Approved: February 5, 2009
Date

MINUTES OF THE HOUSE TAXATION COMMITTEE

The meeting was called to order by Chairman Richard Carlson at 9:00 a.m. on January 22, 2009, in Room 535-N of the Capitol.

All members were present.

Committee staff present:
- Hank Avila, Kansas Legislative Research Department
- Chris Courtwright, Kansas Legislative Research Department
- Gordon Self, Office of the Revisor of Statutes
- Scott Wells, Office of the Revisor of Statutes
- Kathy Beavers, Committee Assistant

Conferees appearing before the committee:
- Joan Wagnon, Secretary, Kansas Department of Revenue (KDOR)
- Duane Goossen, Director of Division of Budget (KDOR)
- Mark Desetti, Kansas Association of School Boards and Kansas National Education Association
- April Holman, Kansas Action for Children
- John Donley, Assistant General Counsel for Kansas Livestock Association
- Kent Eckles, Kansas Chamber of Commerce
- Dan Murray, National Federation of Independent Business (NFIB)
- Dave Holtwick, Overland Park Chamber of Commerce
- Mike Murray, Embarq
- Natalie Bright, Wichita Independent Business Association
- Kenneth Daniel, Exec. Director, Topeka Independent Business Association

Written Testimony only:
- Brad Harrelson, Kansas Farm Bureau
- Christy Caldwell, Greater Topeka Chamber of Commerce
- Ashley Sherard, Lenexa Chamber of Commerce

Others attending:
See attached list.

Bill Introductions:
Representative Julie Menghini made a motion, at the request of Representative Jerry D. Williams, to introduce a bill concerning property taxation relating to real property taxes due and unpaid interest and penalties redemption procedures. Representative Frownfelter seconded the motion. The motion carried.

Mr. John Peterson, on behalf of the Kansas Health and Fitness Association, requested an introduction of a bill dealing with sales tax exemptions. It is a continuation of a discussion, by the committee on the House floor, last year regarding tax sales exemptions. This bill does not ask for any additional exemptions but it would treat all currently granted ones on an equal basis. A motion was made by Representative Carlson and seconded by Representative King to accept the bill introduction. The motion carried.

HB 2028 - Continuation of the franchise tax.

Staff Chris Courtwright gave a brief introduction and history of the Corporation Franchise Tax (Attachment 1). He stood for questions.

Mr. Duane Goossen explained that the FY 2009 budget would be $142 million in the red and explained that a wide gap has opened up between our expected State General Fund revenues and our planned or expected State General Fund (SGF) Expenditures (Attachment 2). He provided detailed information and made suggestions on how to close the gap in the budget, mainly by reducing the expenditures. Mr. Goossen asked the committee to make policy changes to reduce the budget. He stated the decisions will be difficult but they have to be made to close the negative gap. Even with help from the federal government stimulus package, the cuts still need to be considered. He stated the main business before the Legislature is to close the gap and find 944 million dollars worth of solutions between FY 2009 and FY 2010. Mr. Goossen stood for questions.

Minutes of the House Taxation Committee at 9:00 a.m. on January 22, 2009, in Room 535-N of the Capitol.

Secretary Wagnon testified in support of **HB 2028** (Attachment 3). The number of business entities subject to the corporate franchise tax has been drastically reduced due in part to the passage of **SB 247**. During 2004 and 2007 those entities subject to the tax have decreased from 80,000 to 7,000. Enactment of **HB 2028** will have a positive fiscal impact. She stated the administrative costs to implement this proposal would be absorbed by the Department of Revenue. Secretary Wagnon stood for questions.

The Chairman requested that the conferees testifying on this bill stand for questions at the conclusion of the oral testimony.

Mark Desetti, Kansas Association of School Boards and Kansas National Education Association, testified in support of **HB 2028**. He stated that increased school funding has led to a large improvement in student achievement. Reduction in school funding would result in significant economic consequences for struggling families (Attachment 4).

April Holman, Kansas Action for Children, testified in support of **HB 2028** (Attachment 5) . Kansas Action for Children works to promote policies that improve education, healthcare for children, and family economic success. The phasing out and elimination of the franchise tax would decrease the monies in the State General Fund by $26 million dollars.

Mr. Desetti and Ms. Holman stood for questions.

The Chairman called attention to the submitted written neutral testimony from Ashley Sherard, Vice President of Lenexa Chamber of Commerce (Attachment 6).

Mr. John Donley, Assistant General Counsel for Kansas Livestock Association, testified in opposition to **HB 2028** (Attachment 7). He stated that this franchise tax is simply a tax companies pay for the privilege of doing business in Kansas and continuing the tax is not fair to Kansas businesses.

Mr. J. Kent Eckles, Kansas Chamber of Commerce, testified in opposition to **HB 2028** (Attachment 8). He stated that "Repealing the recently passed franchise tax phase-out will only serve to exacerbate the competitive disadvantage and hurt investment and job creation in the State."

Dan Murray, NFIB, testified in opposition to **HB 2028**. He stated that a repeal of the franchise tax phase-out could negatively impact the promotion of small business growth (Attachment 9).

Dave Holtwick, Overland Park Chamber of Commerce, testified in opposition to **HB 2028**. He stated that this bill will negatively impact the business climate and give companies seeking to locate in Kansas or retain their facilities in the state one more reason to question that decision. Kansas needs incentives to help attract and retain businesses in the state. Passage of **HB 2028** will reduce competitiveness (Attachment 10).

Mike Murray, Embarq, testified in opposition to **HB 2028** (Attachment 11).

Natalie Bright, Wichita Independent Business Association, testified in opposition to **HB 2028** (Attachment 12).

Mr. Kenneth Daniel, Topeka Independent Business Association testified in opposition to **HB 2028** (Attachment 13). His written testimony stated the franchise tax is an aggressively anti-business tax. He compared the Kansas franchise tax with other states and found that Kansas has one of the most regressive taxes in the nation.

The Chairman called attention to the written testimony of the following persons (Attachment 14 and 15):

Brad Harrelson, Kansas Farm Bureau
Christy Caldwell, Greater Topeka Chamber of Commerce

The meeting was adjourned at 10:55 a.m. The next meeting is scheduled for January 27, 2009.

HOUSE TAXATION COMMITTEE

SIGN IN SHEET

DATE: 1-22-09

Natalie Bright	WIBA
Ron Gaches	GBA
John Peterson	Capitol Strategies
Michelle Butler	" "
Dina Fisk	Verizon
Ken Daniel	TTBA
Mike Murray	Embarq
Doug Galloway	Embarq
Kent Eckles	Kansas Chamber
Leigh Keck	Hein Law Firm
Dan Murray	NFIB
J P Small	Koch Industries

MEMORANDUM **January 21, 2009**

To: House Taxation Committee
From: Chris W. Courtwright, Principal Economist
Re: Corporation Franchise Tax

History

Originally enacted in 1866, the corporation franchise tax was the third tax enacted in the state's history. From 1866 through 1912, various charter and miscellaneous fees were required to be paid by corporations. From 1913 to 1971, the tax ranged from $10 for less than $10,000 of paid-up capital stock to $2,500 for over $5 million of paid-up capital stock. From 1972 to 2001, the tax was set at $1 per $1,000 or corporation's shareholder's equity attributable to Kansas, with a minimum tax of $20 and a maximum of $2,500. (Legislation enacted in the 1990s required limited liability companies (LLCs) to pay $1 per $1,000 of net capital accounts located in or used in the state, also with a minimum tax of $20 and a maximum of $2,500. One-member LLCs taxed as sole proprietorships pay $1 per $1,000 of net book value as calculated on an income tax basis.)

An omnibus tax bill enacted late in 2002 sought to effectively double the amount of revenues received under the corporation franchise taxes. The tax was increased to $2 per $1,000 of shareholder equity up to a maximum of $5,000. This law remained in effect for tax years 2002 and 2003.

Legislation enacted in 2004 subsequently made numerous structural changes in the franchise tax, effective for tax year 2004 and thereafter. The rate of the tax was reduced from $2 per $1,000 of shareholder equity or net worth to $1.25 percent. The maximum liability cap of $5,000 also was increased to $20,000; and a new exemption was provided for entities with equity or net worth of $100,000 or less. (Banks, insurance companies, savings and loans, firemen's relief associations and certain venture capital companies are exempt from the tax altogether.)

Administration of the franchise tax based on shareholder equity or net worth was relocated from the Office of the Secretary of State to the Department of Revenue. Corporations and associations, limited liability companies, limited partnerships, and business trusts are now required to file annual returns with the Director of Taxation and remit the franchise tax liability before April 15 of each year. The franchise tax is deposited in the State General Fund (SGF).

The Secretary of State's Office maintains a separate annual franchise fee of $40 for for-profit and not-for-profit entities. This $40 fee is deposited in SGF and produces about $4 million per year.

The Secretary of State also collects a $10 administrative fee and a $5 technology fee on all annual reports of for-profit entities pursuant to statutory authority contained in KSA 75-438 and 75-444. These fees are deposited in fee funds.

Legislation enacted in 2007 (HB 2264 as amended by SB 215) provided for the phase out of the tax collected by the Department of Revenue that is deposited in the SGF. For tax year 2007, the exemption threshold was increased from $0.1 million to $1.0 million. The rate was reduced from $1.25 per $1,000 of equity to $0.9375 in tax year 2008; to $0.625 in tax year 2009; to $0.3125 in tax year 2010. The tax is scheduled to be repealed altogether starting in tax year 2011.

Governor's Recommendation

The Governor at the outset of the 2009 Session made a number of tax and budget recommendations, including those relating to the franchise tax embodied in HB 2028.

That proposal would freeze the franchise tax rate structure permanently at the tax year 2008 level ($1.0 million exemption threshold and rate of $0.9375) and repeal the phase out.

The following table shows a recent history of tax and fee collections deposited in the SGF:

($ in millions)

Actual SGF Receipts and Nov Consensus Estimate		Governor's Recommendation	Fiscal Note
FY 2001	$16.927		
FY 2002	$18.520		
FY 2003	$31.089		
FY 2004	$36.806		
FY 2005	$47.085		
FY 2006	$46.880		
FY 2007	$47.892		
FY 2008	$46.659		
FY 2009 est	$32.000		
FY 2010 est	$20.000	$34.000	$14.000

Under the Governor's recommendation, receipts for FY 2010 and future years would be expected to stabilize at around $34.0 million.

Overview Presentation

FY 2010 Governor's Budget Report

January 2009

To view the full FY 2010 Governor's Budget Report or to receive further information, please go to http://budget.ks.gov or contact the Division of the Budget at 785-296-2436.

Kansas, like many other states, faces a very challenging financial situation. State costs for public education and Medicaid have increased substantially, but revenue expectations have diminished due to slower economic growth in Kansas and a national recession. The most recent revenue estimates no longer support approved FY 2009 expenditures, and building a new FY 2010 budget following previous standards would lead to a gap between expenditures and available resources of over $900 million.

Within this difficult financial context, Governor Kathleen Sebelius presents a revised budget for FY 2009 and a new balanced budget for FY 2010. Five basic principles guide the Governor's budget recommendations:

Resolve the State General Fund budget gap in a realistic way without raising taxes ;

Protect the state's investment in public education;

Fund human service caseload costs;

Ensure the public safety of Kansans, and the continuation of basic state services; and

Include all state agencies in the budget solution.

Budget Totals
(Dollars in Millions)

	SGF	Percent Change	All Funds	Percent Change
FY 2008 Actual	$ 6,101.8	--	$ 12,688.7	--
FY 2009 Apprv. (May 2008)	6,404.4	5.0%	13,487.1	6.3%
FY 2009 Apprv. with Shifts	6,440.7	5.6%	13,523.4	6.6%
FY 2009 Gov. Est.	6,348.6	4.0%	13,600.1	7.2%
FY 2010 Gov. Rec.	6,153.5	(3.1%)	12,881.4	(5.3%)

Expenditures

Expenditures in almost every State General Fund agency have been reduced in FY 2009, and then reduced further in FY 2010. In addition, State General Fund debt has been restructured, a 9-month moratorium proposed on payments into the KPERS Death and Disability Fund, as well as a 7-pay period moratorium on payments to the state employees' health fund.

Total expenditures to fund public education in 2010 remain flat from the approved FY 2009 amount. The budget includes human service caseload costs. The Governor proposes that state employees receive a 1.0 percent general salary increase, but expects agencies to absorb the cost of the increase.

Changes to Revenue

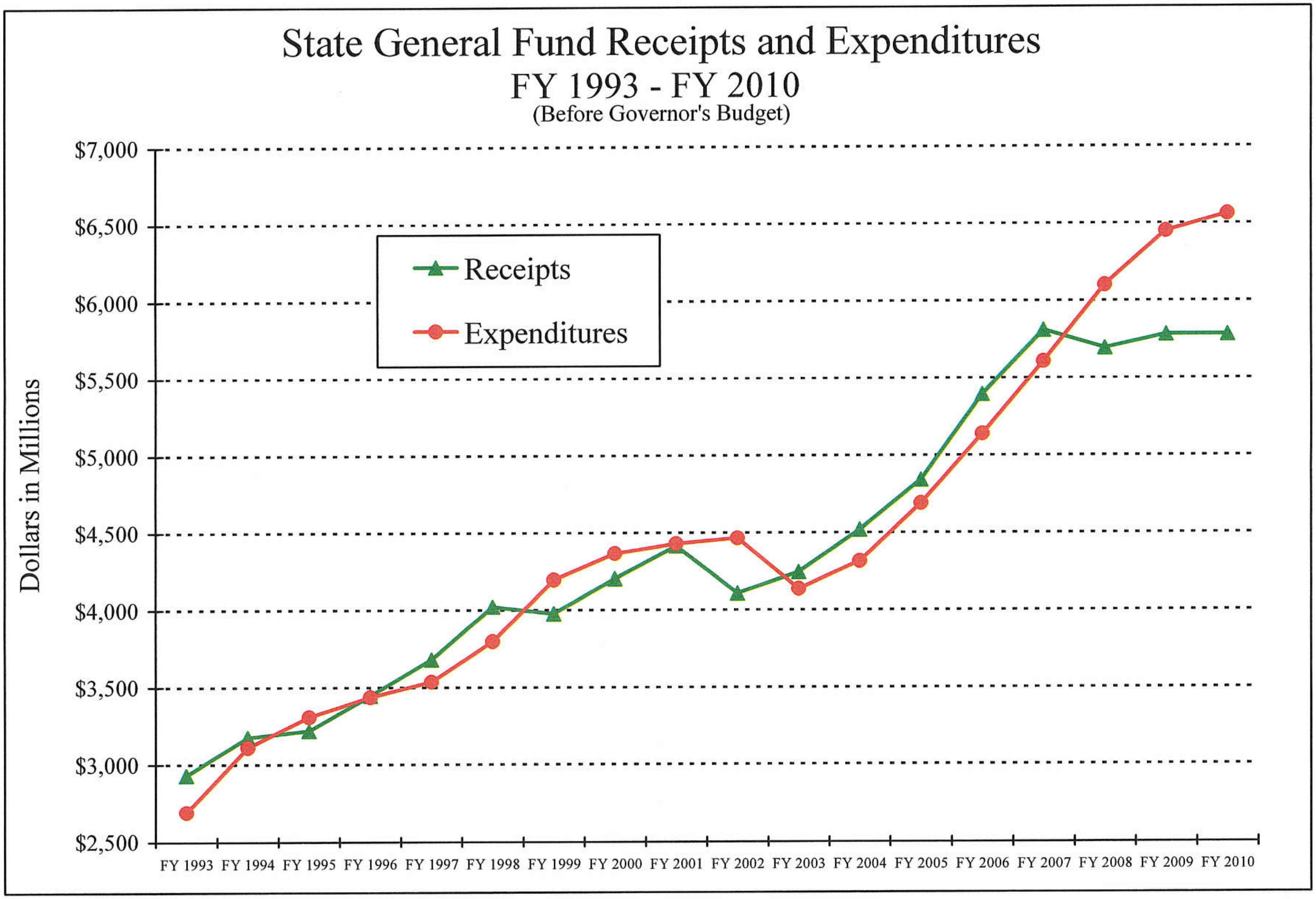
The Governor does not recommend any tax increases as part of her budget, but does propose changes to transfers in and out of the State General Fund. Expenditures in special revenue fund agencies are reduced and the resulting savings plus any other balances transferred to the State General Fund. Available revenue from new gaming operations is proposed to be transferred. Transfers out of the State General Fund are suspended or limited.

The budget also recommends improving revenue through several tax policy changes to suspend the phase-out of the estate and corporate franchise taxes, eliminate the community service credit, accelerate severance tax collections and attribute a larger portion of liquor taxes to the State General Fund.

The next revenue projection will be made in mid-April. While this proposed budget uses updated November estimates, the state's financial situation is still fluid. Further action may be required once the spring estimates are made.

Ending Balance

Together, all of the steps proposed to resolve the budget gap yield an ending State General Fund balance of $58.3 million in FY 2009 and $0.6 million in FY 2010. Under the current extraordinary circumstances, building a realistic budget without tax increases that projects a 7.5 percent ending balance is not possible. A brief budget that meets statutorily required balances has been included in Volume 1 of *The Governor's Budget Report*.


State General Fund Receipts and Expenditures
FY 1993 - FY 2010
(Before Governor's Budget)
Dollars in Millions
$7,000
$6,500
$6,000
$5,500
$5,000
$4,500
$4,000
$3,500
$3,000
$2,500
Receipts
Expenditures
FY 1993
FY 1994
FY 1995
FY 1996
FY 1997
FY 1998
FY 1999
FY 2000
FY 2001
FY 2002
FY 2003
FY 2004
FY 2005
FY 2006
FY 2007
FY 2008
FY 2009
FY 2010

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State General Fund Outlook--Without Solutions

Approved FY 2009 Budget Plus Consensus Amounts for Caseloads and School Finance

(Dollars in Millions)

	FY 2008	FY 2009	FY 2010
Beginning Balance	$ 935.0	$ 526.6	$ (142.0)
November 4, 2008 Updated Revenues	5,693.4	5,781.2	5,782.4
Total Available	$ 6,628.4	$ 6,307.8	$ 5,640.4
Expenditures			
Aid to K-12 Schools	$ 3,065.1	$ 3,222.4	$ 3,357.9
School Finance Consensus Adjustments	--	3.7	--
Higher Education	829.1	852.6	852.6
Health/Human Services Caseloads	831.7	886.9	923.2
Consensus Caseload Adjustments	--	5.4	--
Undermarket Salary Adjustments	--	--	8.5
All Other Expenditures	1,370.1	1,442.5	1,442.5
Reappropriations from FY 2008	--	36.3	--
Total Expenditures	$ 6,096.0	$ 6,449.8	$ 6,584.8
Ending Balance	$ 532.4	$ (142.0)	$ (944.4)
As Percent of Expenditures	*8.7 %*	*(2.2%)*	*(14.3%)*

State General Fund Outlook--With Solutions

Governor's Proposed Balanced Budget

(Dollars in Millions)

	FY 2008 Actual	FY 2009 Gov. Rec.	FY 2010 Gov. Est.
Beginning Balance	$ 935.0	$ 526.6	$ 58.3
November 4, 2008 Updated Revenues	5,693.4	5,781.2	5,782.4
Governor's Revenue Adjustments	--	99.2	313.4
Total Available	$ 6,628.4	$ 6,407.0	$ 6,154.1
Expenditures			
Aid to K-12 Schools	$ 3,065.1	$ 3,223.5	$ 3,181.9
Higher Education	829.1	830.0	773.0
Health/Human Services Caseloads	836.1	883.8	870.6
All Other Expenditures	1,371.5	1,411.3	1,328.0
Total Expenditures	$ 6,101.8	$ 6,348.6	$ 6,153.5
Ending Balance	$ 526.6	$ 58.3	$ 0.6
As Percent of Expenditures	*8.6 %*	*0.9%*	--

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Steps to Resolve Budget Gap

(Dollars in Millions)

	FY 2009	FY 2010
Changes to State General Fund Expenditures		
Reduce Current Year Approved Budgets	101.2	--
Reduce FY 2010 Budgets	--	431.3
Require Agencies to Absorb FY 2010 1% Salary Increase	--	--
Changes to State General Fund Revenues		
Transfers In:		
Reduce CIF Expenditures and Transfer Balance	--	9.2
Reduce EDIF Expenditures and Transfer Balance	--	3.5
Reduce non-SGF Agencies and Transfer Balances	2.2	2.9
Transfer Other Special Revenue Balances	29.0	2.2
End KSIP and Transfer Balances	4.2	--
Transfer Unallocated Gaming Revenue	(1.6)	56.7
KPERS D&D Moratorium Spec. Rev. Fund Savings	--	5.1
Health Insurance Moratorium	--	23.7
Limit Transfers Out:		
Stop Highway Fund Loan Repayment	30.9	30.9
Stop Other Fund Loan Repayments	3.8	3.8
Limit Bioscience Authority Transfer ($35M FY '09 $40M FY '10)	12.0	20.0
Suspend Transfers to SCCHF, SWPF, Health Care Stab.	19.1	19.1
Suspend Deferred Maintenance Transfer to Regents	--	15.0
Reduce Regents Research Corp. for Debt Restructuring	--	5.0
Limit Housing Trust Fund Transfer	--	2.0
Suspend Restoration of LAVTR Transfer	--	13.5
Suspend Property Tax Slider	--	45.3
Net of All Other Changes	(0.4)	(5.0)
Tax Policy Changes:		
Suspend Phase-Out of Corporate Franchise Tax	--	14.0
Suspend Phase-Out of Estate Tax	--	5.0
Elminate Community Service Credit	--	4.4
Accelerate Severance Tax Due Date	--	10.0
Attribute all Liquor Taxes to State General Fund	--	27.2
Total of All Changes	$ 200.4	$ 744.7

2-5

State General Fund Expenditure Reductions

FY 2009

Operating Budget Reductions	$ (38.8)
Debt Restructuring	(14.0)
School Finance Held Flat	(17.7)
Regents System Reductions	(24.6)
KHPA--Switch to Fees Fund	(8.5)
SRS--HCBS PD Waiver	8.4
Close DOC Facilities	(1.6)
Close Atchison Juv. Correc. Fac.	(2.0)
Delay Osawatomie 30-Bed Unit	(1.8)
Net of Other Adjustments	(0.6)
Total	$ (101.2)

FY 2010

School Finance CPI Increase	(108.4)
Special Education Increase	(37.9)
Other School Finance Increases	(18.7)
Regents System Reductions	(56.3)
Kan-Ed Shift to KUSF	(2.0)
KUMC--WCGME	(2.5)
Caseload Policy Changes:	
Freeze Nursing Home Rates	(6.0)
KHPA Switch SGF to Fee Funds	(5.7)
KHPA--Administrative Initiatives	(9.6)
SRS--New Foster Care Contract	(14.1)
MedKan/GA 18-month Limit	(12.3)
CINC Policy	(3.8)
CMHC Grants	(7.0)
CDDO Grants	(2.0)
DOC Facility Closures	(7.8)
Atchison Juv. Correc. Facility Closure	(3.7)
KHP--Suspend New Trooper Class	(1.0)
KPERS D&D 3-Quarter Moratorium	(30.4)
Health Ins. 7-Payroll Cycle Moratorium	(32.0)
Debt Restructuring	(34.1)
Net of Other Adjustments	(36.1)
Total	$ (431.3)

Expenditure reductions have also been recommended for agencies that are not financed from the State General Fund. In most cases, the savings from these reductions are proposed for transfer to the State General Fund. In addition, the budget includes Economic Initiatives Fund reductions resulting from the merger of KTEC and Kansas, Inc. operations into the Department of Commerce, and reductions in Children's Initiatives Fund and Water Plan Fund spending.

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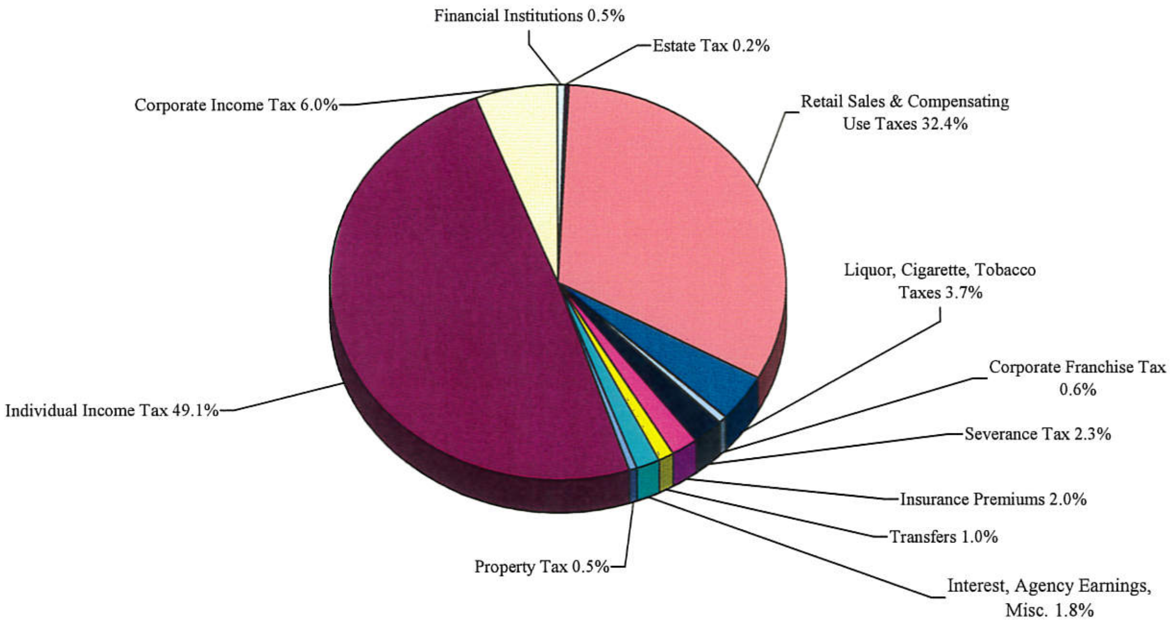
Key Expenditures for Aid to Schools

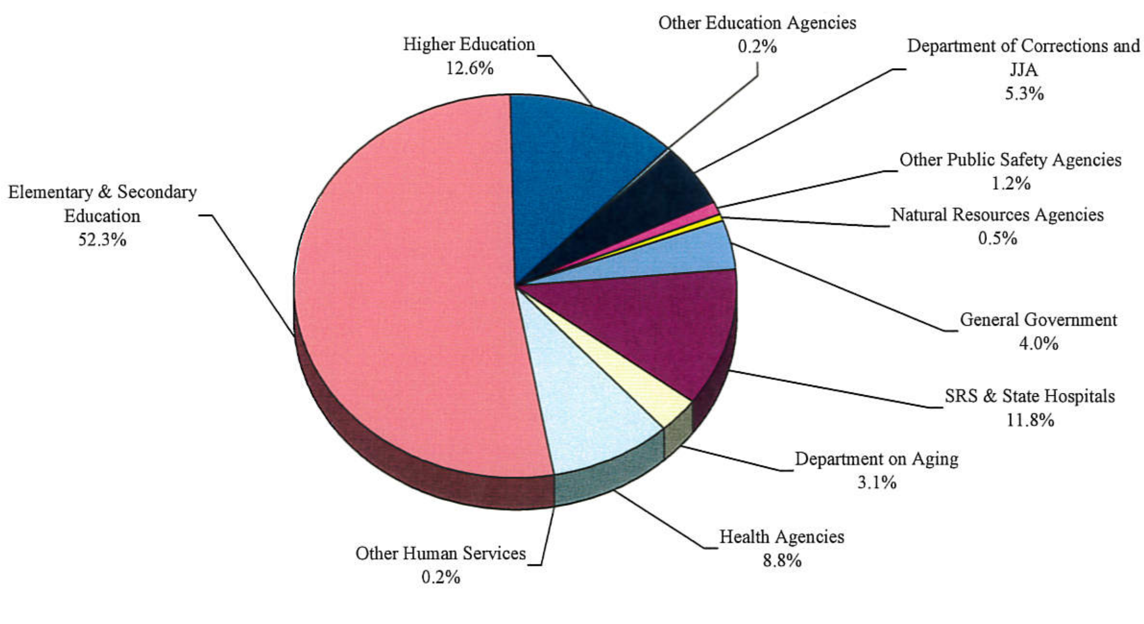
	Approved FY 2009	Consensus FY 2009	Gov. Rec. FY 2009	Consensus FY 2010	Gov. Rec. FY 2010
General State Aid	$ 2,183,419,242	$ 2,197,321,000	$ 2,183,920,915	$ 2,245,217,000	$ 2,126,235,466
Special Education Aid	427,753,137	432,035,493	427,753,137	465,718,765	427,753,137
Local Option Budget	332,676,369	324,146,000	324,146,000	339,212,000	339,212,000
KPERS Emplyer Contributions*	249,998,012	249,989,121	249,989,121	282,188,282	274,111,409
Capital Outlay Aid	25,439,522	22,600,000	22,600,000	25,600,000	25,600,000
Subtotal--SGF	$ 3,219,286,282	$ 3,226,091,614	$ 3,208,409,173	$ 3,357,936,047	$ 3,192,912,012
20 Mill Property Tax Levy	560,060,359	$570,937,468	$570,937,468	$586,434,629	$586,434,629
Total School Funding	$ 3,779,346,641	$ 3,797,029,082	$ 3,779,346,641	$ 3,944,370,676	$ 3,779,346,641

**KPERS--School expenditures are before the proposed FY 2010 KPERS Death & Disability Moratorium.*

Where State Dollars Come From
State General Fund
FY 2010



Where State Dollars Go
State General Fund
FY 2010

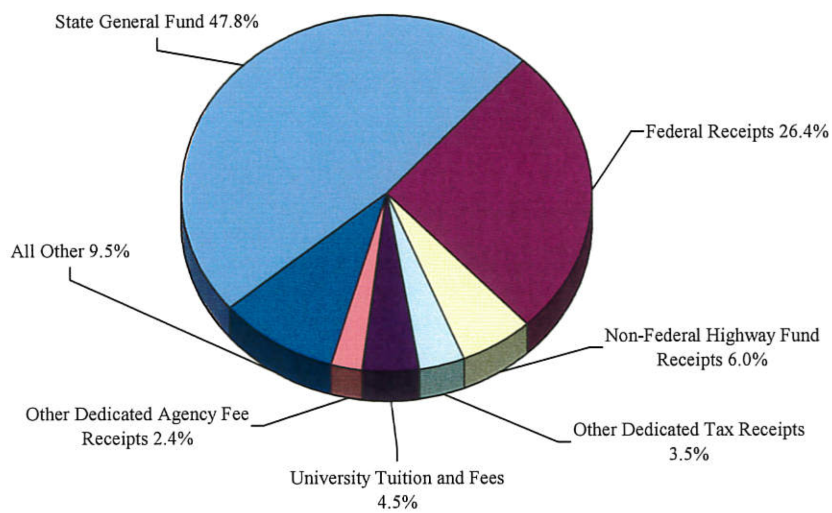


2-8

How the All Funds Budget Is Financed

All Sources of Funding

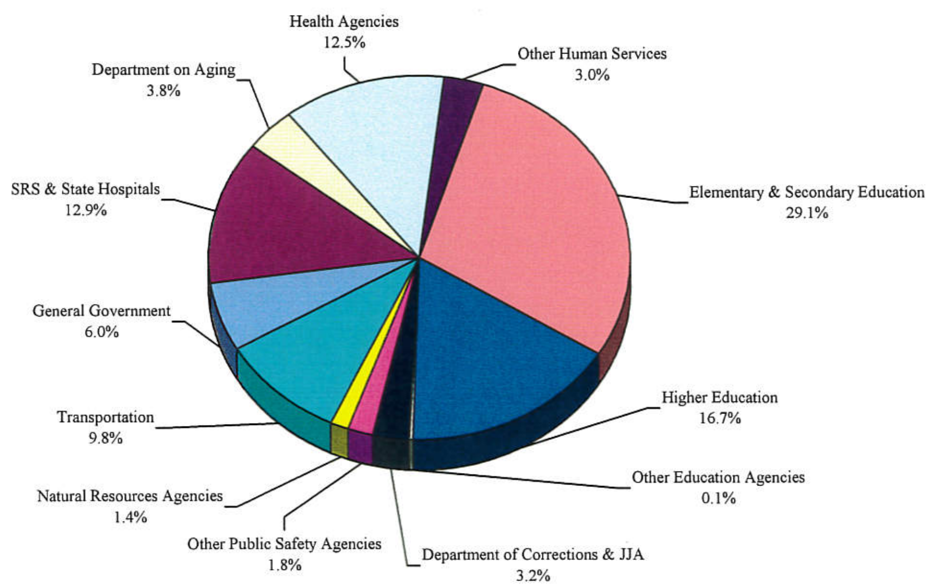
FY 2010



Where All Funds Go

All Sources of Funding*

FY 2010



** Excludes non-reportable expenditures.*

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Economic Development Initiatives Fund Summary

	FY 2008 Actual	FY 2009 Approved	FY 2009 Revised	FY 2010 Gov. Rec.
Beginning Balance	$ 4,034,032	$ 1,127,110	$ 4,980,302	$ 3,204,654
Revenues:				
Released Encumbrances	1,253,077	--	--	--
Lottery Revenues	42,432,000	42,432,000	42,432,000	42,432,000
Interest & Other Revenues	1,724,149	1,400,000	1,400,000	1,000,000
Transfer to KEOIF	(3,000,000)	(1,250,000)	(1,250,000)	(3,250,000)
Transfer to SECPDPF	(150,000)	--	--	--
Transfer to KQBFPIF	(400,000)	(400,000)	(400,000)	(200,000)
Transfer to SWPF	(2,000,000)	(3,043,985)	(3,043,985)	(2,000,000)
Transfer to PUGAADF	--	--	--	(1,000,000)
Parsons Road Transfer	--	750,000	750,000	--
KPERS Death & Dis. Transfer	--	--	--	(46,665)
Health Insurance Transfer	--	--	--	(194,411)
Transfer to SGF	--	--	--	(3,533,611)
Total Available	$ 43,893,258	$ 41,015,125	$ 44,868,317	$ 36,411,967
Expenditures:				
Department of Commerce	18,410,072	18,543,972	19,574,729	25,923,979
KTEC	12,162,460	12,032,258	11,083,876	--
Kansas, Inc.	504,743	415,363	321,139	--
Board of Regents	2,677,723	2,745,500	2,813,277	2,745,500
KSU-ESARP	300,000	300,000	300,000	293,911
WSU-Aviation Research	4,747,958	7,500,000	7,502,042	7,448,577
State Fair	110,000	70,000	68,600	--
EDIF Pay Plan Savings	--	8,789	--	--
Total Expenditures	38,912,956	41,615,882	41,663,663	36,411,967
Ending Balance	$ 4,980,302	$ (600,757)	$ 3,204,654	$ --

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Children's Initiatives Fund

	FY 2008 Actual	FY 2009 Approved	FY 2009 Revised	FY 2010 Gov. Rec.
Beginning Balance	$ 743,550	$ 12,276,628	$ 12,747,981	$ 600,515
Revenues:				
Released Encumbrances	300,233	--	--	--
Transfer From KEY Fund	62,922,205	64,458,892	64,458,892	66,867,010
Transfer from CIRF	825,952	825,952	825,952	825,952
Total Available	$ 64,791,940	$ 77,561,472	$ 78,032,825	$ 68,293,477
Expenditures				
Social & Rehabilitation Services				
Early Childhood Block Grant	--	11,100,000	11,100,000	11,098,462
Children's Mental Health Initiative	3,800,000	3,800,000	3,800,000	3,800,000
Family Centered System of Care	5,000,000	5,000,000	5,000,000	5,000,000
Therapeutic Preschool	1,000,000	--	--	--
Child Care Services	1,400,000	1,400,000	1,400,000	1,400,000
Community Svcs. For Child Welfare	3,298,500	3,208,938	3,136,934	--
Smart Start Kansas	8,986,263	8,443,279	8,443,279	8,442,190
Pre-K Pilot	5,000,000	--	--	--
Early Head Start	1,600,000	3,452,779	3,452,779	3,452,779
Child Care Quality Initiatives	500,000	500,000	500,000	500,000
Children's Cabinet Account. Fund	541,802	541,802	541,802	541,802
Family Preservation	3,151,403	3,241,062	3,313,066	3,241,062
Attendant Care for Independ. Living	50,000	--	--	--
School Violence Prevention	227,392	--	--	--
Total--SRS	34,555,360	40,687,860	40,687,860	37,476,295
Kansas Health Policy Authority				
Immunization Outreach	277,876	500,000	500,000	--
Healthwave	2,000,000	2,000,000	2,000,000	--
Medical Assistance	3,000,000	3,000,000	3,000,000	--
Total--KHPA	5,277,876	5,500,000	5,500,000	--
Health & Environment--Health				
Healthy Start/Home Visitor	250,000	250,000	250,000	250,000
Special Health Services	208,000	208,000	208,000	--
Newborn Hearing Aid Loaner Program	--	50,000	50,000	50,000
SIDS Network Grant	--	75,000	75,000	75,000
Newborn Screening	--	2,216,888	2,221,556	2,202,682
Infants & Toddlers Program	1,200,000	5,700,000	5,700,000	5,700,000
Smoking Prevention Grants	1,000,000	1,000,000	1,000,000	1,000,000
Total--KDHE	2,658,000	9,499,888	9,504,556	9,277,682
Department of Education				
Reading, Vision, General Aid	300,000	300,000	200,000	--
Parent Education	--	7,539,500	7,539,500	7,539,500
Pre-K Pilot	--	5,000,000	5,000,000	5,000,000
Total--KSDE	300,000	12,839,500	12,739,500	12,539,500
University of Kansas Medical Center	252,723	--	394	--
Juvenile Justice Authority	9,000,000	9,000,000	9,000,000	9,000,000
Total Expenditures	52,043,959	77,527,248	77,432,310	68,293,477
Ending Balance	$ 12,747,981	$ 34,224	$ 600,515	$ --

2-11

State Water Plan Fund

	FY 2008 Actual	FY 2009 Approved	FY 2009 Revised	FY 2010 Gov. Rec.
Beginning Balance	9,052,462	2,846,479	2,846,479	--
Revenues				
Released Encumbrances	981,099	1,107,136	1,087,010	421,709
Transfer to GMD #3	(739,964)	--	--	--
Transfers to the SGF	--	--	--	(16,152)
Transfer to KCC	(400,000)	(400,000)	(320,000)	(288,000)
SGF Transfer	6,000,000	6,000,000	--	--
EDIF Transfer	2,000,000	3,043,985	3,043,985	2,000,000
Kansas v. Colorado Damage Award	584,217	525,729	525,729	--
Clean Drinking Water Fee Revenue	--	6,480,609	6,480,609	3,469,486
Fee Receipts	9,605,356	9,591,669	9,591,669	9,429,270
Total Available	27,083,170	29,195,607	23,255,481	15,016,313
Expenditures				
Dept. of Health & Environment	4,087,999	3,929,512	3,143,610	2,617,221
Univ. of Kansas--Geological Survey	40,000	40,000	32,000	28,800
Department of Agriculture	1,130,152	1,403,501	1,245,979	1,124,615
State Conservation Commission	15,173,035	19,118,350	15,210,497	9,065,321
Kansas Water Office	2,765,505	4,664,244	3,591,395	2,151,556
Department of Wildlife and Parks	1,040,000	40,000	32,000	28,800
Total Expenditures	24,236,691	29,195,607	23,255,481	15,016,313
Ending Balance	2,846,479	--	--	--

2-12

KANSAS
DEPARTMENT OF REVENUE

Kathleen Sebelius, Governor
Joan Wagnon, Secretary

www.ksrevenue.org

Testimony to the House Taxation Committee

Joan Wagnon

January 22, 2009

Testimony in Support of House Bill 2028

Representative Richard Carlson, Chair, and Members of the Committee:

House Bill 2028 would amend K.S.A. 79-5401 to continue the franchise tax at the rate in effect for Tax Year 2008, which is .09375% of Kansas taxable equity for a business entity subject to the tax (Kansas taxable equity of $1 million or more), with maximum tax liability capped at $20,000. The bill would also strike the language phasing out the corporation franchise tax. Kansas taxable equity is the entity's net book value, net capital accounts, or shareholder's equity as reflected on the balance sheet multiplied by the average percent of property, payroll, and sales attributable to Kansas.

Under current law, foreign and domestic for-profit corporations, professional corporations or associations, limited liability companies, limited partnerships, limited liability partnerships, and business trusts authorized to do business in Kansas with Kansas taxable equity of $1 million or more are subject to the corporate franchise tax. The current rate is .09375% of Kansas taxable equity, dropping to .0625% for Tax Year 2009, .03125% for Tax Year 2010, and phasing out effective in Tax Year 2011. Maximum tax liability is capped at $20,000. Electric co-ops, renewable energy electric co-ops, and not-for-profit corporations are not subject to the franchise tax.

Background

The corporate franchise tax is one of the oldest taxes in the Kansas tax base, going back almost to the State's infancy, first enacted in 1866. It was administered by the Secretary of State until 2004, when administration was moved to the Department, pursuant to Senate Bill 147.

The corporate franchise tax rates have been changed several times during this decade, most recently in 2007, when House Bill 2264 raised the threshold for a business entity to be subject to the tax from Kansas taxable equity of $100,000 to $1 million. House Bill 2264 also put in place the current rate reduction schedule and phase out of the tax, reducing the rate from .125% of Kansas taxable equity to .09375% effective for Tax Year 2008, with the further rate reductions until total phase out in Tax Year 2011. The annual maximum tax liability cap of $20,000 per entity was not changed.

In 2004, Senate Bill 147 moved administration of the corporate franchise tax from the Secretary of State to the Department of Revenue, reduced the rate from .2% of Kansas taxable equity to .125%, added a threshold of $100,000 in Kansas taxable equity before the entity would be subject to the tax, and raised the annual maximum tax liability cap from $5,000 to $20,000 per entity.

In 2002, Senate Bill 39 raised the corporate franchise tax rate from .1% of Kansas taxable equity to .2%, and raised the annual maximum tax liability cap from $2,500 to $5,000.

The number of business entities subject to the corporate franchise tax has been drastically reduced, as a result of 2004 Senate Bill 147 (which exempted entities with less than $100,000 of Kansas taxable equity) and 2007 House Bill 2264 (which exempted entities with less than $1 million of Kansas taxable equity). The reductions (all estimates) are shown below:

taxable entities prior to 2004 SB 147—80,000
taxable entities after 2004 SB 147—22,000
taxable entities after 2007 HB 2264—7,000

The corporate franchise tax revenues are deposited in the State General Fund. Corporate franchise tax revenue receipts for the past ten fiscal years are shown below:

FY 1999	$15,866,000
FY 2000	$16,834,000
FY 2001	$16,927,000
FY 2002	$18,520,000
FY 2003	$31,089,000
FY 2004	$36,806,000
FY 2005	$47,085,000
FY 2006	$46,880,000
FY 2007	$47,892,000
FY 2008	$46,659,000

The November 2008 Consensus Revenue Estimate forecasts that FY 2009 corporate franchise tax receipts will be $32 million, with FY 2010 corporate franchise tax receipts dropping to $20 million, due to the Tax Year 2009 rate reduction.

The corporate franchise tax rate of .09375% of Kansas taxable equity proposed in House Bill 2028 is actually lower than the rate that was in effect prior to 2002, although the current maximum tax liability cap of $20,000 is higher than the $2500 cap in place prior to 2002. At the .09375% rate, an entity would need to have Kansas taxable equity of $21.33 million before the $20,000 cap would apply.

Fiscal Impact

Enactment of House Bill 2028 should have a positive fiscal impact of $14 million for FY 2010, $26 million for FY 2011, $38 million for FY 2012, and $40 million for FY 2013. Administrative costs to implement this proposal would be absorbed by the Department.

Distribution

We estimate that under House Bill 2028, the distribution of corporate franchise tax liability among the estimated 7000 businesses subject to this tax would be as follows:

Net Worth	Average Tax Liability	Number of Businesses
$1-2.5 million	$1641	3100
$2.5-5 million	$3,515	1925
$5-10 million	$7,031	1000
$10-15 million	$11,719	400
$15-21 million	$16,875	300
over $21 million	$20,000	275

KANSAS ASSOCIATION OF SCHOOL BOARDS
1420 SW Arrowhead Road • Topeka, Kansas 66604-4024
785-273-3600

Testimony before the
House Committee on Taxation
by

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

January 22, 2009

Mr. Chairman, Members of the Committee:

Thank you for opportunity to appear before as a proponent of **HB 2028**. As representatives of Kansas public schools, we understand the magnitude of the budget crisis facing the Governor and Legislature. In making the painful choices necessary to resolve this crisis, we believe that minimizing funding reductions for public education will help minimize both the short-term and long-term damage to the Kansas economy. This bill, which would freeze the phase-out of the corporate franchise tax, is part of the plan proposed by the Governor that makes K-12 education funding a priority.

The Kansas National Education Association has also joined in this statement.

KASB appears as a proponent of this bill because our Delegate Assembly in December adopted a resolution on school finance that included the following statement:

"*Revenues.* If state revenues are inadequate to provide current commitments or enhancements required for student achievement, KASB supports repeal or delay of recent tax reductions, elimination or reducing tax exemptions, or raising tax rates on sales or income."

We believe that tax policy, as well as spending issues, must be part of the solution. As you weigh your choices, please consider the following facts.

Public schools differ from most agencies and local governments in a number of important ways:

- The Kansas Constitution and statutes require school districts to provide every student a free education, including a minimum curriculum and school term, regardless of funding.
- Under the constitution, public schools are managed by locally elected boards, but the responsibility for funding lies with the state, and each child is equally entitled to a quality education as defined by the state, regardless of where the child lives.

- State law requires school accreditation based on improvement in student academic progress; and under No Child Left Behind schools must be increasing student proficiency targets each year.

- A high percentage of school district employees are professionally licensed and have collective bargaining and continuing contract rights.

- School districts are limited on what revenues they can raise and spend locally and differences in local funding options have constitutional implications.

Increased school funding has led to dramatic increases in student achievement.

- As shown in attachment pages 1 through 3, student performance on state tests has increased equal to or greater than increases in funding. The achievement gap for previously low-achieving groups has narrowed dramatically. Performance has also increased on national tests and Kansas' national ranking has improved to among the best in the nation.

- As pages 4 through 6 indicate, performance has improved because schools have effectively targeted new resources on new programs and personnel, which will be at-risk if funding is cut.

- Every part of a school district budget – not just "classroom instruction" – has an impact on student achievement. "Outside the classroom" makes "inside the classroom" more effective.

Major cuts in school funding will have significant economic consequences.

- Educational attainment is the single important factor in personal and social economic prosperity.

- Significant cuts to public education will eliminate high-paying jobs, benefits and purchases in communities across the state. (School jobs have the same impact in their communities as the National Bio- and Agro-Defense Laboratory will have on Kansas.)

- School budget cuts resulting in higher fees for meals, transportation, books, activities, drivers' education, kindergarten and pre-school programs and summer school or enrichment programs will fall hardest on economically struggling families.

We therefore believe tax revenues should be part of solution to the budget crisis.

- While no one wants to pay more taxes, vital public services like public education must be paid for by someone. Reducing or eliminating taxes either reduces the level of education attainment we can provide, or shifts the tax burden to someone else.

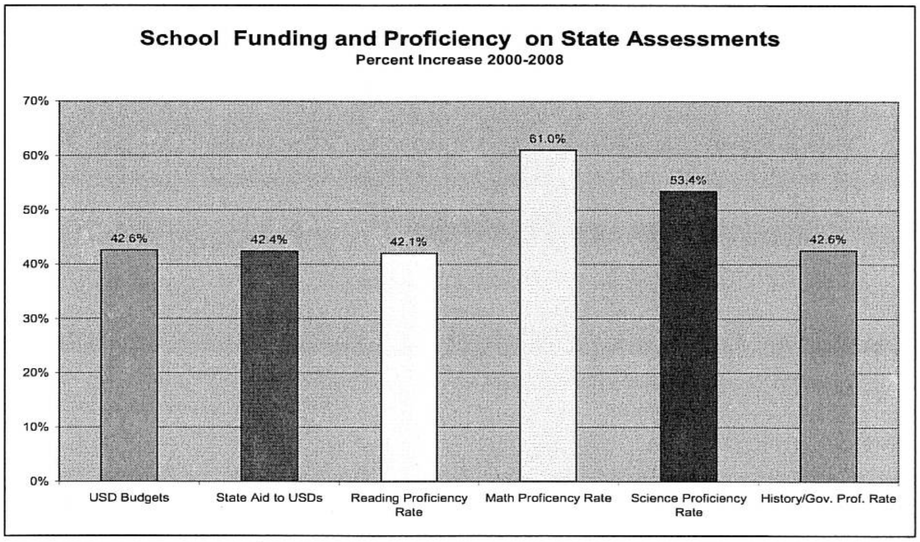
- Business benefits from education through both a more qualified and productive workforce and higher earning consumer. It is reasonable to that business share in the protecting the successful investment in our schools.

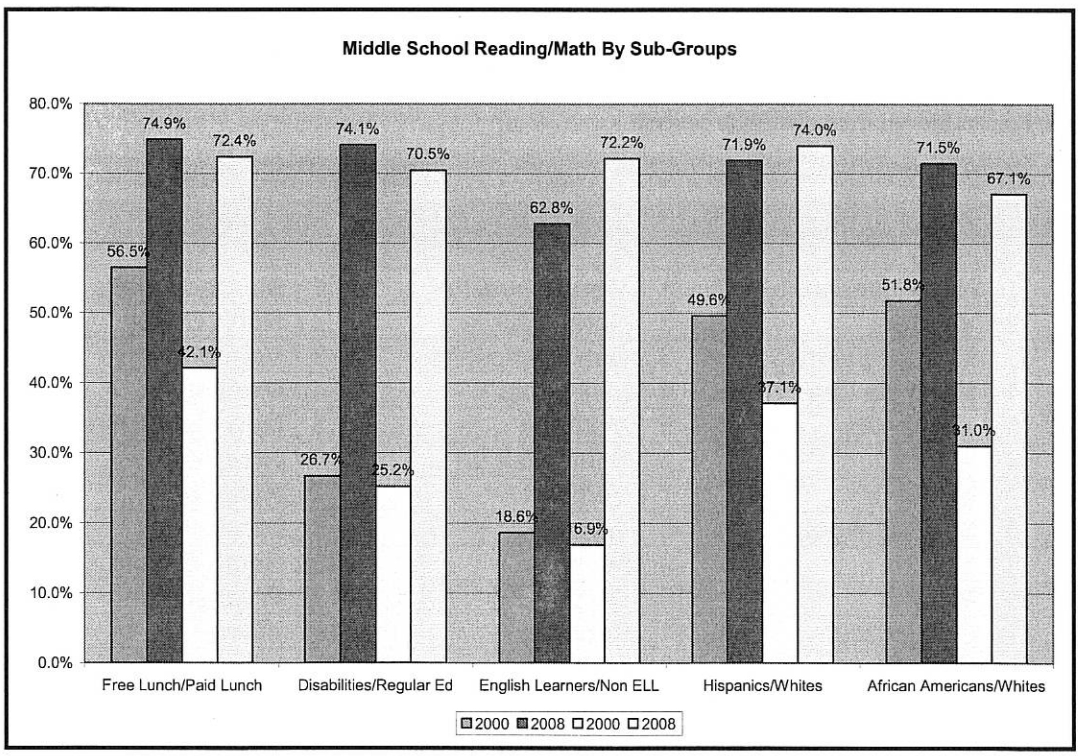
Finally, we continue to urge the Legislature to create a special study to address the long term tax and budget structure of the state.

Student Achievement Increased with Higher Funding

Has increased funding led to better educational outcomes? The 2006 Kansas Legislative Post Audit Outcomes-based cost study found: "A 1.0% increase in district performance was associated with a 0.83% increase in spending – almost a one-to-one relationship. *This means that all other things being equal, districts that spend more had better student performance*….we can be more than 99% confident there is a relationship between spending and outcomes." *(Emphasis added)* The 2008 Kansas Education Report Card demonstrates similar results. Between 2000 and 2008, the percent of students scoring proficient or above on state assessments increased at least as much as school district funding.

A key focus of the lawsuit was the deep disparity in achievement between certain low achieving student groups and their peers. Much of the new funding was successfully targeted to narrow these achievement gaps. For example, in 2000, the proficiency rate of free lunch middle school students was only 57% of the paid lunch students in reading and 42% in math. By 2008, they were over 70%. Other groups had even larger gains.

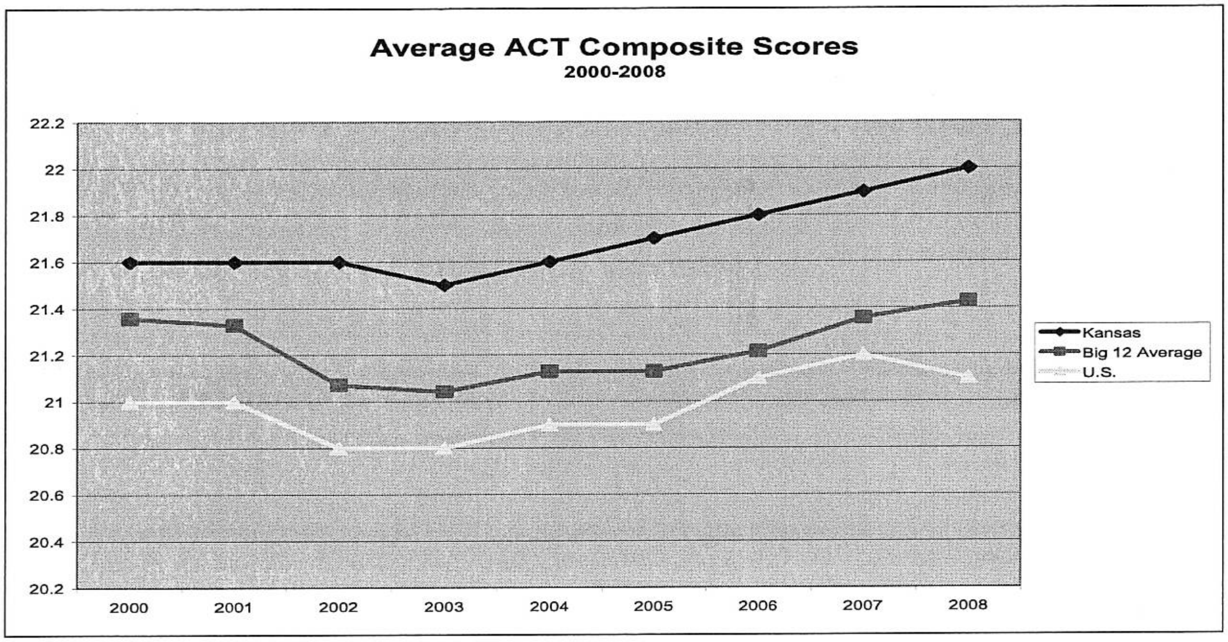




4-3

Kansas and National Education Achievement

How does improving student achievement compare with other states? One common measure of student achievement is the ACT test for high school seniors. Kansas scores have improved annually since 2003, with Kansas ranking well above the national average. Kansas also scores well above the average of states with "Big 12" universities (Colorado, Iowa, Kansas, Missouri, Nebraska, Oklahoma and Texas). Kansas also tests over 75% of high school seniors, one of the highest rates in the nation.



Another measure of achievement is the National Assessment of Education Progress (NAEP). Since 2003, all states have participated in the NAEP reading and math tests, which are given every other year to a sampling of students at fourth and eighth grade. By combining those scores, an overall national ranking can be determined. Over the past four years, Kansas moved from twelfth to seventh.

Top Performing States on the National Assessment of Education Progress					
	2003		2005		2007
1	New Hampshire	1	Massachusetts	1	Massachusetts
2	Vermont	2	North Dakota	2	North Dakota
3	Massachusetts	3	New Hampshire	3	Vermont
4	North Dakota	4	Minnesota	4	Montana
5	Minnesota	5	Montana	5	New Hampshire
6	Wyoming	6	South Dakota	6	New Jersey
7	Montana	7	Vermont	7	Kansas
8	South Dakota	8	Wyoming	8	Minnesota
9	Iowa	9	Maine	9	South Dakota
10	Maine	10	Delaware	10	Wyoming
11	Connecticut	11	Kansas	11	Maine
12	Kansas	12	New Jersey	12	Iowa

4-4

How does Kansas compare to states in the region? Kansas combined scores and national ranking now leads all our neighboring and "Big 12" states.

Kansas and Regional Ranking by combined NAEP Scores					
2003		2005		2007	
State, National Rank	Score	State, National Rank	Score	State, National Rank	Score
Iowa (9)	308%	Kansas (11)	309%	Kansas (7)	323%
Kansas (12)	304%	Iowa (14)	306%	Iowa (12)	318%
Colorado (18)	298%	Nebraska (19)	303%	Colorado (21)	306%
Missouri (20)	297%	Colorado (23)	295%	Nebraska (23)	304%
Nebraska (21)	297%	Texas (26)	292%	Texas (24)	304%
Texas (30)	281%	Missouri (27)	292%	Missouri (28)	296%
Oklahoma (36)	273%	Oklahoma (38)	274%	Oklahoma (35)	285%

How does Kansas compare on international measures? Two states (Massachusetts and Minnesota) participated in the 2007 Trends in International Mathematics and Science Study. Those two states scored well above the results for the United States as a whole. Although Kansas did not participate in the TIMSS, on the 2007 National Assessment of Education Progress math test, Kansas compared favorably with the two states that did. Along with Kansas, both states were in the top five states on the 2007 NAEP. The results suggest that Kansas students are more competitive than most other states.

Kansas Compared To High Ranking States on International Math Test

Table shows average scale scores for countries above the international average on the 2007 Trends in International Mathematics and Science Study (TIMSS). Two U.S. states, Massachusetts and Minnesota, were also "benchmarking" participants. The scores and national ranking of these two states on the 2007 National Assessment of Education Progress (NAEP) mathematics test, are listed along with Kansas math scores and national ranking.

Fourth Grade Math

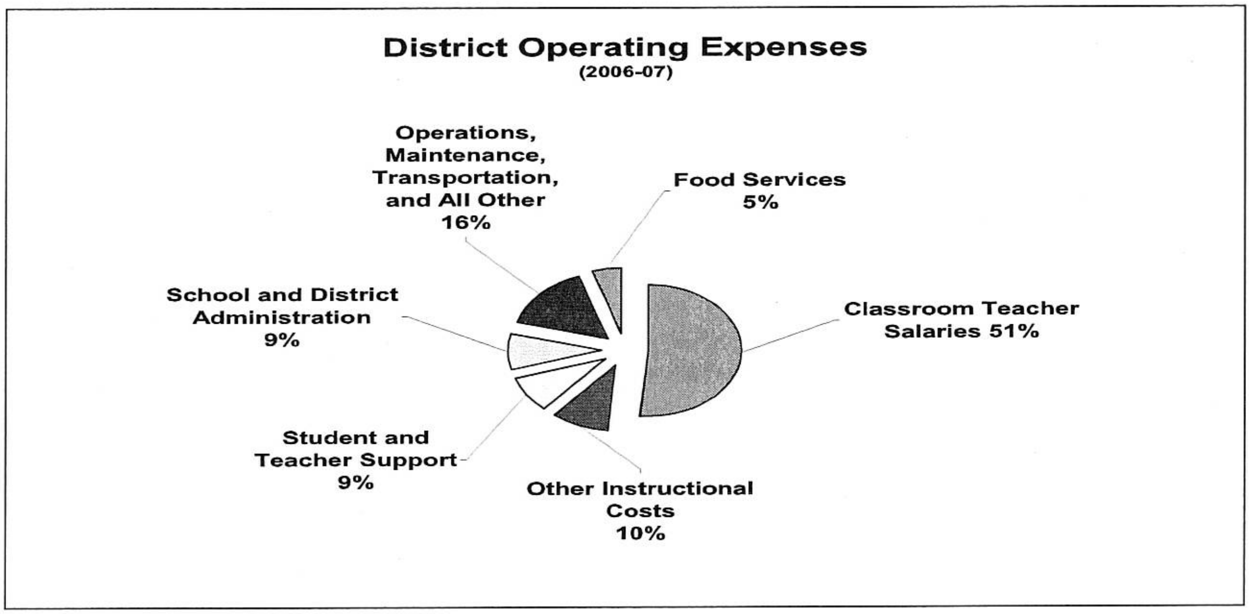
TIMSS		NAEP (National Rank)	
Hong Kong	607		
Singapore	599		
Chinese Taipei	576		
Massachusetts	572	Massachusetts (1)	252
Japan	568	**Kansas (3)**	**248**
Minnesota	554	Minnesota (5)	247
Kazakhstan	549		
Russian Fed.	544		
England	541		
Latvia	537		
Netherlands	535		
Lithuania	530		
United States	529	U.S. Average	239
(8 other countries)			
International Ave.	**500**		

Eighth Grade Math

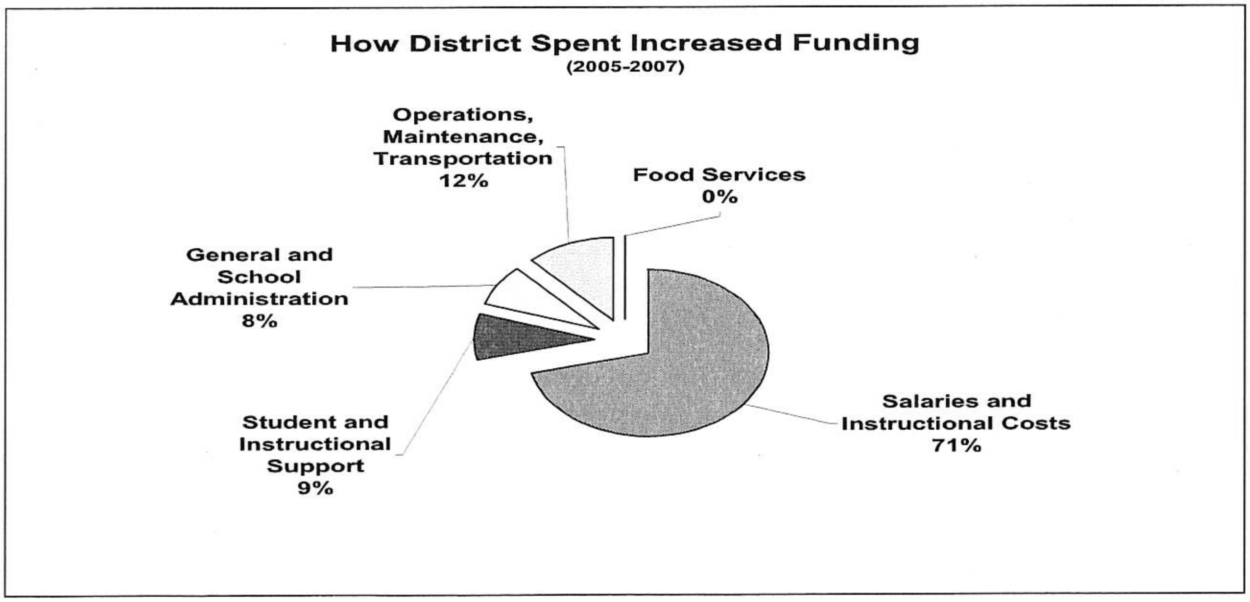
TIMSS		NAEP (National Rank)	
Chinese Taipei	598		
Korea	597		
Singapore	593		
Hong Kong	572		
Japan	570		
Massachusetts	547	Massachusetts (1)	298
Minnesota	532	Minnesota (2)	292
Hungary	517	**Kansas (5)**	**290**
England	513		
Russian Fed.	512		
United States	508	U.S. Average	280
Lithuania	506		
Czech Republic	504		
Slovenia	501		
International Ave.	**500**		

School District Spending Supports Achievement

How do Kansas school districts spend their resources to get high and improving student outcomes? Over half of school district operating budgets (including local option budgets but excluding equipment, land, capital outlay and bond and interest payments) statewide goes to classroom teacher salaries and benefits, with another 10% percent for other instructional costs, such as books and teacher aides. Eighteen percent is spent on district and school leadership and programs to support students and teachers. School meals account for 5%. The balance goes to all other expenses, including utilities, building maintenance, safety and security, and student transportation.



How have districts spent "new" funding? A recent Kansas Legislative Post Audit review of how districts spent new funding received from the state since 2005 found that 71% went to instruction.



Impact of Potential School District Budget Reductions

The following are potential areas for school district budget reductions if state funding is reduced. While each proposal will reduce current expenditures, each must also be evaluated in terms of legal requirements, impact on student achievement and other issues. It should also be noted that any reductions in school staff, salaries and purchases will have that same negative economic impact as job and spending cuts in the private business sector.

Instruction (62% of current operating budgets)	
Increase pupil-teacher ratios as a result of reduced teaching staff.	• *Legal:* Boards must notify teachers of non-renewal by May 1. Tenured teachers have right to due process hearing before independent hearing officer, with cost paid by district. Subject to certain exceptions, teachers must be paid through that process (which often takes months and significant legal expenses). • *Achievement:* Additional staff improves learning through smaller classes and additional time for at-risk students.
Reduce non-essential travel such as student field trips.	• *Achievement:* Limits supplemental educational opportunities for students. • *Other:* Produces minimal savings.
Reduce instructional supplies.	• *Achievement:* Limits teacher resources (paper, copies, workbooks, activities). • *Other:* Produces minimal savings.
Reduce or eliminate before and after school and summer programs.	• *Achievement:* These programs provide needed additional time and specialized attention for struggling students or enrichment, without diverting teacher time from other students.
Delay textbook and computer purchases.	• *Achievement:* Over time, can result in students learning from out-of-date textbooks and obsolete technology.
Reduce number of teaching days to minimum required by law.	• *Legal:* Districts must offer a school term of at least 186 days or 1,116 hours. Many districts currently provide for a longer year. • *Achievement:* Reducing days or hours limits instructional time; lengthens summer vacation periods and may require more "re-teaching" after break; more difficult to cover curriculum.
Reduce or eliminate early childhood education programs.	• *Legal:* Districts are required to provide half-day kindergarten and special education for 3-5 year-olds. • *Achievement:* Growing evidence supports the long-term effectiveness of early education.
Student Support Services (5% of current operating budgets)	
Reduce positions such as nurses, counselors, social workers.	• *Legal:* Schools must provide certain services to qualifying special education students. • *Achievement:* Students with physical or mental health issues are less likely to meet academic standards. Districts also use support staff to reach students and their families to promote attendance and parental involvement.
Instructional Support Services (4% of current operating budgets)	
Reduce professional development for teachers.	• *Legal:* Districts are required to provide professional development programs for licensed staff, regardless of state aid for this purpose. • *Achievement:* Gains in student achievement have resulted from helping teachers improve teaching strategies and collaboration. 2010 Commission placed high priority on staff development.
Reduce instructional support such as reading coaches, paraprofessionals, etc.	• *Achievement:* New positions in many districts have helped teachers be more effective in designing and delivering classroom instruction.
Delay library and media/technology purchases.	• *Achievement:* Over time, affects quality of educational programs. • *Other:* Produces minimal savings.

4-7

General Administration Support Services (3% of current operating budgets)	
Reduce central office personnel.	• *Legal:* Cutting these positions can reduce the effectiveness of required activities such as financial oversight, planning and evaluation, state and community reporting and other compliance functions and public outreach. • *Achievement:* 2010 Commission placed high priority on leadership.
Reduce professional and board travel and development.	• *Achievement:* Loss of continuing education on student achievement and effective management.
School Administration Support Services (6% of current operating budgets)	
Reduce principal and assistant principal positions.	• *Achievement*: Affects instructional leadership, teacher evaluation and support for school safety, student discipline and activities, and parent involvement. 2010 Commission placed high priority on leadership.
Operations and Maintenance (10% of current operating expenses)	
Reduce custodians and maintenance personnel.	• *Other:* Can result in long-term deterioration of school facilities.
Close buildings if possible.	• *Other:* May have negative impact on communities and neighborhoods.
Reduce security/resource officers.	• *Other:* Positions may seem expendable – until the next school tragedy.
Transportation (4% of current operating expenses)	
Delay bus purchases.	• *Other:* May provide short-term savings, but must be made up eventually; possibly at greater cost.
Discontinue transporting students not required by law or charge fees.	• *Legal:* Districts must provide transportation only for students living more than 2.5 miles from schools. Other students are often bussed for student safety. • *Achievement:* Cutting bus service may increase tardiness and truancy, especially for students whose parents or guardians lack transportation. • *Other:* Imposing transportation fees can be a hardship for parents.
Food Service (5% of current operating expenses)	
Reduce food service workers.	• *Legal:* State law requires most schools to provide breakfast programs. • *Other:* Cutting food service staff could result in less student participation and reduce revenues, offsetting savings.
Increase lunch fees.	• *Other:* Hardest impact on struggling families.
All Areas	
Fund programs from contingency reserve.	• *Other:* One-time revenue source; many districts have little or no contingency reserve. (Others are criticized for having too much money in contingency reserves or other balances.)
Reduce health insurance benefits.	• *Legal:* May require agreement by teachers. • *Achievement:* Over time, makes school employment less competitive in recruiting high quality personnel.
Provide minimum salary increases.	• *Legal:* May require agreement by teachers. • *Achievement:* Over time, makes school employment less competitive in recruiting high quality personnel.
Consolidation of school districts.	• *Legal:* Consolidation of two or more districts requires public vote. • *Other:* Most savings only occur with closing of buildings; may be offset by other costs such as guaranteed state aid incentives.

FISCAL FOCUS

Budget and Tax Policy in Perspective

April Holman, Director of Economic Policy
Kansas Action for Children
House Taxation Committee
January 22, 2009
Legislative Testimony - HB 2028

Good morning Chairman Carlson 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 HB 2028.

KAC is a not-for-profit child advocacy organization that has been in existence since 1979. We work to promote policies that improve child well-being in the areas of health, education and family economic success. Several years ago KAC developed Fiscal Focus as part of this work to improve the economic security of Kansas children and their families, and ensure a balanced and fair tax system and budget process that promotes both the well-being of children and families and provides a stable system of state revenues.

We stand in support of HB 2028 and ending the phase out of the franchise tax. Our support of this policy is not a reflection of the value we place on the business community in Kansas. Instead it is a very practical acknowledgement of the extremely difficult fiscal situation in our state. In order to pass a balanced budget for fiscal year 2009 and 2010 state expenditures must be cut or revenues must be found to meet spending needs.

The budget shortfall that we face is not entirely a function of a struggling economy. We know that our state's current tax structure is no longer keeping pace with public infrastructure costs. Although major components of the Kansas tax structure have been in place for quite some time, the strength of our tax policy has eroded little by little through legislative action each year. In the past four years alone, tax cuts including the elimination of the estate tax and the franchise tax have resulted in a State General Fund revenue reduction of almost $150 million in this fiscal year alone. This cut in the tax base grows to $180 million dollars in fiscal year 2010.

At the heart of this process is an analysis of the priorities of our state. In this year of extremely difficult decisions, we believe that adequate funding for education, healthcare and other important programs for children and families is more important to the people of Kansas than further tax cuts for businesses. The resources we dedicate to our next generation this Session will determine whether Kansas has a short-term economic problem or a long-term crisis.

Without legislative action, the franchise tax will be eliminated entirely in 2010, taking with it an estimated $26 million dollars from the State General Fund. While that might have been feasible several years ago, this is not the time to eliminate entire sources of revenue to the State General Fund. We urge your support of HB 2028.

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Lenexa Chamber of Commerce

The Historic Lackman-Thompson Estate
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Lenexa, KS 66219-1236
913.888.1414
Fax 913.888.3770
www.lenexa.org

TO: Representative Richard Carlson, Chairperson
Members, House Taxation Committee

FROM: Ashley Sherard, Vice-President
Lenexa Chamber of Commerce

DATE: January 22, 2009

RE: **HB 2028—Continuation of Kansas Franchise Tax**

The Lenexa Chamber of Commerce would like to express its concern regarding HB 2028, which would continue the Kansas franchise tax at 2008 levels rather than phase it out according to the statutory schedule previously approved by the legislature.

Businesses have faced particularly difficult economic challenges in recent years, and the state's unfair franchise tax contributes yet another burden at a time when the viability of many businesses is at a crossroads. We believe the legislature's planned repeal of the franchise tax was a key step in the right direction, saving Kansas employers millions of dollars a year, helping to prevent additional job loss and encouraging the economic recovery and competitiveness that will provide jobs and revenue to the state over the long-term.

But the state is facing an historic budget deficit, and we understand that every Kansan will need to contribute to the solution. We hope the legislature will not find it necessary to suspend previously approved tax cuts – which we believe could help spur the economy at this critical time – but if so, we are concerned that HB 2028 appears to continue the franchise tax at 2008 levels indefinitely.

If the committee intends to move the bill out favorably, **the Lenexa Chamber of Commerce strongly urges that it first be amended to contain a sunset or a date certain when the franchise tax phase-down will continue.**

Thank you for your time and consideration of this important issue.

KANSAS LIVESTOCK ASSOCIATION

Since 1894

TESTIMONY

To: The House Committee on Taxation
Rep. Richard Carlson, Chairperson

From: John Donley

Date: January 22, 2009

Subj: **House Bill 2028 –**Continuation of the franchise tax.

> *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, dairy production, grazing land management and diversified farming operations.*

The Kansas Livestock Association opposes HB 2028.

The franchise tax is essentially a tax on the privileges of doing business in Kansas. It is paid by foreign and domestic corporations, associations, limited liability companies, and limited liability partnerships.

In 2007 the Kansas Legislature began the process of phasing out the state franchise tax. At that time, many Kansas businesses were paying a much larger amount in franchise taxes due to legislative changes that had increased the exemption amount, but had also increased the maximum amount paid by an individual entity. The earlier changes had resulted in many mid-sized operations in the state having a significantly higher franchise tax.

Many Kansas businesses, including KLA members, have created corporations or limited liability companies or partnerships for liability protection. This is a technique that attorneys and tax practitioners have recommended and utilized for years in business planning. Additionally, many businesses have multiple business entities that make up their entire business structure for a multitude of reasons.

There are numerous reasons that Kansas needs to continue down the path of phasing out this tax. First, the franchise tax is a burden on Kansas businesses

House Taxation Committee
1-22-09
Attachment 7

6031 SW 37th Street • Topeka, KS 66614-5129 • (785) 273-5115 • Fax (785) 273-3399 •

that competitors in many other states do not have to bear. The tax penalizes Kansas businesses for making investments in Kansas. Additionally, the tax applies disproportionately due to the structure of the business. Finally, the franchise tax is levied upon a business regardless of the profitability of the business due to the fact that it is assessed on the assets a business owns.

In production agriculture, net worth is built up in order to make it through tough economic times such as the current economic situation. A tax on an entity's net worth discourages savings to help make it through tougher economic periods. Essentially, the franchise tax penalizes well run businesses for planning ahead.

It is also important to remember that industries such as the cattle feeding and dairy industry are quite fluid and can be moved if a state's business climate is not conducive to continuing operations in that state. The cattle feeding industry is extremely important to Kansas and is the economic driver in many regions of the state. The legislature needs to ensure that the business climate continues to provide incentives to keep the industry in this state.

The business structures of KLA members are as varied as the business structures in any other industry. Our members have continuously voiced their displeasure with the franchise tax over the years. The tax is fundamentally unfair and is applied in a manner in which there are gross inequities created based on an entity's business structure.

HB 2028 is an attempt to continue the franchise tax into the future. KLA asks that you oppose any efforts to continue the franchise tax, and we encourage you to support the current phase out of the estate tax in 2011.

Thank you.

achieve more

Testimony before the House Committee on Taxation
HB 2028 – Repeal of the Franchise Tax Phase Out
Presented by J. Kent Eckles, Vice President of Government Affairs

Thursday, January 22nd, 2009

The Kansas Chamber of Commerce appreciates the opportunity to submit testimony in opposition to House Bill 2028, which would repeal the Franchise Tax Phase-out passed during the 2007 Legislative Session.

House Bill 2028 would freeze in perpetuity the 2008 corporate franchise tax rate at .09375% and cap taxes at $20,000 for companies with assets in excess of $1m. Under the enabling legislation of 2007, the rate would have dropped to .0625% in 2009 and .03125% in 2010 before being phased out altogether for 2011 and beyond.

The franchise tax is one companies pay simply for the privilege of doing business in the State. It is a tax on companies' net worth or "success tax." Further, there are no offsets for corporate subsidiaries, which must pay the full franchise tax and are thus penalized under Kansas law.

In our annual CEO Poll of 300 Kansas businesses taken in September 2008, when respondents were asked what issues were the most important to their profitability, "lower taxes on businesses" was the second most selected response to "reducing fuel and energy costs."

Each year the Kansas Chamber commissions the Annual Competitive Index to measure Kansas' performance against its peer states (all surrounding states plus Iowa) by comparing nearly 80 metrics that measure the State's business and economic climate. When the State's business tax structure was measured, after some slippage in 2004 & 2005, the State improved in ranking in 2006 and 2007 as a result of eliminating the business machinery and equipment property tax in 2006 and phasing out the franchise tax in 2007. However, at a rank of 38 nationally, Kansas is still surpassed by all of its peers except Iowa, which ranks 45 nationally.

It would be unfortunate if the State's business tax structure were to regress after seeing positive gains thanks to the legislature over the past three sessions. Repealing the recently passed franchise tax phase out will only serve to exacerbate the competitive disadvantage and hurt investment and job creation in the State.

The Kansas Chamber, with headquarters in Topeka, Kansas, is the leading statewide pro-business advocacy group moving Kansas towards becoming the best state in America to live and work. The Chamber represents small, medium, and large employers all across Kansas. Please contact me directly if you have any question regarding these comments.

THE KANSAS CHAMBER

835 SW Topeka Blvd. Topeka, KS 66

House Taxation Committee
1-22-09
Attachment 8

NFIB

The Voice of Small Business®

House Taxation Committee
Daniel S. Murray: State Director, NFIB-Kansas
Comments on HB2028
January 22, 2009

Taxes that are too high, and a tax system that is ridiculously complex, stand in the way of small business growth.

Mr. Chair, Members of the Committee: My name is Dan Murray and I am the State Director of the National Federation of Independent Business-Kansas. NFIB-KS is the leading small business association representing small and independent businesses. A nonprofit, nonpartisan organization founded in 1943, NFIB-KS represents the consensus views of its 4,000 members in Kansas. Thank you for the opportunity to comment on HB2028.

NFIB-KS recognizes the severity of the state's economic crisis. Our members appreciate the legislature's difficult task of balancing the state's budget. If anyone can understand the challenge of balancing income and expenses, it's small and independent businesses. Further, we fully understand that "desperate times call for desperate measures," and that you must consider every option.

However, NFIB-KS and its 4,000 members oppose HB2028. HB2028 simply repeals the corporate franchise tax phase-out. There is no provision to sunset this freeze, nor is there a trigger to restart the phase-out. We believe that a repeal of the franchise tax phase-out could negatively impact the promotion of small business growth.

Our members have overwhelmingly supported previous legislation to phase-out the franchise tax. In one poll, 77% of our members that voted were in favor of repealing the state corporate franchise tax. We believe that the legislature must do all it can to ensure Kansas' business tax climate stimulates job creation and capital investment, particularly in a recession.

Increasing costs of healthcare, transportation, etc. are already taking their toll on small businesses. The last thing that small businesses need is an uncertain and confusing tax climate.

Thank you for the opportunity to comment on HB2028.

National Federation of Independent Business – KANSAS
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EMBARQ™
Embarq Corporation
EMBARQ.com

Before the House Taxation Committee
HB 2028
Michael R. Murray, Embarq
January 22, 2009

Mr. Chairman and Members of the Committee:

Thank you for the opportunity to comment on HB 2028 which would repeal the phase out of the corporate franchise tax enacted by the Legislature in 2007 by freezing the rate at its 2008 level of .09375%.

Embarq has 22 separate entities which recently have been subject to the Kansas franchise tax . As a result of this legislation Embarq has seen a reduction of about $17,000 in franchise taxes thus far.

If this legislation passes Embarq will see no further reduction and will continue to pay about $250,000 in franchise taxes.

In order for Embarq to receive any further significant benefit from the 2007 legislation, the franchise tax rate would have to be at zero because so many of our companies are paying the maximum franchise tax of $20,000 per year.

Respectfully, we ask that you reject HB 2028.

I'd be pleased to respond to questions.

Wichita Independent Business Association

THE VOICE OF INDEPENDENT BUSINESS

Kansas House Taxation Committee
Testimony in opposition of:
House Bill 2028
January 22, 2009

Presented by Natalie S. Bright

Chairman Carlson and honorable committee members:

Thank you for the opportunity to appear before you in opposition to HB 2028, which proposes to repeal the phase out the corporate franchise tax. I am appearing on behalf of the members of the Wichita Independent Business Association (WIBA), who worked for many years to eliminate the corporate franchise tax in Kansas because it is a tax on net worth, disproportionately taxes small businesses and serves as a disincentive to growing a business in Kansas.

WIBA members are sensitive to the severe budget deficits the state is experiencing because many of our members are having similar declines in their revenue and are struggling to remain competitive in this uncertain economy. Retaining the corporate franchise tax in an effort to fix the state budget will only create an even bigger financial burden for struggling Kansas businesses and discourage capital investment at a time when the state needs it most. By our best estimates, if HB 2028 is passed, almost 25 ~~63~~% of our membership will be negatively impacted by this proposed repeal. I am attaching testimony offered by Pete Schrepferman, a WIBA member, during the 2007 Legislative Session which highlights the negative impact franchise tax has on his small business in Kansas.

While the members of WIBA encourage you to oppose HB 2028, they do sympathize with the quandary this Legislature is facing. Yet in a recession, the worst thing the State can do is to increase taxes on Kansas businesses because they are our very source for creating jobs, making investments and stimulating the Kansas economy. If you increase their tax liability, you will leave them with a smaller cash flow to keep their doors open. The members of WIBA ask the state to join us in our efforts to trim our budgets, tighten our belts and develop policies and business practices that will afford us the ability to remain competitive in both the good and bad economic times.

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Wichita Independent Business Association

THE VOICE OF INDEPENDENT BUSINESS

Kansas House Taxation Committee
Testimony in support of:
House Bill 2031

By:
Pete Schrepfermann, Past Chairman
Wichita Independent Business Association
Kansas Independent Business Coalition
445 N Waco, Wichita, KS 67202
Phone 316 267 8987 – Fax 316 267 8964

Chairman Wilk and Honorable Committee members:

Thank you for the opportunity to appear before you in favor of HB 2031, which proposes to repeal the Kansas franchise tax. My name is Pete Schrepfermann and I am the past chairman of WIBA/KIBC. I am the owner of Johnstone Supply, an air conditioning and refrigeration distributor.

For several years, the members of WIBA and KIBC have advocated for the elimination of the franchise tax because we believe it is an anti-business tax that disproportionately burdens small business. It also penalizes Kansas businesses for making investments in our state. Franchise tax is levied whether a business is profitable or not because it is assessed against a businesses net worth. Similar types of businesses, when organized differently, pay widely varying amounts. For instance, a business that needs little capital, such as a lawyer or doctor, will typically pay little franchise tax. However, businesses such as machine shops, manufacturers, distributors, require heavy capitalization and therefore pay a significant amount in franchise tax. Some have made the analysis that the franchise tax is in essence a form of property tax on Kansas corporations.

For our small business owners, much if not all of their personal net worth is invested in their business. For instance, I started my business in 1981. We have built our equity to slightly under $900,000, which resulted in a franchise tax for 2006 of $1,084; in addition to our corporate income taxes and personal income taxes. Thus, the franchise tax is in essences a tax on my life savings. To illustrate how much this tax is slanted against small businesses, compare our payment with a large corporation whose equity is hundreds of times greater than ours yet their franchise tax is capped at $20,000.

Great strides have been made over the past few years with the phasing out of the business machinery and equipment tax and the Kansas estate tax. The members of WIBA/KIBC are pleased that the Kansas Legislature is looking at eliminating this tax and getting serious about removing another impediment to economic development in Kansas. Kansas is in the minority as a state that employs a franchise tax. We urge you to support the passage of HB 2031. Thank you for considering our position.

Presentation to the House Taxation Committee
January 22, 2009

By Kenneth L. Daniel
Executive Director, Topeka Independent Business Association
Chairman, Midway Wholesale, Topeka
Publisher, KsSmallBiz.com

Mr. Chairman and Members of the Committee:

My name is Kenneth Daniel. I am the Chairman of the Board of Midway Wholesale, a building materials distributor headquartered in Topeka with branches in six other Kansas Cities and one in Grand Island, Nebraska. I am also the volunteer Executive Director of the Topeka Independent Business Association, and publisher of KsSmall.Biz.com.

I strongly encourage you to oppose this bill. It is a breathtakingly anti-small business bill.

The Franchise Tax is an aggressively anti-business tax. It is basically a penalty for making permanent business investments in the state. Only 19 states have a franchise tax. Until now there were two more states that were phasing it out.

The Franchise Tax:

It is a highly unfair tax, levied whether a business is profitable or not.

The Kansas version is heavily targeted to small businesses.

Identical businesses, organized differently, pay widely varying amounts. Businesses that need little capital—doctors, lawyers, and service providers, for instance—pay little tax. Businesses that require heavy capitalization—banks, medium to large contractors, manufacturers, transportation, and distribution—pay a lot of tax.

For most small business owners, much or all of their personal net worth is invested in their business, so this tax is nothing less than a tax on their life savings.

What is the Franchise Tax?

The tax is levied on the net worth of corporations and limited liability partnerships. The "franchise" in the name of the tax refers to the right to operate in Kansas as a limited liability entity. (At least theoretically, the business can be sued, but the stockholders, owners, management and employees are protected from liability arising out of the business.)

The franchise tax is not imposed on sole proprietorships or standard partnerships. The owners of those types of businesses, which constitute 79% of all businesses in the U.S., do not enjoy limited liability protection. The individuals and the businesses are one and the same, and the owners' personal assets are at risk in lawsuits and government seizures.

Comparison to Other States in the Region

If this passes, Kansas businesses will have to pay $.9375 per thousand, capped at $20,000 in tax, which equates to $21,333,000 in net worth.

The Oklahoma version, at $1.25 per thousand, is capped at $20,000 of tax, which equates to a $16,000,000 net worth.

The Missouri version, at $.33 per thousand, applies only to the portion of corporate net worth in excess of $1 million, thereby eliminating this tax for most small businesses. The Missouri version is more of tax on medium and large businesses.

The Nebraska version, at $.12 per thousand, is capped at $11,995 of tax ($15,000 for out-of-state corporations) which equates to $100,000,000 of net worth, making it the same percentage for almost all businesses in the state, and enabling the rate to be kept very low.

Colorado and Iowa, like many other states across the nation, do not have this tax at all.

Comparison to Other States Nationwide:

Of the nineteen states that have a stand-alone franchise tax, Kansas has the tenth highest tax rate. At $20,000, Kansas is tied for the fourth lowest "cap" or maximum. Ten of the nineteen states have no "cap" at all. With Kansas' combination of a low cap and a high rate, Kansas still has the distinction of having one of the most regressive franchise taxes in the nation.

This anti-small business tax needs to be allowed to die its scheduled death.

KANSAS FARM BUREAU
The Voice of Agriculture

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PUBLIC POLICY STATEMENT

HOUSE COMMITTEE ON TAXATION

RE: HB 2028 – an act relating to the franchise tax; rates and continuation.

January 22, 2009
Topeka, Kansas

Testimony provided by:
Brad Harrelson
State Policy Director
KFB Governmental Relations

Chairman Carlson and members of the House Committee on Taxation, thank you for the opportunity to share our member policy and opposition to HB 2028. I am Brad Harrelson, State Policy Director—Governmental Relations for Kansas Farm Bureau. KFB is the state's largest general farm organization representing more than 40,000 farm and ranch families through our 105 county Farm Bureau Associations.

In 2007 Kansas Farm Bureau supported repeal of the Kansas franchise tax. Aside from the issue of fundamental fairness, there were a host of economic and tax policy reasons why the Legislature took affirmative action and passed legislation to phase out this tax.

Everyone can agree that it is in the state's best interest to have a healthy, vibrant economy that encourages creation of jobs and wealth. It seems counterintuitive to re-impose a tax that discourages growth and penalizes accumulation of assets. The franchise tax appears to be nothing more than an annual bill for the privilege of doing business in Kansas, unrelated to realized income, profitability, or productivity.

Many farm and ranch operations are structured in a way that meets the definition and threshold of businesses that must pay the tax. Furthermore, it is not uncommon for agricultural businesses to create multiple subsidiaries or related businesses for liability protection. As such, operators may have the additional burden of tax liability for each individual entity.

As you know, modern production agriculture is a very capital-intensive business and it doesn't take a very large operation to exceed the minimum $1,000,000 threshold of net worth as proposed in HB 2028. Unfortunately, farms and ranches operate on very narrow margins compared to investment. In many cases, absorbing the tax is much more burdensome to the bottom line of these family businesses than say a large public company.

Kansas Farm Bureau recognizes the budgetary challenges currently faced by the legislature. You will likely explore many avenues to find new sources of revenue. However, the legislature agreed repeal of this onerous tax was good public policy two years ago. Simply because the state has fallen on hard economic times doesn't change that fact. We believe elimination of the franchise tax will likely have a beneficial fiscal impact. A more favorable tax policy can only help attract new business. Furthermore, elimination of this deterrent to growing assets will stimulate new economic growth, and increased opportunities in a state desperately needing it.

In conclusion, Kansas Farm Bureau respectfully urges your recommendation to not pass favorably HB 2028. Thank you, once again, for the opportunity to appear before you and share the policy of our members. KFB stands ready to assist you as you consider this important measure. Thank you.

GREATER TOPEKA CHAMBER

GO TOPEKA

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Written Testimony: HB 2028
Before the House Taxation Committee
January 22, 2009
By: Christy Caldwell, Vice President Government Relations
Greater Topeka Chamber of Commerce
ccaldwell@topekachamber.org

Mr. Chairman and members of the committee:

The Greater Topeka Chamber of Commerce would like to express our opposition to HB 2028, a bill to repeal the continuation of the phase-down of the franchise tax.

Our state is in an unfortunate budget situation as this fiscal year ends and FY 2010 begins. The state is not alone in this situation. Businesses across the nation face grave financial issues as they see their markets shrink, consumers draw back and access to dollars minimize. Many businesses are challenged to weather this financial storm by cutting their expenses, being forced to reduce their workforce and carefully spending every penny to make the most in difficult times.

At the same time as our state and nation face uncertain times and reduced revenues, there is recognition that recovery can only be achieved by thriving businesses, customers comfortable in purchasing goods and services and confidence restored in financial markets. The federal government is working to institute every means to assist businesses across the country to again, as always, stoke the economic engine to get people back to work, raise confidence and rev up the buying power of the American public and foreign customers. Solutions offered have not included increasing taxes or reducing dollars American companies have to invest in jobs and their companies. Kansas should march along with the federal government, this in not the time to reduce dollars businesses have to invest, grow and hire people. Bringing the franchise tax phase-down to a close in 2009 is shortsighted. In the worst situation consideration should only be given to slow, not eliminate the phase-down.

The Greater Topeka Chamber of Commerce asks the committee not to advance HB 2028. If, after all options considered, there is remains a need to capture additional tax dollars from business, it be only a temporary stall in the phase-down. At that time HB 2028 should be rewritten to reflect a short and temporary stalling to the phase-down timeframe so that the promised tax elimination is completed. The franchise tax is a tax on net worth, closely related to an income tax, which the state already collects from businesses. Past legislators and the governor agreed with the value of eliminating this punitive tax, we urge the committee and the legislature to remain committed.

Thank you for the opportunity to offer our views on HB 2028.