

**House Taxation Committee
Testimony on HB 2747
Kansas Society of Certified Public Accountants**

The Kansas Society of Certified Public Accountants cannot support HB 2747 for the following reasons.

First, the Bill provides that the exemption of business income from Kansas income taxation is phased-in over the time period of 2013 through 2018. This phase-in period provides too much uncertainty for Kansas businesses in assessing how much Kansas income tax liability they will incur from year to year. The phase-in has established "hard dollar" thresholds under which the Kansas small business person's business income will either be taxed or exempted. To make an extreme example, if the taxpayer's federal adjusted gross income is \$99,999 in 2013, his or her business income is exempt from Kansas taxation but if the taxpayer's federal adjusted gross income is \$100,000, his or her business income is fully taxable to the state of Kansas. In these times of economic uncertainty, many taxpayers do not know how much taxable income they will have earned until after the end of the year at which time it is too late to have provided for any planning of the financial affairs.

Second, in today's business environment it is very common for both spouses of a household to be employed outside of the home. If one of the taxpayers is a salaried employee and the other taxpayer in the household conducts a qualified small business, it is very possible that their combined incomes for any given year may fluctuate around the \$100,000 threshold. It is possible that the small business may incur a profit in one year and a loss in another year. Under this Bill, the taxpayers may be taxed on the small business profit but gain no benefit from the small business loss. Please see Attachment A for an example where the taxpayer's can be whip-sawed by this legislation and end up paying more income tax on their small business income than they do today.

Third, this Bill effectively de-couples the taxation of the profits earned by small business from the federal income tax statute. The Bill does not address all of the issues created by the de-coupling measure. Specifically, the taxpayers' basis in pass-through entities (partnerships and subchapter S corporations) and basis in property held by small businesses will ultimately impact the taxation of gain when the partnership interest or subchapter S stock is sold or when the underlying depreciable assets of a small business is sold. Failure to address these two issues creates yet additional tax liability for Kansas taxpayers that they are not subject to today.

The Kansas Society of Certified Public Accountants is in favor of reducing taxes for everyone, in favor of reducing the complexity of our tax system and in favor of growth and prosperity for all Kansas taxpayers. However, we cannot support this Bill due to the complexities created by the de-coupling aspects of this Bill and the establishment of the hard-dollar thresholds which create undue uncertainty for the small business person to effectively budget and finance his or her business, and, as illustrated, results in unintended adverse tax consequences in certain situations.

HB-2747
Analysis of Business Income Provision

	<u>Taxpayer A</u>				<u>Taxpayer B</u>			
	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>Aggregate</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>Aggregate</u>
Federal:								
Business Income	(50,000)	(75,000)	125,000	-	(50,000)	(75,000)	125,000	-
Other income	<u>85,000</u>	<u>85,000</u>	<u>85,000</u>	<u>255,000</u>	<u>185,000</u>	<u>185,000</u>	<u>185,000</u>	<u>555,000</u>
Adjusted gross Income	<u>35,000</u>	<u>10,000</u>	<u>210,000</u>	<u>255,000</u>	<u>135,000</u>	<u>110,000</u>	<u>310,000</u>	<u>555,000</u>
Kansas:								
Business Income	-	-	125,000	125,000	(50,000)	(75,000)	125,000	-
Other Income	<u>85,000</u>	<u>85,000</u>	<u>85,000</u>	<u>255,000</u>	<u>185,000</u>	<u>185,000</u>	<u>185,000</u>	<u>555,000</u>
Kansas Adjusted Gross Income	<u>85,000</u>	<u>85,000</u>	<u>210,000</u>	<u>380,000</u>	<u>135,000</u>	<u>110,000</u>	<u>310,000</u>	<u>555,000</u>