KANSAS ECONOMIC PROGRESS COUNCIL

Kansas Economic Progress Council
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Testimony on Senate Bill 339
Senate Assessment & Taxation Committee
February 14, 2012

Mr. Chairman and members of the committee, thank you for the opportunity to testify. I'm Bernie Koch with the Kansas Economic Progress Council, a statewide not for profit organization of businesses, trade associations, chambers of commerce, and individuals.

Lowering taxes can be an important part of state policies to encourage economic development.

However, other factors that can be encouraged by government have been shown by respected empirical studies to be as important, if not more important, including investment in infrastructure and equipment; human capital and labor efficiency; continuing technological innovation; and reliable legal systems.

We believe there's merit in looking at carefully targeted income tax reductions, but completely eliminating a source that provides almost 45% of our general fund revenue doesn't seem justified.

States without an income tax usually have abundant natural resources or heavy tourism that results in significant state revenue. States without an income tax depend more on sales and property taxes to fund government services. And states without an income tax often have many kinds of other taxes and fees that we don't have in Kansas.

A study released this month by the Institute on Taxation and Economic Policy concludes that residents of "high rate" income tax states are actually experiencing economic conditions at least as good, if not better, than those living in states lacking a personal income tax.

The study says six of the nine non-income tax states are doing worse than average when it comes to economic growth per capita, and five of the nine non-income tax states are doing worse than average in terms of median income growth.

Kansas Economic Progress Council opposes the 2 percent mechanism in this bill that, in effect, acts as a spending lid. In 26 of the past 30 years, the inflation rate in the United States has been above 2%, according to the Bureau of Labor Statistics. Last year, it was 3.2%.

A 2% limitation puts the state in a squeeze.

I believe a limitation would inevitably lead to another raid on the transportation program. Even without a spending lid, we have taken $1.4 billion from those revenues over the past 22 years.

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We suggest it would be beneficial to look at total tax burden. There is a valuable study that was released by the Arkansas State Chamber of Commerce recently that included information about Kansas business tax structure that is very significant. The study was done by Ernst & Young.

The report looks at the total effective tax rate after statutory tax credits on different kinds of businesses in eight states in the region, including Kansas. The eight states are: Arkansas, Kansas, Louisiana, Mississippi, Missouri, Oklahoma, Tennessee, and Texas.

The types of companies considered are corporate headquarters, research and development, durable goods manufacturing, food product manufacturing, renewable energy equipment manufacturing, motor vehicle parts manufacturing, and business support services.

Some of the findings:

- Missouri out-competes all of the other states studied in five of the seven categories.
- Missouri's tax credits average 27%, the highest of the states studied, and have a significant impact on that state's business tax rankings.
- Texas is most competitive in the region for company headquarters and business support services.
- Effective tax rates vary widely in Kansas by business. For example, Kansas business support services have an effective tax rate of 19.7% while durable goods manufacturing has an effective tax rate of 8.1%. Kansas has the highest tax burden in the region for services, but among the lowest for manufacturing.
- Kansas effective tax rate on corporate headquarters is 11 and a half times as great as Texas in this category.

I have included the most important chart in the study at the end of my testimony.

Our Effective Tax Rate on business services is the highest of any Effective Tax Rate in any state in this study on any kind of business. It really sticks out.

I also wanted to speak with you about the impact of no income tax on property taxes. Thirty percent of all local and state taxes in Kansas are property taxes, according to a study by the Institute on Taxation and Economic Policy.

Four of the nine states without an income tax depend more heavily on property taxes for local and state government than Kansas. Alaska is 37 percent, New Hampshire 61 percent, South Dakota 34 percent, and Texas local and state taxes make up 42 percent of the tax burden in that state.

There does seem to be a relationship between not having an income tax and property taxes.

I would conclude by reminding you of the extreme political and financial turmoil surrounding property taxes in the last 25 years.

- For many years, Kansas had a Local Ad Valorem Tax Reduction Fund and a County-City Revenue Sharing Funds as a way to hold down property taxes.
- After reappraisal and classification went into effect in Kansas in the late 1980s, the resulting wild property tax swings caused so much turmoil that a special legislative session was called in December of 1989.
- In the 1990 Republican primary election, Governor Mike Hayden had five challengers, including Wichita real estate executive Nestor Weigand, Jr., who ran because of property taxes. Governor

Hayden won the primary with 44 percent, but he later lost the general election to Governor Joan Finney.

- Governor Hayden readily admitted the property tax changes caused by reappraisal were to blame for his loss. He called it "the kiss of death."
- There was another impact of the property tax turmoil in that 1990 election. The Democratic Party won a majority in the Kansas House of Representatives for only the second time in 100 years.
- In 1992, faced with a school finance lawsuit, the legislature included as part of the financing increased income taxes along with sales taxes to buy down the property tax statewide. That was just 20 years ago
- In the mid-90s, the anti-property tax sentiment was so strong, there was legislation to completely eliminate statewide property taxes for schools by increasing income and sales taxes. Governor Graves became concerned about this loss of balance to the three-legged stool, so he issued an executive order creating the Governor's tax equity task force to conduct a comprehensive review of the tax structure of the state.
- That report established the importance of maintaining the balance between sales, income, and property taxes. It stated:

"The state and local tax system should be balanced and diversified. A diversified tax system offers a blend of economic tradeoffs. Because all revenue sources have weaknesses, a balanced tax system will reduce the magnitude of problems caused by over reliance on a single tax source. It will also result in lower rates on each tax and reduce the pressure of competition from other states that have lower rates for a particular tax."

Thank you for the opportunity to appear today.

Arkansas Chamber of Commerce Tax Study
December 2011

Table 6
State and Local Effective Tax Rates Net of Statutory Credits, by Industry and State

State	Headquarters		Research & Development		Durable Goods Manufacturing		Business Support Services		Food Product Manufacturing		Renewable Energy Equipment Manufacturing		Motor Vehicle Parts Manufacturing	
	ETR	Rank	ETR	Rank	ETR	ETR	ETR	Rank	ETR	Rank	ETR	Rank	ETR	Rank
Arkansas	4.7%	2	9.8%	5	9.2%	4	16.2%	4	5.2%	3	12.5%	4	10.6%	4
Kansas	4.6%	3	12.0%	2	8.1%	6	19.7%	1	7.9%	4	3.0%	7	7.2%	7
Louisiana	6.2%	1	12.7%	1	6.8%	7	14.3%	7	9.8%	2	13.5%	2	12.4%	2
Mississippi	1.5%	7	9.5%	6	10.3%	1	15.0%	6	9.2%	1	14.4%	1	12.0%	3
Missouri	4.1%	6	7.7%	8	5.0%	8	15.0%	5	4.5%	8	6.7%	8	5.9%	8
Oklahoma	4.4%	5	11.4%	3	9.2%	2	18.0%	2	7.2%	6	10.8%	5	8.7%	6
Tennessee	4.6%	4	11.1%	4	9.2%	3	16.8%	3	7.3%	5	9.9%	6	9.2%	5
Texas	0.4%	8	5.4%	7	8.7%	5	13.7%	8	6.5%	7	12.6%	3	13.6%	1
Other States' Avg.	3.7%		10.4%		8.2%		16.1%		7.7%		10.9%		9.3%	

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Institute on Taxation and Economic Policy's 2009 study, *"Who Pays?"*

State	Property tax	Sales tax	Other
Alaska	21%	10%	**53%**
Florida	**37%**	**49%**	**11%**
Nevada	28%	**58%**	**14%**
New Hampshire	**61%**	12%	**8%**
South Dakota	**34%**	**55%**	**8%**
Tennessee	24%	**57%**	**12%**
Texas	**42%**	**46%**	**12%**
Washington	27%	**62%**	**11%**
Wyoming	**37%**	33%	**30%**
Kansas	30%	36%	5%

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