GROWING THE KANSAS ECONOMY

Governor Brownback campaigned on the "Roadmap for Kansas," a clearly articulated set of goals to move the state forward after a decade of lost jobs. There were two distinct goals in the roadmap related to growing the Kansas economy. One was to increase the net personal income of Kansas families and the second was to increase private sector employment. Another goal discussed often is increasing the capital flow in the state.

In proposing and passing last year's tax reform a few questions needed to be answered and continue to be important going forward.

- What has been the historic economic performance of Kansas?
- Does tax policy matter in economic growth and what policy works best?
- Why do some states prosper economically and others do not?
- What are the best economic growth strategies for a state?

Kansas' Historic Economic Performance

- Lost population – As a percentage of U.S. population Kansas dropped from 29th in 1960 to 33rd in 2010 and is projected to drop to 36th in 2030.
  Source: U.S. Census Bureau

- Between 2004 and 2010, there was a net outmigration from Kansas of 21,259 people with a total adjusted gross income of $1.04 billion.

  - Texas gained the most from Kansas outmigration with 6,395 tax filers from Kansas moving to Texas along with 12,837 dependents and a total adjusted gross income of $305.4 million.

  - Only 10 states out of 50 had worse outmigration than Kansas from 2000 – 2009.

  Source: Kansas Dept. of Labor and Internal Revenue Service

- 2011 Average Annual Private Sector Employment Growth

  Texas = + 17.5%
  Adjacent States = +3.1%
  Kansas = +0.4%
  Source: Tax Foundation

  "The last decade was a lost decade for jobs in Kansas. Fewer Kansans were working in private sector jobs in January 2011 than were in January of 2001. A growing government and a shrinking private sector are not sustainable. Fixing that is our top priority." - Governor Sam Brownback

Status quo is unacceptable. A top priority is policy that will grow the Kansas economy.

Does Tax Policy Matter to Economic Growth and What Policy Works Best?

John F. Kennedy – Speaking in 1962 to the Economic Club of New York – "In short, it is a paradoxical truth that tax rates are too high today and tax revenues are too low. Only full employment can balance the budget, and tax reduction can pave the way to that employment. The purpose of cutting taxes now is not to incur a budget deficit, but to achieve the more prosperous, expanding economy which can bring a budget surplus."

Ronald Reagan – Radio Address to the Nation – 1982 – "I know you have been told by some that we should do away with the tax cuts in order to reduce the deficit. That's like trying to pull a game out in the fourth quarter by punting on third down."

Recently the Tax Foundation posted a paper titled, *What Is the Evidence on Taxes and Growth?* The special report was written by William McBride, PhD, chief economist for the Tax Foundation. The following are quotes from the report and some of the summary information on other studies contained in the report.

"While there are a variety of methods and data sources, the results consistently point to significant negative effects of taxes on economic growth even after controlling for various other factors such as government spending, business cycle conditions, and monetary policy. In this review of the literature, I find 26 such studies going back to 1983, and all but three of those studies, and every study in the last 15 years find a negative effect of taxes on growth. Of course those studies distinguish between types of taxes. Corporate income taxes are found to be most harmful, followed by personal income taxes, consumption taxes and property taxes.

"If we intend to increase employment, we should lower taxes on workers and businesses that hire them.

"This review of empirical studies of taxes and economic growth indicates that there are not a lot of dissenting opinions coming from peer-reviewed academic journals. More and more, the consensus among experts is that taxes on corporate and personal income are particularly harmful to economic growth, with consumption and property taxes less so. This is because economic growth ultimately comes from production, innovation and risk-taking."

Sampling of Empirical Studies on the Effects of Taxes on Economic Growth

Reference	Summary of Findings
Karel Mertens & Morten Ravn, The dynamic effects of personal and corporate income tax changes in the United States. AMERICAN ECONOMIC REVIEW (2012)	A 1 percentage point cut in the average personal income tax rate raises real GDP per capita by 1.4 percent in the first quarter and by up to 1.8 percent after three quarters. A 1 percentage point cut in the average corporate income tax rate raises real GDP per capita by 0.4 percent in the first quarter and by 0.6 percent after one year.
Randall Holcombe & Donald Lacombe, The effect of state income taxation on per capita income growth. PUBLIC FINANCE REVIEW (2004)	States that raised income taxes averaged a 3.4 percent reduction in per capita income.
John Mullen & Martin Williams, Marginal tax rates and state economic growth. REGIONAL SCIENCE AND URBAN ECONOMICS (1994)	Higher marginal tax rates reduce GDP growth.

Why Do Some States Prosper Economically and Others Do Not?

While there are a number of factors that affect a state's economy and create growth or decline, it is apparent, by many studies such as reported by the Tax Foundation, that tax policy plays an important role.

Arthur Laffer – top economic advisor to Ronald Reagan and creator of the "Laffer Curve." –

"Economics is about incentives: Government policies change the attractiveness of activities. Does the policy incentivize work or non-work?"

"Tax rates don't directly affect economic performance per se, instead tax rates affect taxpayer incentives and it is the change in the taxpayer incentive that affects economic performance. People work and save to get what they can after tax."

The administration has spent considerable time traveling the state visiting with Kansans, economists and business leaders. We also visited with some national economists and business leaders. The administration contracted with Arthur Laffer, who has done extensive research on the effect of tax policy on state's economies.

The following are charts showing the economic performance of the nine states with the highest and lowest tax burden as a percent of personal income. Both cover different 10 year periods of economic growth.

Table 1A

The Nine States with the Highest and Lowest Tax Burden as a Percent of Personal Income, Ten-Year Economic Performance

(performance between 2001 and 2010 unless otherwise noted)

State	State & Local Gov't Tax Burden as a % of Personal Income*	Gross State Product Growth	Nonfarm Payroll Employment Growth	Population Growth	Net Domestic In-Migration as a % of Population	State & Local Tax Revenue Growth***
Alaska	6.3%	77.0%	12.2%	12.1%	-0.9%	175.1%
Nevada	7.5%	58.9%	6.1%	28.9%	13.3%	74.0%
South Dakota	7.6%	58.5%	6.4%	7.3%	1.0%	47.2%
Tennessee	7.6%	38.6%	-2.8%	10.3%	4.2%	43.9%
Wyoming	7.8%	105.6%	15.2%	14.3%	4.0%	168.8%
Texas	7.9%	57.7%	8.7%	17.9%	3.5%	65.1%
New Hampshire	8.0%	35.2%	-0.7%	4.7%	2.4%	52.1%
South Carolina	8.1%	37.1%	-1.0%	13.8%	6.7%	37.1%
Louisiana	8.2%	58.7%	-1.6%	1.6%	-6.8%	60.5%
9 States with Lowest Tax Burden as a % of Personal Income**	**7.67%**	**58.57%**	**4.72%**	**12.34%**	**3.04%**	**80.43%**
*9 States with Lowest Tax Burden as a % of Personal Income Excluding AK & WY***	*7.84%*	*49.22%*	*2.17%*	*12.08%*	*3.46%*	*54.28%*
Oklahoma	***8.7%***	***51.81%***	***2.18%***	***8.27%***	***1.17%***	***48.30%***
U.S. Average**	**9.38%**	**46.61%**	**0.51%**	**8.63%**	**0.88%**	**51.04%**
Kansas	***9.7%***	***42.35%***	***-1.91%***	***5.61%***	***-2.36%***	***50.61%***
9 States with Highest Tax Burden as a % of Personal Income**	**11.02%**	**38.24%**	**-2.89%**	**3.78%**	**-2.71%**	**41.83%**
Maine	10.1%	35.4%	-2.5%	3.4%	2.1%	32.6%
Vermont	10.2%	36.1%	-1.6%	2.2%	-0.3%	54.9%
Minnesota	10.3%	39.5%	-1.9%	6.4%	-0.9%	32.2%
California	10.6%	42.1%	-4.8%	8.0%	-4.0%	41.2%
Rhode Island	10.7%	38.1%	-4.1%	-0.5%	-4.4%	39.7%
Wisconsin	11.0%	35.3%	-2.8%	5.1%	-0.3%	30.1%
Connecticut	12.0%	40.9%	-4.3%	4.2%	-2.7%	34.8%
New York	12.1%	43.1%	-0.4%	1.5%	-8.6%	56.0%
New Jersey	12.2%	33.7%	-3.6%	3.6%	-5.2%	55.1%

*State & Local Government Tax Burden as of 2009 from Tax Foundation

**Equal-weighted averages.

***2000-2009

Table 1B

The Nine States with the Highest and Lowest Tax Burden as a Percent of Personal Income, Ten-Year Economic Performance

(performance between 1998 and 2007)

State	State & Local Gov't Tax Burden as a % of Personal Income*	Gross State Product Growth	Nonfarm Payroll Employment Growth	Population Growth	Net Domestic In-Migration as a % of Population	State & Local Tax Revenue Growth
Alaska	5.9%	91.3%	15.6%	10.1%	-1.9%	145.6%
Wyoming	6.8%	129.3%	26.5%	6.6%	0.8%	132.7%
South Dakota	7.3%	67.2%	12.9%	6.8%	-0.2%	50.1%
Nevada	7.4%	109.1%	39.6%	38.6%	17.5%	119.2%
New Hampshire	7.5%	49.8%	10.0%	9.2%	4.1%	65.7%
Texas	7.6%	80.8%	16.2%	18.3%	2.9%	77.1%
Tennessee	7.6%	49.0%	6.0%	10.8%	4.3%	66.6%
Louisiana	8.5%	70.7%	1.5%	-1.4%	-8.8%	74.9%
Montana	8.6%	74.6%	18.4%	7.3%	3.1%	62.3%
9 States with Lowest Tax Burden as a % of Personal Income**	**7.47%**	**80.20%**	**16.31%**	**11.80%**	**2.43%**	**88.23%**
*9 States with Lowest Tax Burden as a % of Personal Income excluding AK & WY***	*7.79%*	*71.61%*	*14.94%*	*12.79%*	*3.27%*	*73.69%*
Oklahoma	***8.82%***	***73.68%***	***9.53%***	***6.08%***	***0.58%***	***57.69%***
U.S. Average**	**9.34%**	**62.45%**	**10.53%**	**8.98%**	**0.76%**	**65.42%**
Kansas	***9.39%***	***56.76%***	***5.01%***	***4.32%***	***-2.45%***	***53.95%***
9 States with Highest Tax Burden as a % of Personal Income**	**10.85%**	**57.09%**	**7.87%**	**5.06%**	**-2.55%**	**61.20%**
Maine	10.3%	53.4%	8.5%	4.6%	2.8%	43.1%
Vermont	10.4%	50.7%	8.2%	3.3%	0.2%	70.6%
Rhode Island	10.4%	60.9%	7.6%	2.3%	-3.4%	55.4%
Wisconsin	10.5%	47.7%	6.1%	5.7%	0.1%	40.2%
Maryland	10.6%	69.1%	12.1%	8.3%	-1.2%	68.6%
California	10.8%	68.5%	11.6%	9.8%	-4.0%	82.2%
Connecticut	11.2%	54.2%	3.3%	3.7%	-3.1%	48.5%
New York	11.6%	57.6%	6.0%	3.6%	-9.3%	70.8%
New Jersey	11.8%	51.6%	7.3%	4.2%	-5.1%	71.4%

* State and Local Tax Burden as of 2007 from Tax Foundation

**Equal-weighted averages.

We thank retired professor William T. Terrell, Ph.D. for suggesting this period as preferable to our original choice of 2001-2010. Our results are much stronger using his period.

The next chart shows the economic consequences from the introduction of a state income tax.

Table 2
Economic Consequences from the Introduction of State Income Tax

State (Year of Introduction)		Economic Performance: % of U.S. GDP	Economic Performance: % of U.S. Population	Economic Performance: State Tax Revenues % of U.S.	Top PIT: Introduced	Top PIT: Current
Connecticut (1991)	5 Years Prior	1.74%	1.33%	1.70%		
	2010	1.63%	1.16%	1.81%	1.50%	6.50%
	Change	-0.11%	-0.17%	0.11%		5.00%
New Jersey (1976)	5 Years Prior	3.66%	3.47%	2.77%		
	2010	3.35%	2.85%	3.79%	2.50%	8.97%
	Change	-0.31%	-0.62%	1.02%		6.47%
Ohio (1972)	5 Years Prior	5.42%	5.25%	3.61%		
	2010	3.28%	3.74%	3.35%	3.50%	5.93%
	Change	-2.14%	-1.51%	-0.26%		2.43%
Rhode Island (1971)	5 Years Prior	0.44%	0.46%	0.47%		
	2010	0.34%	0.34%	0.36%	5.25%	5.99%
	Change	-0.10%	-0.12%	-0.11%		0.74%
Pennsylvania (1971)	5 Years Prior	5.72%	5.88%	5.59%		
	2010	3.91%	4.11%	4.21%	2.30%	3.07%
	Change	-1.81%	-1.77%	-1.38%		0.77%
Maine (1969)	5 Years Prior	0.39%	0.51%	0.43%		
	2010	0.35%	0.43%	0.49%	6.00%	8.50%
	Change	-0.04%	-0.08%	0.06%		2.50%
Illinois (1969)	5 Years Prior	6.52%	5.53%	4.64%		
	2010	4.48%	4.16%	4.09%	2.50%	5.00%
	Change	-2.04%	-1.37%	-0.55%		2.50%
Nebraska (1968)	5 Years Prior	0.67%	0.75%	0.45%		
	2010	0.62%	0.59%	0.54%	2.60%	6.84%
	Change	-0.05%	-0.16%	0.09%		4.24%
Michigan (1967)	5 Years Prior	5.08%	4.34%	5.03%		
	2010	2.64%	3.20%	3.18%	2.00%	4.35%
	Change	-2.44%	-1.14%	-1.85%		2.35%
Indiana (1964)	5 Years Prior	2.61%	2.55%	2.09%		
	2010	1.89%	2.10%	2.08%	2.00%	3.40%
	Change	-0.72%	-0.45%	-0.01%		1.40%
West Virginia* (1962)	5 Years Prior	0.79%	0.97%	1.01%		
	2010	0.48%	0.60%	0.67%	5.40%**	6.50%
	Change	-0.31%	-0.37%	-0.34%		1.10%

* Due to State GDP data limitations, West Virginia's economic activity is measured as a share of national personal income

** Statutory rate was 6.0% of U.S. tax liability applied to top rate of 91%

The debate then becomes why individual income tax and not corporate, sales or property. Again we should be most interested in policy that grows the Kansas economy and allows us to be competitive.

Corporate Income Tax

As reported by the Tax Foundation, corporate income tax rates are important to economic growth. Obviously corporate tax rates effect investment and job creation. Kansas and every other state have developed a number of competitive tax incentives and credits to attract companies. These are beneficial to C-corps and provide tools for recruitment and retention. Currently 59.3 percent of our C-corps do not pay any corporate income tax to Kansas due to a number of factors.

Last year, and effective as of January 1, 2013, Kansas has eliminated non-wage business income for LLCs, S-corps, and sole proprietors to grow our small businesses. In Kansas, 98 percent of our businesses have 100 employees or fewer and 77 percent have fewer than 10 employees. According to the Small Business Administration, two-thirds of new jobs are created by small business. This tax policy will help our small businesses with some additional capital to grow their business through investment and jobs.

Individual Income Tax

Individual income tax rates have a significant impact on the state's economic growth. The net personal income of Kansas families matters. Through lowering individual income tax rates we put more money back in Kansans pockets. It also makes us more competitive with our adjacent states.

Top Rate for Individual Income Taxes in Adjacent States to Kansas

Before Jan. 1, 2013	After Jan. 1, 2013
Colorado – 4.63%	Colorado – 4.63%
Oklahoma – 5.25%	**Kansas – 4.9%**
Missouri – 6%	Oklahoma – 5.25%
Kansas – 6.45%	Missouri – 6%
Nebraska – 6.84%	Nebraska – 6.84%

The goal of the Governor is to provide a competitive, simpler, fairer and flatter individual income tax in Kansas.

It should be noted that changes in tax policy, as of January 1, 2013, included a doubling of the standard deduction for single head of households and increasing the standard deduction for married filing jointly. Currently, only about 30 percent of Kansans itemize and 70 percent do not itemize. With these significant increases in standard deductions, we will most likely see a further reduction in the number of filers itemizing on their 2013 tax returns.

Sales Tax

Numerous studies show sales tax rates seem to have a lesser effect on economic growth than corporate or individual income taxes. The following are Dr. Laffer's data on the effect of sales tax rates on the state's economy.

Dr. Arthur Laffer's Analysis of Sales Taxes

"The same economic benefits as we saw with income taxes, corporate taxes and right to work states do not accrue to those states with low sales tax burdens (measured as sales tax revenues per $1,000 of personal income) compared to those states with the highest sales tax burdens. We find that **sales taxes are economic performance neutral and therefore are far preferable as a means for a state to raise needed tax revenues**. All taxes are bad in the sense that they impede a productive activity. But some taxes are a lot worse than others and the government does need revenues after all to carry out its appointed tasks. If tax they must, the sales tax is one of the least harmful taxes.

"The following table illustrates that the states with the lowest sales tax burdens have lower state GDP growth, lower employment growth, and less population growth than the states with the highest sales tax burdens. But in truth these measures are probably spurious when it comes to sales tax burden as a stand-alone tax. Oregon, which has no sales tax at all, has the single highest income tax rate in the nation. Mississippi, which has a high sales tax burden, has one of the lowest corporate tax rates in the nation and Tennessee and Wyoming have no income tax at all and yet are high sales tax burden states.

"Because sales taxes are, by definition, flat taxes on consumption, these taxes should be less economically distorting than progressive income taxes either personal or corporate. Additionally, several of the states with the highest sales tax burdens (Tennessee, Wyoming, and Washington) also have no income tax. Because states need to raise money to provide needed public services, no income tax states rely on the sales tax to a greater extent – hence the higher sales tax burdens. Sales taxes affect where sales occur and income taxes – corporate and personal – affect where income occurs."

The Nine States with the Highest and Lowest Sales Tax Burden
Ten-Year Economic Performance
(performance between 2001 and 2010 unless otherwise noted)

State	Sales Tax Burden*	Gross State Product Growth	Non-Farm Payroll Employment Growth	Population Growth	Net Domestic In-Migration as a % of. Population	Unemployment Rate
Delaware	$0.00	41.9%	-1.6%	13.0%	5.2%	8.5%
Montana	$0.00	56.0%	9.4%	9.2%	4.0%	7.2%
New Hampshire	$0.00	35.2%	-0.7%	4.7%	2.5%	6.1%
Oregon	$0.00	55.0%	-0.3%	10.4%	4.5%	10.8%
Alaska	$7.31	77.0%	12.2%	12.1%	-2.0%	8.0%
Massachusetts	$12.41	34.2%	-4.6%	2.1%	-4.7%	8.5%
Virginia	$13.79	51.4%	3.2%	11.3%	1.7%	6.9%
Maryland	$13.89	50.9%	1.7%	7.4%	-1.5%	7.5%
Vermont	$14.31	36.1%	-1.6%	2.2%	-0.1%	6.2%
9 States with Lowest Sales Tax Burden**	**$6.86**	**48.62%**	**1.97%**	**8.06%**	**1.06%**	**7.73%**
U.S. Average**	**$24.58**	**46.61%**	**0.51%**	**8.63%**	**0.86%**	**8.75%**
9 States with Highest Sales Tax Burden**	**$43.03**	**55.47%**	**3.07%**	**10.63%**	**1.90%**	**8.56%**
Mississippi	$35.16	44.3%	-3.5%	4.0%	-1.1%	10.4%
Arkansas	$40.09	44.6%	0.8%	8.4%	2.5%	7.9%
Tennessee	$40.59	38.6%	-2.8%	10.3%	4.2%	9.7%
Arizona	$40.89	49.0%	5.0%	20.5%	10.7%	9.9%
New Mexico	$42.35	53.1%	5.9%	12.6%	1.5%	8.4%
Louisiana	$43.37	58.7%	-1.6%	1.6%	-6.1%	7.5%
Wyoming	$47.50	105.6%	15.2%	14.3%	4.3%	7.0%
Hawaii	$48.56	57.4%	5.7%	11.7%	-2.2%	6.6%
Washington	$48.73	47.8%	3.0%	12.3%	3.4%	9.6%

*State and local Sales tax imposed as of 1/1/11 using the tax rate of each state's largest city as a proxy for the local tax. Sales tax burden of $1,000 of personal income

**Equal-weighted averages.

The *Wall Street Journal* in a Jan. 30, 2012 editorial titled "What's Right With Kansas" discussed keeping the state sales tax rate at 6.3 percent in Kansas to lower income taxes: "The trade-off is worth it since taxes on investment and production are generally more harmful to economic growth than taxes on consumption."

Property Tax

Property tax has the least effect on economic growth. In Kansas, property tax is generally a local issue and funding stream. The state only levies 21.5 mills, which primarily funds education. Changes to property tax rates would affect local government and the state's funding of education.

The state has programs such as the Homestead Refund which helps Kansans who are 55 years old or older, disabled or blind, or who have a dependent child under 18 living with them. The refund is a percentage of property taxes paid calculated according to income up to $32,401.