harder than the Wealthy, January 7, 2003, p 1.
[5] McIntyre, Robert S., et al, Who Pays? A Distributional Analysis of the Tax Systems in All 50 States, The Institute on Taxation and Economic Policy, January 2003, p 49.
[6] ITEP press release, Kansas Taxes Hit Poor & Middle Class Much Harder than the Wealthy, January 7, 2003, p 2.
[7] Ibid.

Assessment & Taxation
Date 3-6-07
Attachment # 5-3

The ITEP study demonstrates how the increase in the tax burden between 1989 and 2003 was distributed by income groups. What ITEP found was that low and middle income Kansans were hurt the most by tax policies adopted in that period notwithstanding some measures that were adopted to make the system more progressive – the adoption of the food sales tax credit and the scaling back of the car tax. The lowest 20% of earners saw their tax burden increase by 2%. Middle income Kansans saw their burden increase from 1.6 to 1.8% while the top 1% of Kansas earners saw a modest increase of 0.5% in tax burden.[8]

As to whether or not the ITEP model can appropriately measure tax data, John D. Wong of the Hugo Wall School of Urban and Public Affairs at Wichita State University noted, "The ITEP model uses one of the largest databases of tax returns and supplementary data in existence, with nearly three quarters of a million records. The ITEP model's approach is very similar to that used by the congressional Joint Committee on Taxation, the U.S. Treasury Department and the Congressional Budget Office."[9]

We do believe there is a growing problem with the Kansas tax system. The manner in which tax policy is made – considering increases and cuts as independent issues with little regard for their impact on the state revenue stream and the future ability of the state to meet the needs of citizens – is moving our system away from balance, progressivity, and elasticity and feeding mini tax revolts.

Recently you were told about the experience of New Zealand in which law makers widened the base in order to reduce the burden. The Commission proposed in Senate Bill 305 can take the time to examine all tax issues including the appropriate tax base, the level of the tax burden across the income spectrum, the fairness of the system to individuals and to business, and the ability of the system to supply a revenue stream that will maintain the high quality public services – state infrastructure, public safety, education, and care for our most vulnerable citizens – that Kansans have come to appreciate.

An editorial in the Hutchinson News made this point quite well in yesterday's edition:

> "All of the various tax cut ideas that crop up whenever the state's fiscal affairs look favorable represent a wrong approach. It seems to be a random process when instead discussion of tax cuts should take place in the context of a holistic evaluation of the state's tax structure, including income, sales and property taxes on both individuals and businesses."[10]

The Hutchinson News editorial concluded, "Legislators probably would be prudent to hold off on most of these significant tax cuts for a year and use that time to examine the big picture and consider all the options for reducing taxes."[11] We couldn't agree more.

We urge this Committee to pass Senate Bill 305 and create a sensible and fair tax system for Kansas.

---

[8] McIntyre, Robert S., et al, Who Pays? A Distributional Analysis of the Tax Systems in All 50 States, The Institute on Taxation and Economic Policy, January 2003, p 49.
[9] Wong, John D., Kansas Tax Incidence Study: Who Pays Kansas Individual Income, Residential Property, and Retail Sales Taxes, Kansas Public Finance Center, Hugo Wall School of Urban and Public Affairs, Wichita State University, March, 2006, p 17.
[10] Hutchinson News Editorial, Kansas Tax Cuts, March 5, 2007.
[11] Ibid.

Income

Exhibit 61 shows average effective retail sales tax rates by income quintile for 2003. The third income quintile (3.90 percent) had the highest effective retail sales tax rate, followed by the fourth quintile (3.79 percent), the first quintile (3.72 percent), the second quintile (3.65 percent), and the fifth quintile (2.74 percent). This indicates that taxpayers in moderate income counties paid a higher percentage of their income in sales tax, than did taxpayers in higher income or lower income counties.

Exhibit 61: Retail Sales Tax Incidence by Population

Quintile	Percentage	Suits	Kakwani
First	3.72%	(0.1655)	(0.1562)
Second	3.65%	(0.1714)	(0.1635)
Third	3.90%	(0.1818)	(0.1755)
Fourth	3.79%	(0.1742)	(0.1681)
Fifth	2.74%	(0.1661)	(0.1606)
Total	3.73%	(0.1731)	(0.1643)

Exhibit 61 also shows Suits and Kakwani Indices by income quintile for 2003. The first quintile (–0.1655) had the highest Suits Index, followed by the fifth quintile (–0.1661), the second quintile (–0.1714), the fourth quintile (–0.17472), and the third quintile (–0.1818). Similarly, the first quintile (–0.1562) had the highest Kakwani Index, followed by the fifth quintile (–0.1606), the second quintile (–0.1635), the fourth quintile (–0.1681), and the third quintile (–0.1755). Generally, this indicates that the Kansas retail sales tax is less regressively distributed in higher and lower income areas than in moderate income areas.

Incidence of Combined Individual Income, Residential Property, and Retail Sales Taxes

Exhibit 62 presents the distribution of combined Kansas individual income, residential property, and retail sales taxes by income grouping. The first section of the table shows the effective tax rate paid by households within the respective income groupings. Out of the ten income groupings, the highest effective tax rate paid is by households that earn less than $10,000 (32.7 percent), while the lowest effective rate paid is for households with $200,000 or more of income (7.7 percent). Again, it should be kept in mind that the ETRs are computed as a percentage of Kansas adjusted gross income. The average effective tax rate for the state as a whole is 9.2 percent.

As a basis of comparison the *Minnesota Tax Incidence Study* (2005) found an effective average total state and local tax rate on individuals of 8.9 percent, with the lowest income population group ($8,354 and under) paying an effective tax rate of 10.2 percent, while the highest income population group ($102,426 and over) paying an effective tax rate of 9.1 percent. According to the *Oregon Tax Incidence Model* (2001) that state's effective average total state and local tax rate on households was 7.1 percent, ranging from 5.9 percent for households earning between $21,255 and $128,739 to the highest income group (over $126,172) paying an ETR of 8.9 percent. The *Wisconsin Tax Incidence Study* (2004) found that the overall tax structure was moderately progressive to proportional for almost all households. The lowest income group paid 9.6 percent of their income in taxes, while households with income between

Assessment & Taxation
Date 3-6-07
Attachment # 5-5

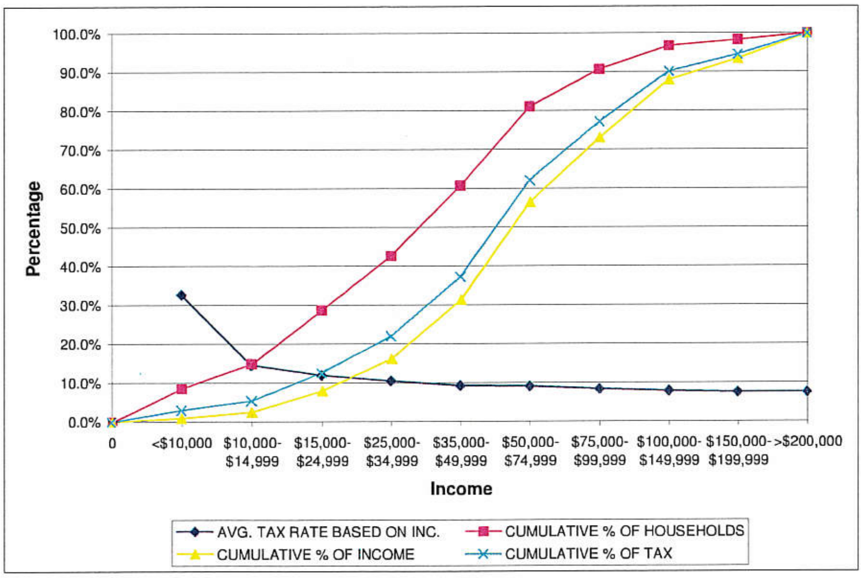
$93,401 and $254,200 paid the highest tax rate of 11.9 percent, but the tax rate for the highest income group declined to 10.9 percent.

The next section of the table shows information used to assess the overall incidence of the combined taxes. The data for this section are derived from the above sections. Both the Suits Index (–0.0888) and the Kakwani Index (–0.0892) indicate total Kansas state and local individual income, residential property, and retail sales taxes are slightly regressive. The Minnesota Tax Incidence Study (2005) reported a Suits Index of –0.018 for total state and local taxes, while the *Wisconsin Tax Incidence Study* (2004) reported a Suits Index of 0.006 and a Kakwani Index of 0.013 for total state and local taxes.

The chart at the bottom of the exhibit shows the relationship among the average effective tax rate, the cumulative percentage of households, the cumulative percentage of income, and the cumulative percentage of tax. Note that there is a comparable table for each of the 105 counties and five county groupings contained in the Detailed Appendix.

Exhibit 62: Combined Tax Incidence by Income Class

2003 TOTAL TAXES KANSAS	<$10,000	$10,000-$14,999	$15,000-$24,999	$25,000-$34,999	$35,000-$49,999	$50,000-$74,999	$75,000-$99,999	$100,000-$149,999	$150,000-$199,999	>$200,000	Total
AVG. TAX RATE BASED ON INC.	32.7%	14.6%	12.0%	10.5%	9.3%	9.1%	8.4%	8.0%	7.6%	7.7%	9.2%
CUMULATIVE % OF HOUSEHOLDS	8.6%	14.9%	28.7%	42.7%	60.8%	81.1%	90.7%	96.8%	98.3%	100.0%	
CUMULATIVE % OF INCOME	0.8%	2.4%	7.9%	16.2%	31.4%	56.4%	73.1%	88.0%	93.4%	100.0%	
CUMULATIVE % OF TAX	3.0%	5.5%	12.6%	22.0%	37.3%	62.1%	77.2%	90.1%	94.5%	100.0%	
KAKWANI INDEX	(0.0009)	(0.0017)	(0.0053)	(0.0074)	(0.0107)	(0.0118)	(0.0047)	(0.0019)	(0.0002)	(0.0001)	(0.0892)
SUITS INDEX	(0.0001)	(0.0004)	(0.0021)	(0.0044)	(0.0089)	(0.0145)	(0.0081)	(0.0046)	(0.0009)	(0.0004)	(0.0888)



County

Exhibit 63 shows combined average effective tax rates by county for 2003. The counties with the highest ETRs are Pratt (11.70 percent), Ellis (11.54 percent), Saline (11.06 percent), Seward (10.92 percent), and Thomas (10.85 percent). The counties

Assessment & Taxation
Date 3-6-07
Attachment # 5-6

ITEP Institute on Taxation and Economic Policy
1311 L Street, NW • Washington, D.C. 20005 • (202) 737-4315

EMBARGOED FOR RELEASE ON
TUESDAY, JANUARY 7, 2003 AT 10:00 AM
CONTACT: Bob McIntyre, 202/737-4315

Kansas Taxes Hit Poor & Middle Class Much Harder than the Wealthy

Low- and middle-income families in Kansas pay a much higher share of their income in state and local taxes than do the richest Kansans, according to a new study by the Institute on Taxation & Economic Policy.

"State and local governments are being called upon to take on more and more responsibilities," said Robert S. McIntyre, ITEP's tax policy director and lead author of the study, titled *Who Pays? A Distributional Analysis of the Tax Systems in All 50 States*. "Unfortunately, when it comes to paying for services, Kansas has an unfair tax system."

Kansas's Tax Code: Tax the Poor & Middle Class More Than the Wealthy

When all Kansas taxes are totaled up, the study found that:

- The state and local tax rate on the best off one percent of Kansas families—with average incomes of $781,000—is 8.0% before accounting for the tax savings from federal itemized deductions. After the federal offset, the effective tax rate is only 5.7%.
- The average tax rate on families in the middle of the income distribution—those earning between $27,000 and $44,000—is 10.4% before the federal offset and about the same after, nearly double the effective rate on the best-off one percent.
- But the tax rate on the poorest Kansas families—those earning less than $14,000—is the highest of all. At 11.5% it is more than double the effective rate on the very wealthy.

"Kansas's income tax fails to offset the regressivity of its sales and excise taxes, giving the state a regressive tax system," McIntyre said. "Taxes ought to be based on people's ability to pay them, which means that the share of income paid in taxes should rise as income grows, not fall as is the case in Kansas."

MORE . . .

Assessment & Taxation
Date 3-6-07
Attachment # 5-7

Tax Regressivity Has Worsened Since 1989

The study also examined the impact of changes in the regressivity of Kansas taxes since 1989, when the last cycle of state government shortfalls began. The study's findings include:

- Effective tax burdens rose across the board, but they increased far more heavily on the low- and middle-incomes than on those with the highest incomes.
- Substantial increases in the state and local sales taxes and rises in excise taxes drove up tax burdens on the poor and middle class.
- The elimination of the deduction for federal income tax paid and higher tax rates overall raised income tax burdens on higher-earning Kansans.

"Low- and moderate-income Kansans were forced to take the money they saved from cuts in income taxes and pay it right back in higher sales and excise taxes," said McIntyre. "As lawmakers consider budget-balancing strategies in 2003, they should remember that their past actions have served to shift a greater share of the tax burden onto low-income taxpayers."

Two pages of tables detailing the Kansas findings of the study follow

The Institute on Taxation and Economic Policy is a nonpartisan Washington-based research group. The full *Who Pays?* report is available in PDF format at www.itepnet.org. Printed copies can be ordered by calling ITEP at 202-737-4315.

Who Pays? examines the tax systems of all 50 states and the District of Columbia, using the Institute on Taxation & Economic Policy Microsimulation Tax Model. The ITEP Model is similar in methodology and data sources to the elaborate computer models used by the U.S. Treasury and the congressional Joint Committee on Taxation, except that the ITEP Model adds state-by-state estimating capabilities.

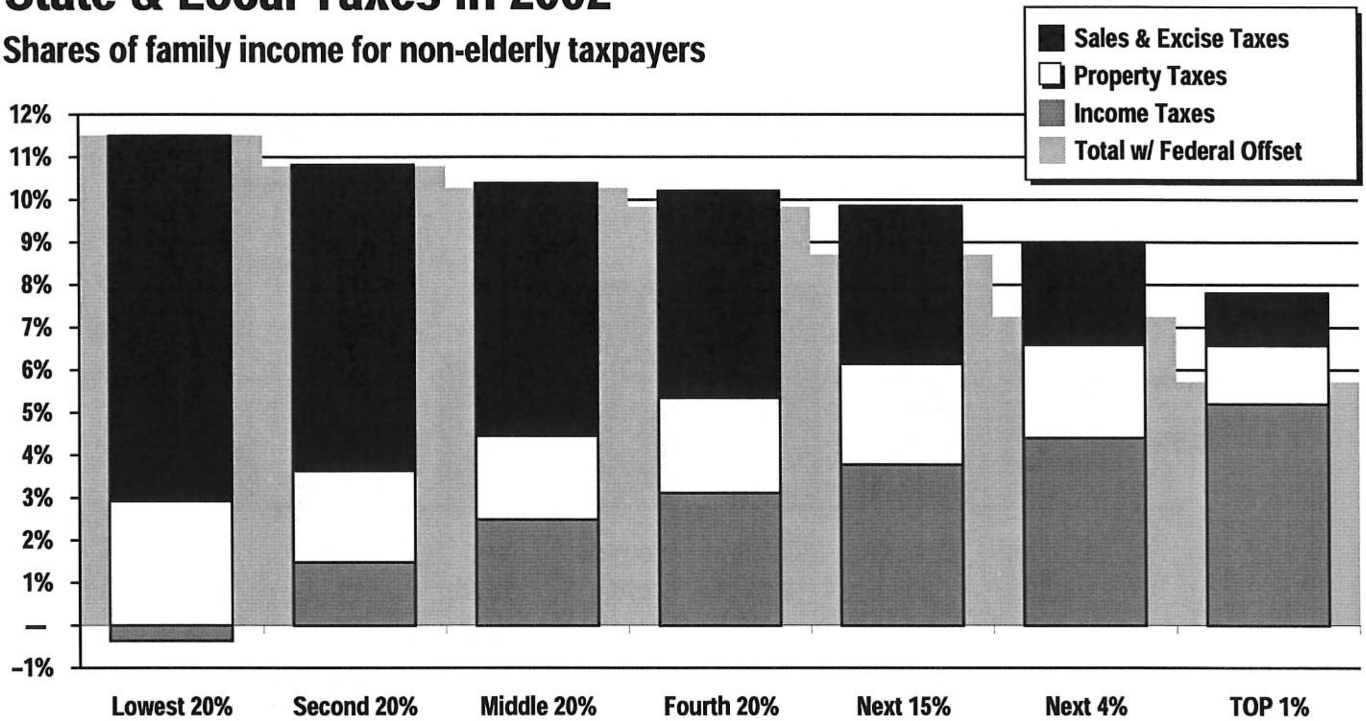
The findings published in the study detail state and local taxes paid by non-elderly couples and individuals. The study includes all major state and local taxes: personal and corporate income taxes, property taxes, and sales and excise taxes.

MORE . . .

Kansas

State & Local Taxes in 2002

Shares of family income for non-elderly taxpayers



Income Group	Lowest 20%	Second 20%	Middle 20%	Fourth 20%	Top 20%		
					Next 15%	Next 4%	TOP 1%
Income Range	Less than $14,000	$14,000 – $27,000	$27,000 – $44,000	$44,000 – $69,000	$69,000 – $126,000	$126,000 – $292,000	$292,000 or more
Average Income in Group	$8,600	$20,200	$34,900	$55,400	$89,300	$175,000	$781,000
Sales & Excise Taxes	**8.8%**	**7.2%**	**5.9%**	**4.9%**	**3.7%**	**2.4%**	**1.2%**
General Sales—Individuals	4.9%	4.3%	3.7%	3.2%	2.5%	1.6%	0.9%
Other Sales & Excise—Ind.	1.9%	1.3%	0.9%	0.6%	0.4%	0.2%	0.1%
Sales & Excise on Business	2.0%	1.7%	1.4%	1.1%	0.8%	0.5%	0.3%
Property Taxes	**3.0%**	**2.1%**	**2.0%**	**2.2%**	**2.4%**	**2.2%**	**1.4%**
Property Taxes on Families	2.9%	2.1%	1.9%	2.1%	2.2%	1.8%	0.7%
Other Property Taxes	0.1%	0.1%	0.1%	0.1%	0.2%	0.4%	0.7%
Income Taxes	**–0.3%**	**1.5%**	**2.5%**	**3.1%**	**3.8%**	**4.5%**	**5.4%**
Personal Income Tax	–0.4%	1.5%	2.5%	3.1%	3.8%	4.4%	5.2%
Corporate Income Tax	0.0%	0.0%	0.0%	0.0%	0.0%	0.1%	0.2%
TOTAL TAXES	**11.5%**	**10.8%**	**10.4%**	**10.2%**	**9.9%**	**9.0%**	**8.0%**
Federal Deduction Offset	—	–0.1%	–0.1%	–0.4%	–1.2%	–1.8%	–2.2%
TOTAL AFTER OFFSET	**11.5%**	**10.8%**	**10.3%**	**9.8%**	**8.7%**	**7.2%**	**5.7%**

Note: Table shows 2002 tax law at 2000 income levels.

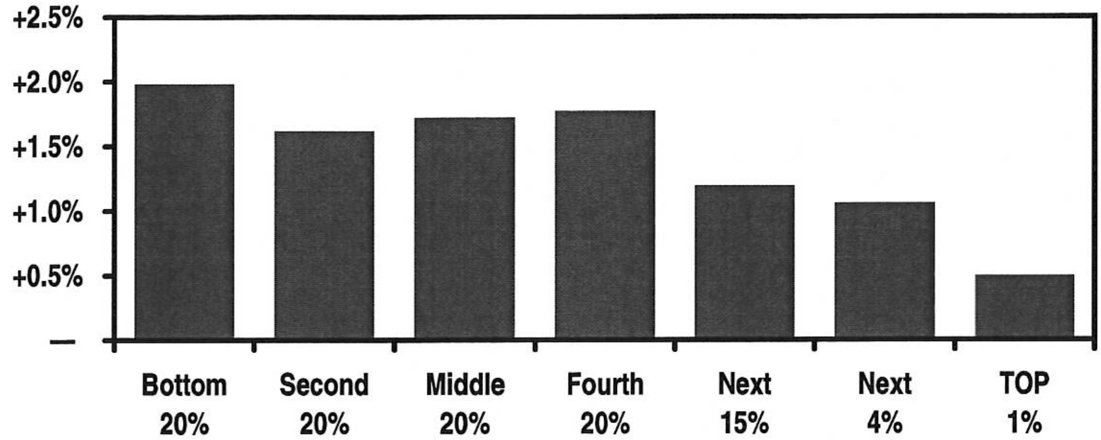
Assessment & Taxation
Date 3-6-07
Attachment # 5-9

Kansas Tax Trends

Progressive Features
- ✔ Refundable EITC
- ✔ Low income property tax circuit breaker

Regressive Features
- ✘ Groceries subject to sales tax

Changes in Taxes as Shares of Income, 1989 – 2002

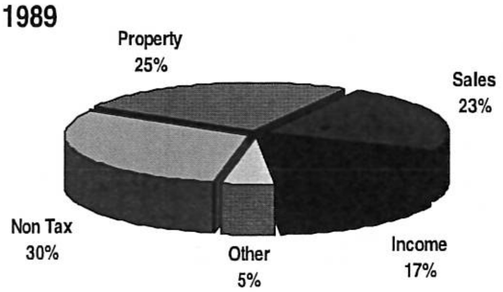


	Bottom 20%	Second 20%	Middle 20%	Fourth 20%	Top 20%		
					Next 15%	Next 4%	TOP 1%
Sales & Excise	+2.7%	+2.0%	+1.6%	+1.3%	+1.0%	+0.6%	+0.3%
Property	+0.3%	–0.1%	–0.3%	–0.3%	–0.6%	–0.4%	–0.2%
Income	–1.1%	–0.4%	+0.3%	+0.8%	+1.0%	+1.3%	+1.3%
Federal Offset	+0.0%	–0.0%	+0.0%	–0.0%	–0.2%	–0.5%	–0.9%
Overall Change	+2.0%	+1.6%	+1.7%	+1.8%	+1.2%	+1.1%	+0.5%

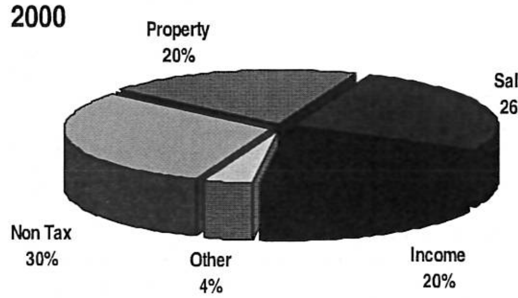
Kansas has moved toward a more progressive system by enacting a 15% refundable EITC, eliminating the federal tax deduction, and adopting a new low-income food sales tax credit. The flatter rate structure has mitigated the overall progressive changes but the income tax is more progressive in 2002 than it was in 1989. These changes and the scaling back of the car tax however were not enough to offset regressive hikes in the general sales tax and the cigarette tax.

Composition of Revenues

1989



2000



Source: Government Finances, US Department of Census

Assessment & Taxation
Date 3-6-07
Attachment # 5-10

KANSAS LIVESTOCK ASSOCIATION

Since 1894

TESTIMONY

To: Senate Committee on Assessment and Taxation
Senator Barbara Allen, Chair

From: Aaron Catlin, Kansas Livestock Association

Date: March 6, 2007

Re: SB 305

The Kansas Livestock Association (KLA), formed in 1894, is a trade association representing over 5,000 members on legislative and regulatory issues. KLA members are involved in many aspects of the livestock industry, including seed stock, cow-calf and stocker production, cattle feeding, grazing land management and diversified farming operations.

Madame Chair and members of the Committee:

My name is Aaron Catlin and I am appearing in favor of SB 305 on behalf of the Kansas Livestock Association.

The KLA is supportive of the Legislature's desire to study and modernize our state's tax structure. Our organization would advocate for an overall tax policy that promotes business growth, allowing for increased economic growth and revenues.

Given agriculture's unique position as a commodity based industry and it's importance to the Kansas economy, I would submit that one member of the proposed tax modernization commission be from the production agriculture industry.

Production agriculture has been a stalwart of the Kansas economy from the earliest days of our state. According to the USDA, the top five Kansas agriculture commodities (cattle, wheat, corn, soybeans, hogs) provided nearly $10 billion in cash receipts in 2005. Of this, the cattle industry provided over $6 billion, or 61% of the total receipts.

Our state's geographical location and topography make it an ideal incubator for agricultural production. Unfortunately, the same geography and topography make it difficult for rural areas to attract additional industries necessary to diversify and protect the tax base. For this reason, it is necessary to proceed with caution when making tax policy that adversely affects the oftentimes lone viable industry of rural Kansas.

Assessment & Taxation
Date 3-6-07
Attachment # 6

6031 SW 37th Street ◆ Topeka, KS 66614-5129 ◆ (785) 273-5115 ◆ Fax (785) 273-3399 ◆ E-mail: kla@kla.org ◆ www.kla.org

Population shift from rural to urban areas has begun to take its toll on many rural communities and counties. As small businesses close and take their employees and families with them, the property tax base erodes, many times leaving agricultural land and related businesses as the only significant taxable base left.

The largest economic engine of rural Kansas is a role the agriculture industry accepts, but it is not a role the industry can sustain in a high tax environment. A representative of the agriculture community on the tax modernization commission can help ensure that the production agriculture industry remains a healthy and vibrant piece of the economy for the foreseeable future.

Our organization is supportive of your desire and efforts to help move Kansas' tax policy at the speed of our state's changing economy and population demographics. I am available for questions when you deem them appropriate.

KANSAS ASSOCIATION OF SCHOOL BOARDS

1420 SW Arrowhead Road • Topeka, Kansas 66604-4024
785-273-3600

Testimony on **SB 305**
before the
Senate Assessment and Taxation Committee

by

Mark Tallman, Assistant Executive Director/Advocacy
Kansas Association of School Boards

March 6, 2007

Madam Chair, Members of the Committee:

Thank you for the opportunity to testify as a proponent of **SB 305**, which would establish a tax modernization committee.

In December, prior to the beginning of the 2007 session, the Kansas Association of School Boards adopted a resolution on school funding issues. One section of that resolution calls for a comprehensive review of state and local tax policy, which we hope will result in a more stable, adequate source of funding for schools and other public programs; an equitable distribution of the tax burden; and an economically responsive tax system.

Our members adopted this position out of a growing concern over recent trends in tax and funding policies, particularly in the area of school finance.

- Although the overall tax burden in Kansas as a percentage of personal income has remained stable, the share of governmental revenues from property taxes has increased while the share from income taxes has declined. In other words, funding has shifted from the source most economically responsive and tied to "ability to pay" to the source that is the most unpopular and least sensitive to "ability to pay." Furthermore, the property tax burden itself has shifted toward residential property.

- Although education is clearly a state responsibility, the portion of school budgets directly funded by the state has declined, and the share which is raised locally has increased. Most local funding comes from the property tax. Unless there is full equalization of local effort in school finance, greater reliance on local revenues results in greater disparities in the tax burden.

Assessment & Taxation
Date 3-6-07
Attachment # 7

- The declining portion of funding now provided by the state means that some districts continue to seek more ways to raise revenues locally, which in turn causes other districts to raise local revenues to maintain competitive salaries and programs. For many districts, the only choice is to raise property taxes on the elderly or short programs for children.

- Reductions in the statewide mill levy for schools have been offset by increases in the Local Option Budget, which means the highest-wealth districts have received a comparative tax reduction while lower wealth districts have had an increase.

- The shift to property and sales taxes to fund both schools and other public programs has made the tax system more regressive. Those who benefit the most from education at all levels – those with the highest skill commanding the highest wages and earning the most income – are paying less of their income. Those who benefit the least – low skill, low income and the elderly – are paying more.

Are any of these trends what we would seek if designing a tax system from scratch? We think not. Instead, we suggest they are the unintended consequences of a long series of decisions made in isolation. Unfortunately, they have also helped created a political climate in which virtually any tax reduction is considered positive regardless of its impact on revenues or equity, and any state-level tax increase brings threats of political retribution, regardless of its impact on local taxes, fairness or quality of services.

Left unchecked, these trends will not only erode the tax base; they will eventually erode the quality of public services, from education to transportation to public safety. While Kansas tends to rank in the middle to the top half of the nation in tax burden, it unquestionably ranks in the top half in many services, especially education, which is usually in the top 10 or 15 of the states. Most other high performing states educationally either spend more than Kansas are have fewer "special needs" students.

We believe that education at all levels, from pre-K to postsecondary, will more than any other factor under the state's control determine its economic future, quality of life and health of our democratic institutions. As advocates of education, school leaders are realizing that how the state pays for education, and who pays for that price, must be part of our concern.

It seems clear that only a high-level, independent review of the entire system can lead to a comprehensive solution. **SB 305** offers the opportunity for that review, and we strongly support such an initiative.

Thank you for your consideration.