Lenexa Chamber of Commerce

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To: The Honorable Les Donovan, Chairman
Members, Senate Taxation Committee

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

Date: March 7, 2012

Re: SB 376

The Lenexa Chamber of Commerce would like to express its strong opposition to certain components of Senate Bill (SB) 376, a bill that proposes significant changes in state tax policy. In particular, the Chamber would like to express its concern with the bill's proposal to expand the sales tax base by eliminating nearly all sales tax exemptions and extending sales tax to certain previously untaxed services.

First, while the bill apparently retains existing sales tax exemptions for manufacturing machinery & equipment, it is important that other current business-related sales tax exemptions also be preserved. For example, the current sales tax exemption for most construction labor services (including labor services related to the original construction of a building or facility or remodeling of a residence) remains good economic policy for the state. The construction industry is a critical component of the Kansas economy. The exemption on labor services was originally approved to promote development and to provide the market competitiveness necessary to attract and retain this key industry. Removing this exemption would be a significant policy shift in Kansas, raising the price of construction, remodeling, and some public works projects, creating a strong disincentive for businesses and residents to build, expand, or remodel in Kansas (most surrounding states do not tax labor services), dampening the construction industry, and costing the state investment, jobs, and tax revenue.

Second, it is critical that sales tax not be extended to a number of additional services that have not previously been taxed -- particularly the rendering of professional, technical, and scientific services (currently no other state taxes professional services). Although the bill currently exempts certain business-to-business transactions, imposing sales tax on the rendering or furnishing of many services would be poor long-term economic policy for the state, creating a number of detrimental effects including:

- Higher costs for consumers.
- Lower demand for services and production.
- New administrative burdens for both the state and for service providers.
- Harming small businesses that may have to purchase non-exempt services that larger firms can provide internally.
- Harming the competitive position of Kansas service providers against competitors located in the vast majority of states that do not tax services. This bill would make it very difficult to recruit service firms or to retain them in Kansas, resulting in lost capital investment, jobs, and state and local taxes.
- The ripple effect from lost business and jobs would adversely affect almost every other sector of the economy.

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The potential consequences are particularly onerous in the state's forty border counties. Because they require few durable fixed assets, service sector firms can be relatively fluid. This concern is especially true in the Kansas City metro area, where labor and capital flow freely across the state line and competing business opportunities abound on the Missouri side – a state that does not tax services. Because Johnson County accounts for the largest percentage of private sector professional & technical services employment in Kansas (45%, or over 41,000 jobs) and private sector professional & technical services payroll (62%, or over $1.8 billion), we fear adversely impacting Johnson County's economic structure and competitiveness would adversely impact the entire State of Kansas.

The possibility of out-migration and its adverse economic impact is very real:

- In a September 26, 2010, *Wichita Eagle* newspaper article, John Wong, chairman of the Department of Urban and Public Leadership at the University of North Texas in Dallas, noted that no state currently taxes professional services. According to Wong, "The problem is, you don't want to be the one that steps off that cliff because you will run everyone out of your jurisdiction."
- Florida repealed its services tax in 1987, after national advertising agencies refused to advertise in that state. (source: *Kansas City Business Journal* column, September 24, 2010)
- Massachusetts repealed a tax on accounting services after one day of public confusion and criticism. (source: *Kansas City Business Journal* column, September 24, 2010)
- The Kansas legislature also seriously considered this issue in the early 1990s. In the January 25, 1991, edition of the *Johnson County Sun* newspaper, the managing partner of Black & Veatch engineering firm explained,

> "This firm cannot be competitive nationally or internationally with a sales tax on our services. It is a very competitive environment.
>
> Oftentimes the difference between the top three contenders on a major project is just a few percent. A sales tax would put us at a horrible competitive disadvantage.
>
> We might be able to pass on the tax for work done in Kansas, but that represents a small part of our work. We would not be able to pass along the work we do for virtually every state and in 30 countries. Competition won't allow it, and we cannot absorb $12 million.
>
> We would begin to phase out of Kansas."

At a time when promoting economy recovery is critical, we believe the short-term revenue gains Kansas might realize from taxing services would be far outweighed by its long-term costs and losses in capital investment, payroll, taxes, and other economic factors.

For all of these reasons, we strongly encourage the legislature not to recommend SB 376 favorable for passage. Thank you for your consideration.