Office of the Secretary
915 SW Harrison St.
Topeka, KS 66612-1588

Kansas
Department of Revenue

phone: 785-296-3041
fax: 785-368-8392
www.ksrevenue.org

Nick Jordan, Secretary

Sam Brownback, Governor

Senate Assessment and Taxation Committee

Testimony of Secretary Nick Jordan: Continue Pro-Growth Tax Reform

January 29, 2013

Chairman Donovan, thank you for inviting me to address your committee on the very important issue of tax reform and how we can create an environment in which Kansas families and businesses can flourish in the 21st century.

This is a most exciting time in Topeka because the conversation truly has changed, and not just about whether to raise or lower taxes — but how we can work together to grow the Kansas economy and make the tax system fairer, flatter, and simpler for our citizens.

You'll recall 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 and outmigration of taxpayers.

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.

Last year's tax relief package was a critical first step in overhauling the state's overly complicated tax code and giving our economy a jolt of adrenaline. **But it was only a first step.**

After all, our current system has been built up over many decades and is filled with special interest items that benefit targeted groups rather than all taxpayers. As a result, taxes at the federal, state, and local levels are a complicated hodge-podge of dozens upon dozens of taxes, credits, and special interests all cobbled together.

It is certainly not a pleasant system for many citizens to try to understand and comply with. To put it bluntly, everyday citizens and small business owners are fed up with this complex mess.

It's imperative to continue streamlining and modernizing our tax policy in a strategic way that funds core government functions while emphasizing economic growth and encouraging greater financial investment in our state.

People deserve a fairer, flatter and simpler tax code and this, in turn, will broaden the tax base and lower rates as much as possible for the benefit of the maximum number of Kansans.

Sn. Assmnt & Tax
1/29/13
Attachment # 4

Lower income tax rates allow families and businesses to keep more of their own hard-earned money. And, importantly, data show states with zero personal income tax significantly outperform states with the highest personal income tax rates; experience larger than average population growth; and boost state tax revenues at a faster pace than high tax states.

Next Steps Toward Zero State Income Tax

After the historic tax cuts enacted last year, which reduced income tax rates by 14 to 24 percent for all taxpayers, the Governor's 2013 tax reform proposal takes the next step on Kansas' path to no state income tax and greater economic growth.

This glide path to zero will not cut funding for schools, higher education or essential safety net programs. It will create jobs and opportunities in our state that the current generation has been going to Texas or Florida to find.

The tax reform plan will do the following:

1. Reduce the state's bottom individual income tax rate from 3 percent to 2.5 percent in tax year 2014 and then to 1.9 percent in tax year 2016. *This provides tax rate reductions of 16 percent and 24 percent.*
2. Reduce the current top tax rate of 4.9 percent to 3.5 percent in tax year 2017. *This provides a tax rate reduction of 28 percent.*
3. In addition to tax relief of half a billion dollars over five years, the Governor proposes using state revenue growth greater than 4 percent to ratchet rates down further until the state income tax is eliminated.
4. **In exchange for much lower income rates**, the plan leaves the state sales tax flat at its current level and further simplifies the tax code by eliminating the mortgage interest and real estate tax deductions at the state level.
5. **More than 70 percent of Kansans already use the standard deduction** and will not be impacted in any way by the elimination of itemized deductions.

It is important to remember that, under current law for tax year 2013, the standard deduction doubled from $4,500 to $9,000 for single head-of-household filers and increased by 50 percent from $6,000 to $9,000 for married taxpayers filing jointly.

This means at the state level the value of itemized deductions is greatly reduced by the value of large reductions in overall tax rates and significant increases in standard deductions.

And changes to itemized deductions at the state level do not impact federal itemized deductions, which are much larger and still available to Kansans eligible to itemize.

Tax Policy Does Matter

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%

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, who found that data "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 ... Every study in the last 15 years find a negative effect of taxes on growth ... If we intend to increase employment, we should lower taxes on workers and businesses that hire them."

He concluded, "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."

While there are a number of factors that affect a state's economy and create growth or decline, it is apparent that tax policy plays an important role.

Interestingly, numerous studies show **sales tax** rates seem to have a lesser effect on economic growth than corporate or individual income taxes.

According to economist Arthur Laffer, "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 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."

Further, the *Wall Street Journal* last year editorialized about 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."

Positive Impact on Families

Further lowering the state income tax rate will give Kansas families and taxpayers more money in their pockets as they decrease their state income tax withholding and keep more of the money they earn as they earn it. In fact, the median Kansas tax return uses the standard deduction, has income of $65,430, and is filed married jointly with one child. This family will see a state income tax reduction of $572 per year in 2013 under current law, an additional $150 reduction per year in 2014 when the bottom rate is reduced to 2.5 percent, and an additional $448 reduction per year when tax relief is fully phased in.

Federal Credits and Deductions Are Not Impacted by Kansas Tax Reform

It is worth repeating: In Kansas, as we make our tax code flatter, fairer, and simpler, we will not impact federal income tax rates, credits, or deductions. Those who claim mortgage interest deductions or receive federal earned income tax credits will continue to do so — and at the significantly higher benefit levels provided by the federal tax code.

As the Kansas Society of CPAs and others have noted, the tax benefit of mortgage interest and other deductions is minimized and then made obsolete as income tax rates move toward zero.

Gary Allerheiligen, CPA, has noted that, when 70 percent of Kansas tax filers do not itemize, the elimination of itemized deductions **is not** a factor to them. When 25 percent of Kansas tax filers pay no Kansas income tax, and 50 percent pay no federal income tax, the elimination of itemized deductions **is not** a factor to them. When 100 percent of the Kansas taxpayers will see a reduction in their marginal tax rate, the elimination of itemized deductions **may or may not** be a factor to them.

The Safety Net for Low-Income Kansans

It's important to be thoughtful about the level of social welfare provided to low-income Kansans and how that assistance should be provided. As Mr. Allerheiligen testified last year, "Social programs should stand on their own, be transparent, be accountable — but not be administered through the tax collection system."

It is also important to remember the full range of assistance provided rather than one item in isolation. Low-income and disabled Kansans receive more than $3.5 billion in assistance annually through DCF and KDHE programs already in place, forming a sizable safety net. In the last fiscal year alone, more than $442 million was provided in food assistance, benefiting an average of 296,000 people per month, and nearly $71 million was provided in child care assistance. This $3.5 billion existing safety net in Kansas (federal and state funding) does not include unemployment benefits or federal programs such as housing assistance that are available on top of other welfare assistance.

With that understanding, we seek to change the dynamic that has led to average (or worse) economic results — so more Kansas families can achieve a meaningful increase in income and opportunity, and small businesses can invest in growth and new jobs.

Moving Forward

We have a clear choice: Maintain the cobbled-together status quo that resulted in the lost decade for jobs, or take serious action to reform our state tax system.

This no doubt takes courage and hard work. But by making Kansas tax policy fairer, flatter and simpler, and by creating a pro-growth business environment that encourages financial investment in Kansas, the state can position itself as a top economic performer. This will reduce poverty and create economic opportunities for the maximum number of Kansans.

The Nine States with the Lowest and the Highest Marginal Personal Income Tax (PIT) Rates
Ten-Year Economic Performance
(performance between 2001 and 2010 unless otherwise noted)

State	Top PIT Rate*	Gross State Product Growth	Non-Farm Payroll Employment Growth	Population Growth	Net Domestic In-Migration as a % of Population***	State & Local Tax Revenue Growth****
Alaska	0.00%	77.0%	12.2%	12.1%	-2.0%	452.6%
Florida	0.00%	47.7%	0.2%	15.0%	6.5%	82.3%
Nevada	0.00%	58.9%	6.1%	28.9%	14.1%	100.1%
New Hampshire	0.00%	35.2%	-0.7%	4.7%	2.5%	59.6%
South Dakota	0.00%	58.5%	6.4%	7.3%	0.8%	51.2%
Tennessee	0.00%	38.6%	-2.8%	10.3%	4.2%	61.7%
Texas	0.00%	57.7%	8.7%	17.9%	3.4%	75.5%
Washington	0.00%	47.8%	3.0%	12.3%	3.4%	57.8%
Wyoming	0.00%	105.6%	15.2%	14.3%	4.3%	172.2%
9 States with No PIT**	**0.00%**	**58.54%**	**5.36%**	**13.65%**	**4.12%**	**123.66%**
U.S. Average**	**5.47%**	**46.61%**	**0.51%**	**8.63%**	**0.86%**	**70.23%**
Kansas	**6.45%**	**42.35%**	**-1.90%**	**5.61%**	**-2.36%**	**62.87%**
9 States with Highest Marginal PIT Rate**	**9.92%**	**42.06%**	**-1.68%**	**5.49%**	**-1.91%**	**61.79%**
Ohio	8.24%	24.8%	-9.3%	1.2%	-3.1%	44.5%
Maine	8.50%	35.4%	-2.5%	3.4%	2.3%	45.3%
Maryland	9.30%	50.9%	1.7%	7.4%	-1.5%	67.0%
Vermont	9.40%	36.1%	-1.6%	2.2%	-0.1%	64.5%
New York	10.50%	43.1%	-0.4%	1.5%	-8.3%	68.3%
California	10.55%	42.1%	-4.8%	8.0%	-3.9%	77.2%
New Jersey	10.75%	33.7%	-3.6%	3.6%	-4.8%	70.4%
Hawaii	11.00%	57.4%	5.7%	11.7%	-2.2%	72.1%
Oregon	11.00%	55.0%	-0.3%	10.4%	4.5%	46.8%

Data compiled by Laffer Associates

*Highest marginal state and local personal income tax rate imposed as of 1/1/2011 using the tax rate of each state's largest city as a proxy for the local tax. The deductibility of federal taxes from state tax liability is included where applicable. New Hampshire and Tennessee tax dividend interest income only.

**Equal-weighted averages

***2000-2009, ****1999-2008

Policy & Research
915 SW Harrison St
Topeka KS 66612-1588

Kansas
Department of Revenue

Phone: 785-296-3081
FAX: 785-296-7928
www.ksrevenue.org

Nick Jordan, Secretary
Richard Cram, Director

Sam Brownback, Governor

TESTIMONY REGARDING SENATE BILL 78
Before the Senate Committee on Assessment and Taxation
January 19, 2013

Chairman Donovan and Members of the Committee:

The Department of Revenue respectfully submits the following in support of Senate Bill 78:

GENERALLY

The specifics of the Governor's tax plan are contained in Senate Bill 78. They includethe following:

- **Lowing individual income tax rates:**
  - **2.5 percent** rate for income under $15,000 ($30,000 married filing jointly) for tax years 2014 and 2015
  - **1.9 percent** rate for income under $15,000 ($30,000 married filing jointly) for tax year 2016 and tax years thereafter
  - **3.5 percent** rate for income of $15,000 and over ($30,000 married filing jointly) for tax year 2017 and tax years thereafter
  - *Note: Current rates are 3.0 percent and 4.9 percent*
- **Reducing Kansas itemized deductions** by disallowing real property taxes and mortgage interest included in federal itemized deductions
- **Holding the sales tax rate steady** at 6.3 percent, with 4/10 of a cent going to the highway fund as planned in FY14, as data show that sales tax rates have the least negative impact on economic growth relative to other tax types.
- Beginning at the end of fiscal year 2015, **automatically reducing individual income tax rates,** when actual state general fund receipts from taxes exceed the actual state general fund receipts from taxes for the immediately preceding fiscal year by more than 4%.

Overview of Bill

Lowering individual income tax rates:

The imposition of Kansas income tax, and the rate of tax, is controlled by K.S.A. 79-32,110. The new rate structure for individuals is found in Section 1, on page 1 and 2, of the Bill.

Reducing Kansas itemized deductions:

If an individual taxpayer uses itemized deductions on their federal return they may use itemized deductions on their Kansas return. The starting point for determining the amount of Kansas itemized deductions is federal itemized deductions. Then certain modifications are made to determine the amount of Kansas itemized deductions.

The Bill amends K.S.A. 79-32,120 to disallow real property taxes and mortgage interest included in federal itemized deductions. The new provisions are found in Section 2 on page 3 of the Bill.

Holding the sales tax rate steady:

The rate of the Kansas sales tax is set by K.S.A. 79-3603. Effective July 1, 2010 the rate increased from 5.3% to 6.3%. Under current law it will be reduced to 5.7 percent effective July 1, 2013. The amendments to K.S.A. 79-3603 and K.S.A. 79-3620, found in Section 3, page 3, and Section 4, page 8 (and page 10), respectively, hold the sales tax steady at 6.3%, with 4/10 of a cent going to the highway fund as planned in FY14. Similarly, the amendments to K.S.A. 79-3703 and K.S.A. 79-3710, found in Section 5, page 11, and Section 6, page 11 (and page 13), respectively, hold the use tax steady at 6.3%, with 4/10 of a cent going to the highway fund as planned in FY14.

Automatic Income Tax Rate Reduction:

New Section 7, page 14, provides for the automatic reduction of income tax rates when actual state general fund receipts from taxes exceeds the actual state general fund receipts from taxes for the immediately preceding fiscal year by more than 4%, beginning in fiscal year 2015. Top marginal rates for individual tax will be reduced to rates estimated by the Secretary of Revenue. Reduced rates will be published by October 15 of the year prior to their effect. Lower tax receipts will not trigger an automatic rate increase.

Section By Section Summary

Section 1, page 1. K.S.A. 79-32,110 imposes the Kansas income tax and establishes the rate of tax. The amendments to this statute reduce, over time, the bottom rate from 3.0% to 1.9% and the top rate from 4.9% to 3.5%. The rates for all other taxpayers are left unchanged.

Section 2, page 3. K.S.A. 79-32,120 permits an individual to use itemized deductions, rather than the standard deduction found in K.S.A. 79-32,119, if the individual uses itemized deductions on their federal income tax return. The starting point for determining the amount of Kansas itemized deductions is federal itemized deductions; certain modifications are made to determine the amount of Kansas itemized deductions. The amendments to this statute disallow real property taxes and mortgage interest included in federal itemized deductions from being included in Kansas itemized deductions.

Sections 3 and 4, pages 3 and 8 (and page 10). K.S.A. 79-3603 imposes the Kansas retailers' sales tax, and K.S.A. 79-3620 deals with depositing and distributing the tax. The amendments hold the sales tax steady at 6.3%, with 4/10 of a cent going to the highway fund as planned in FY14.

Sections 5 and 6, page 11 (and page 13). K.S.A. 79-3703 imposes the Kansas consumers' compensating use tax, and K.S.A. 79-3710 deals with depositing and distributing the tax. The amendments hold the use tax steady at 6.3%, with 4/10 of a cent going to the highway fund as planned in FY14.

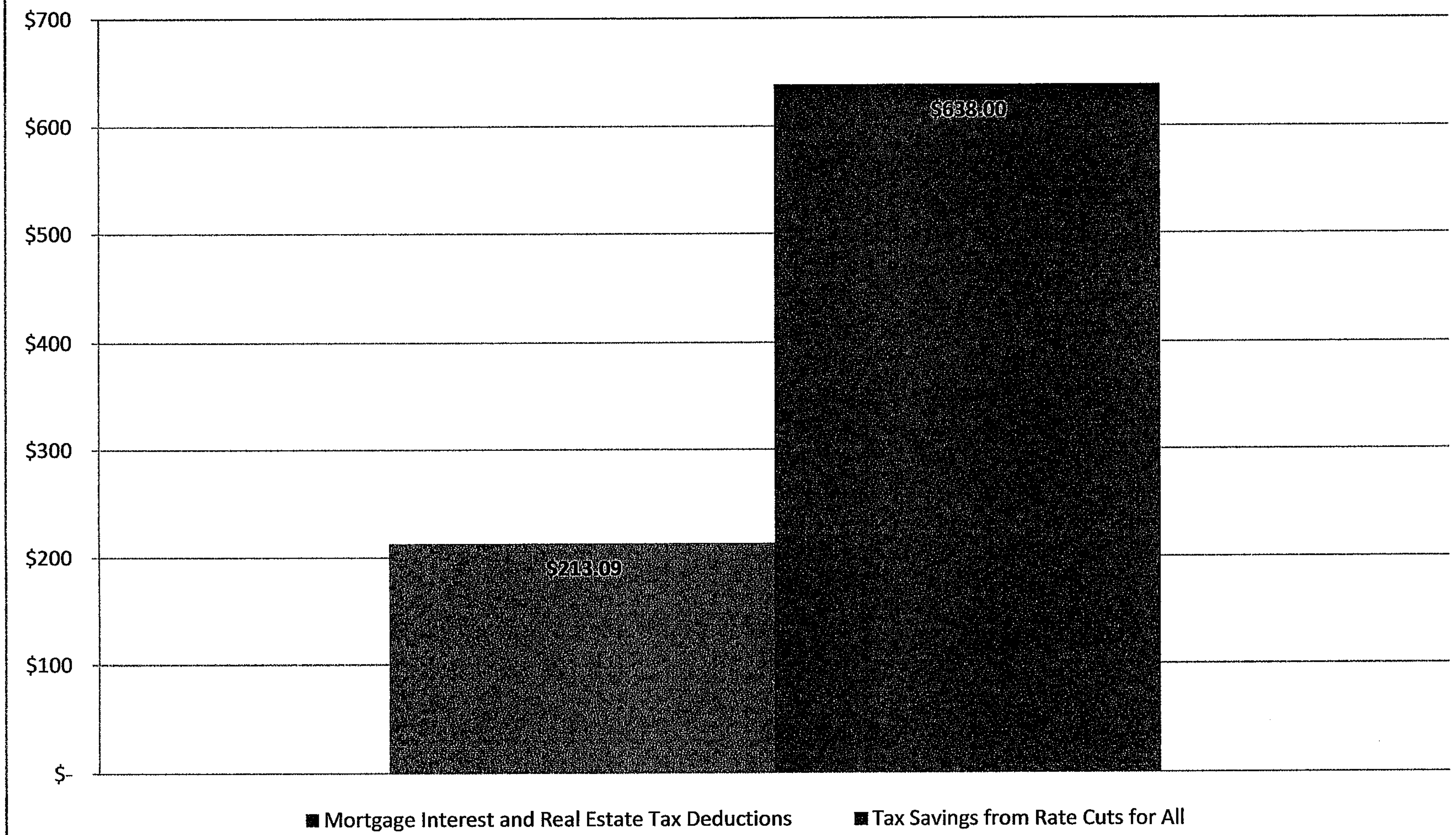
New Section 7, page 14. Beginning in FY 2015, provides for the automatic reduction of income tax rates when actual state general fund receipts from taxes exceeds the actual state general fund receipts from taxes for the immediately preceding fiscal year by more than 4%. The top marginal rates for individual income tax will be reduced to rates estimated by the Secretary of Revenue. Reduced rates will be published by October 15 of the year prior to their effect. Tax year 2016 should be the earliest year that this provision could affect. Lower tax receipts will not trigger an automatic rate increase.

Section 8, page 14. This section repeals statutes included in the 2012 supplement.

Section 9, page 14. This is the effective date provision.

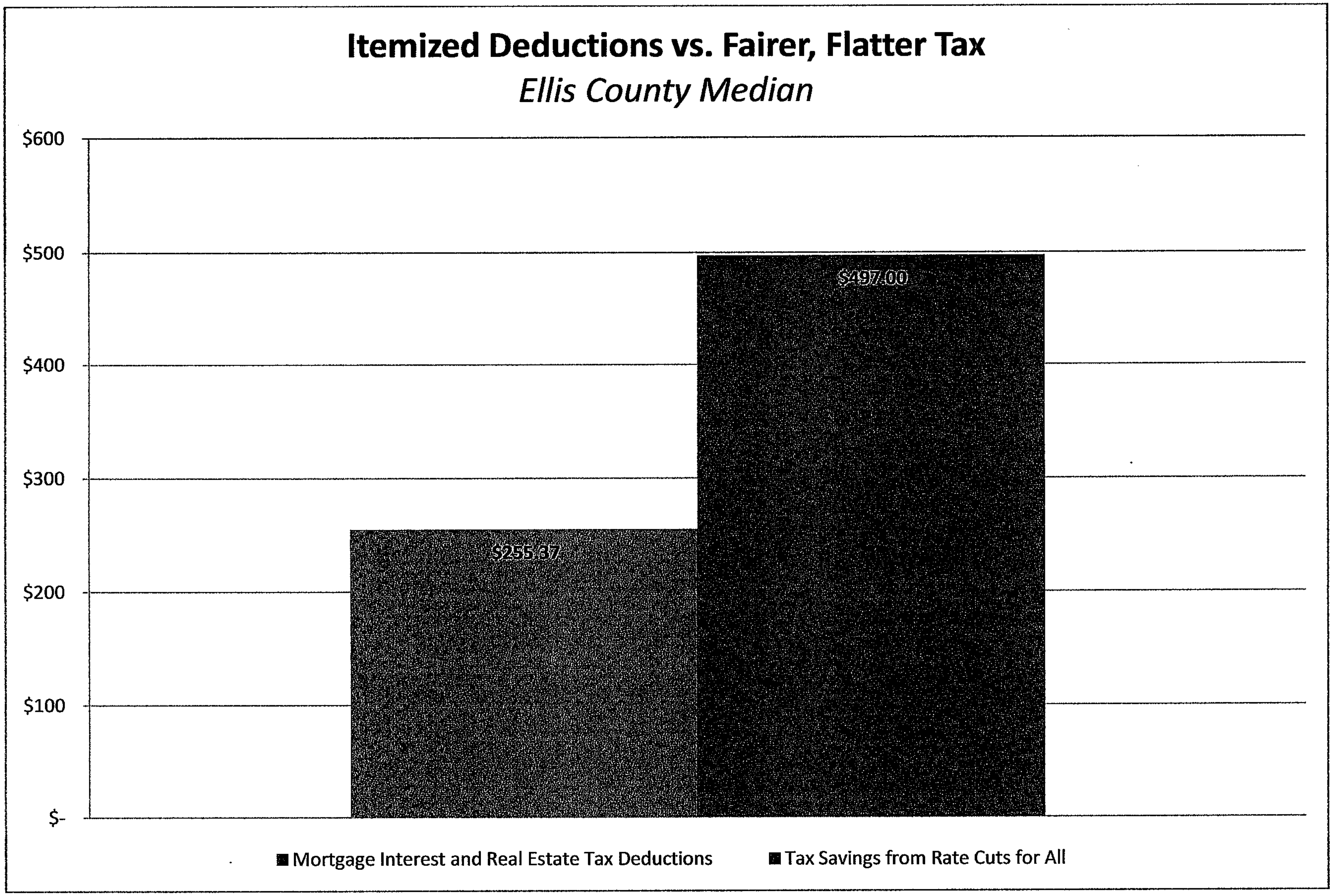
Itemized Deductions vs. Fairer, Flatter Tax

Sedgwick County Median



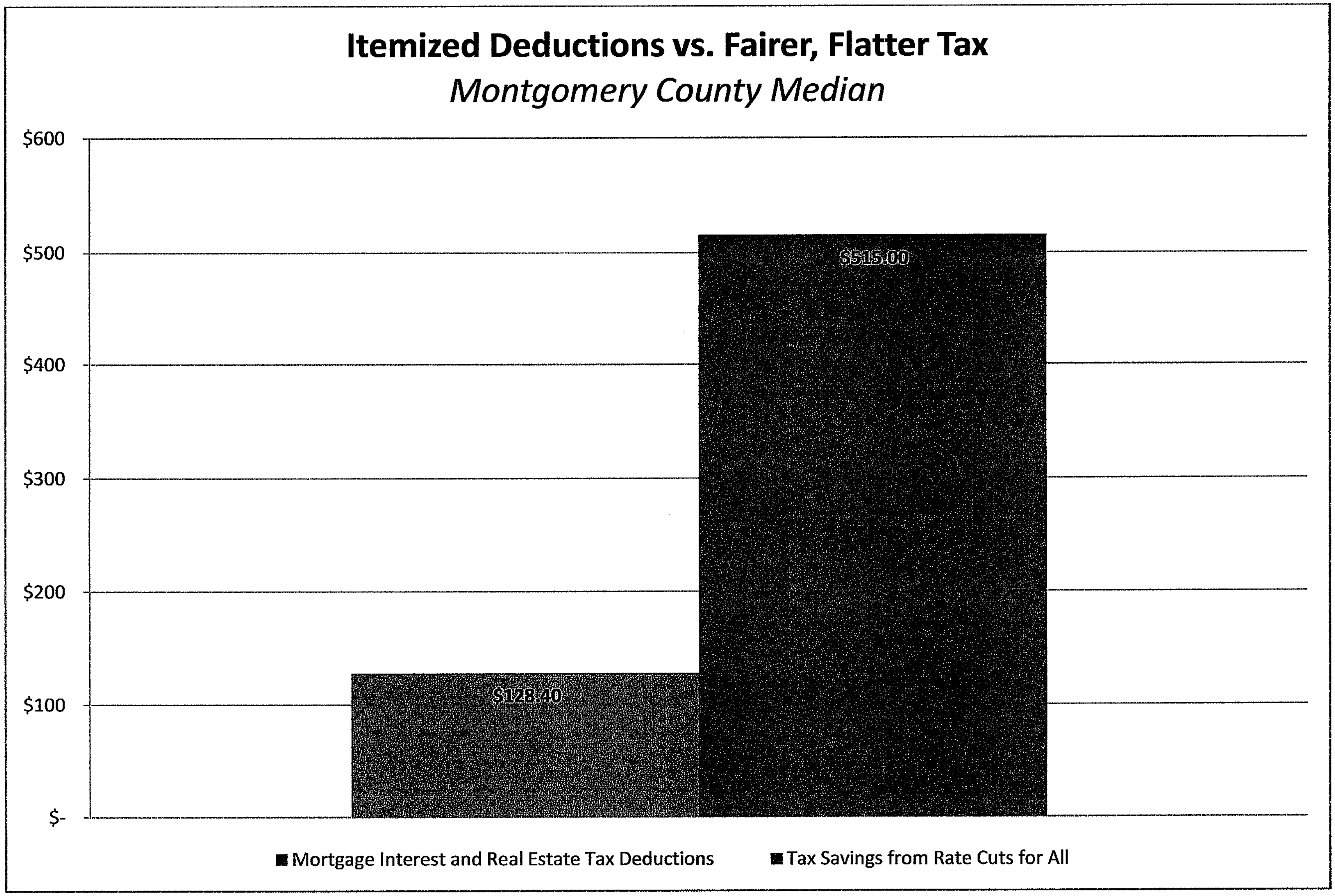
Top income tax rate of 3.5 percent
Source: Kansas Department of Revenue

Att. 4-10

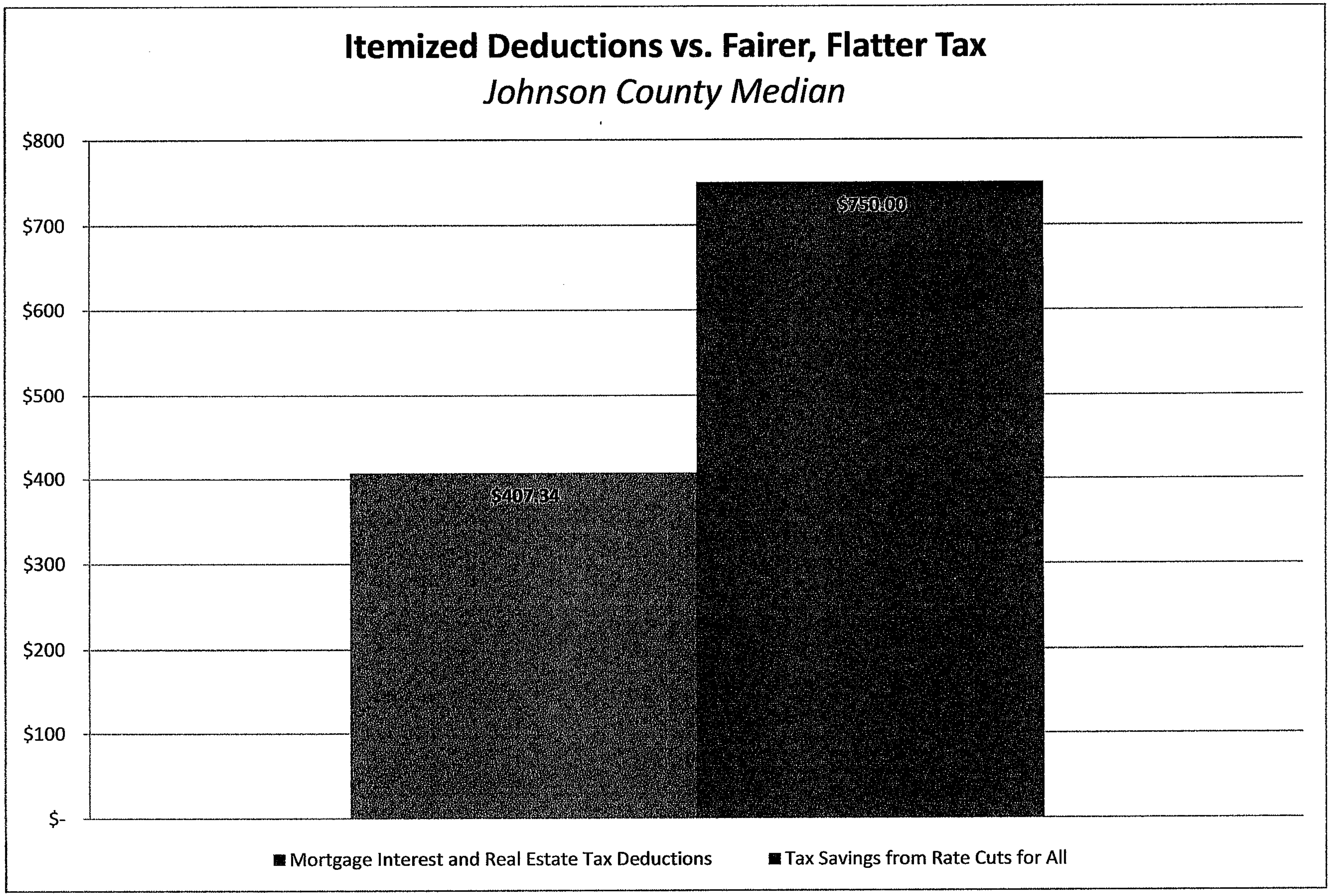


Top income tax rate of 3.5 percent
Source: Kansas Department of Revenue

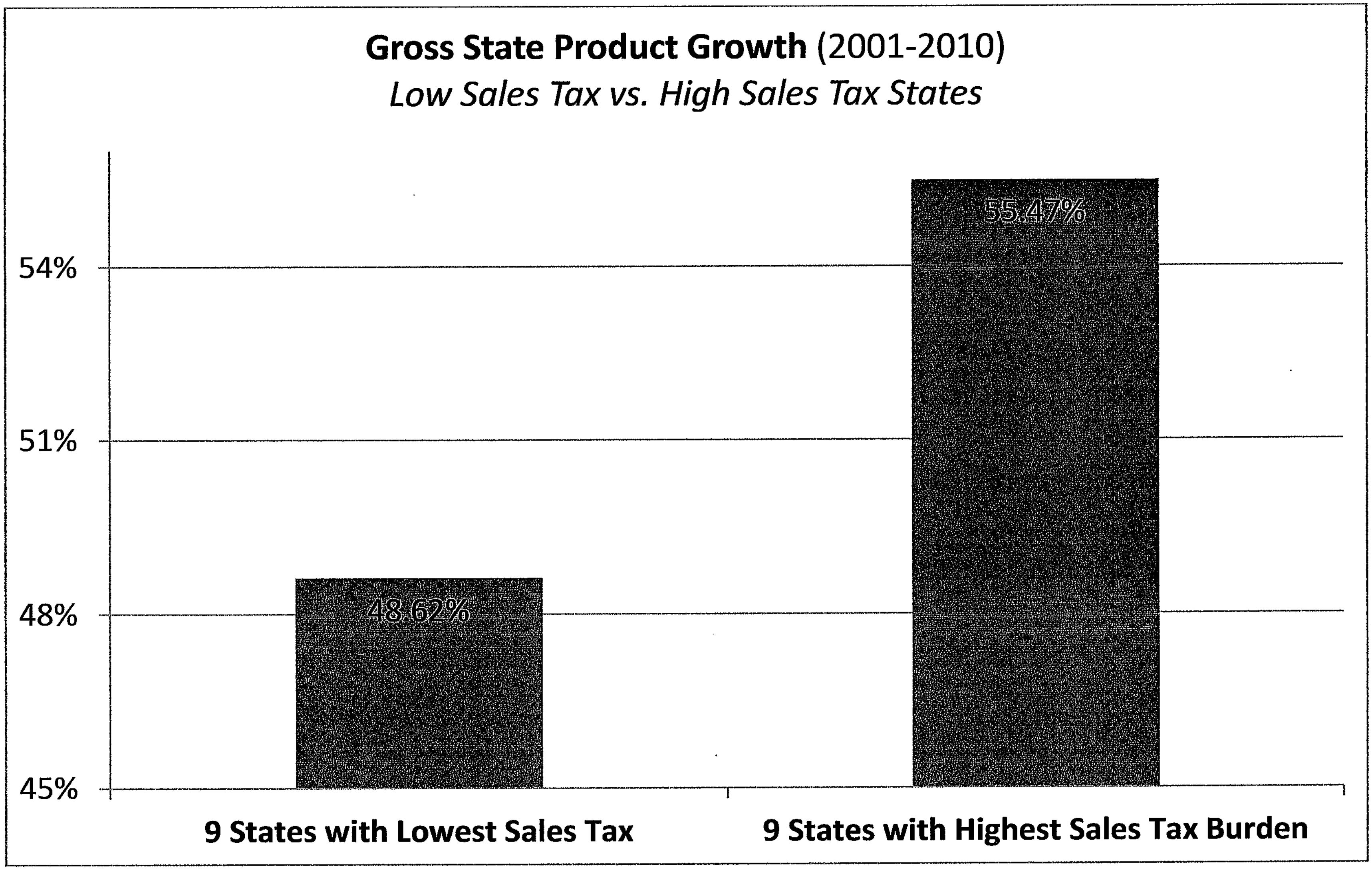
Att. 4-11



Top income tax rate of 3.5 percent
Source: Kansas Department of Revenue

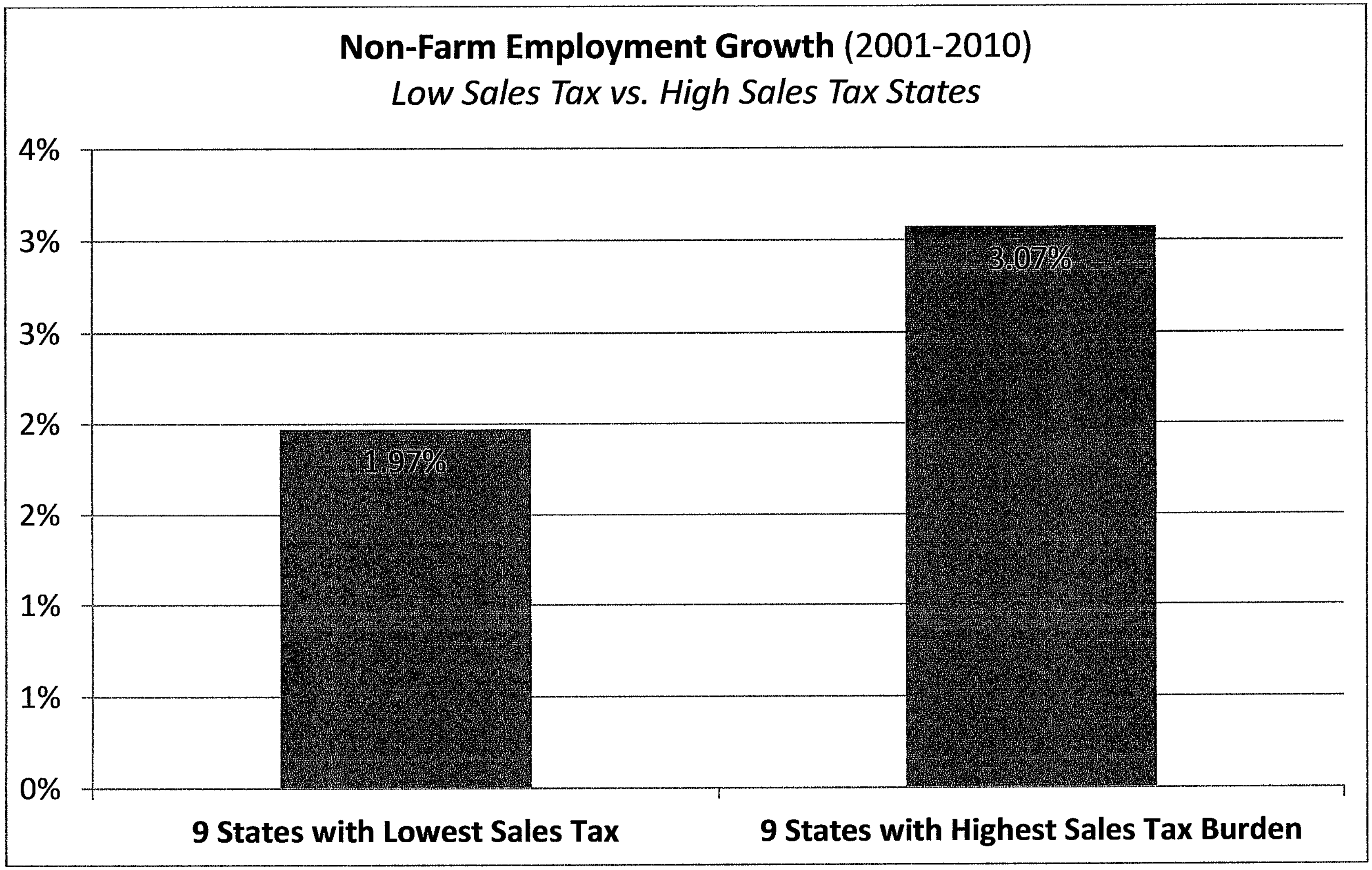


Top income tax rate of 3.5 percent
Source: Kansas Department of Revenue

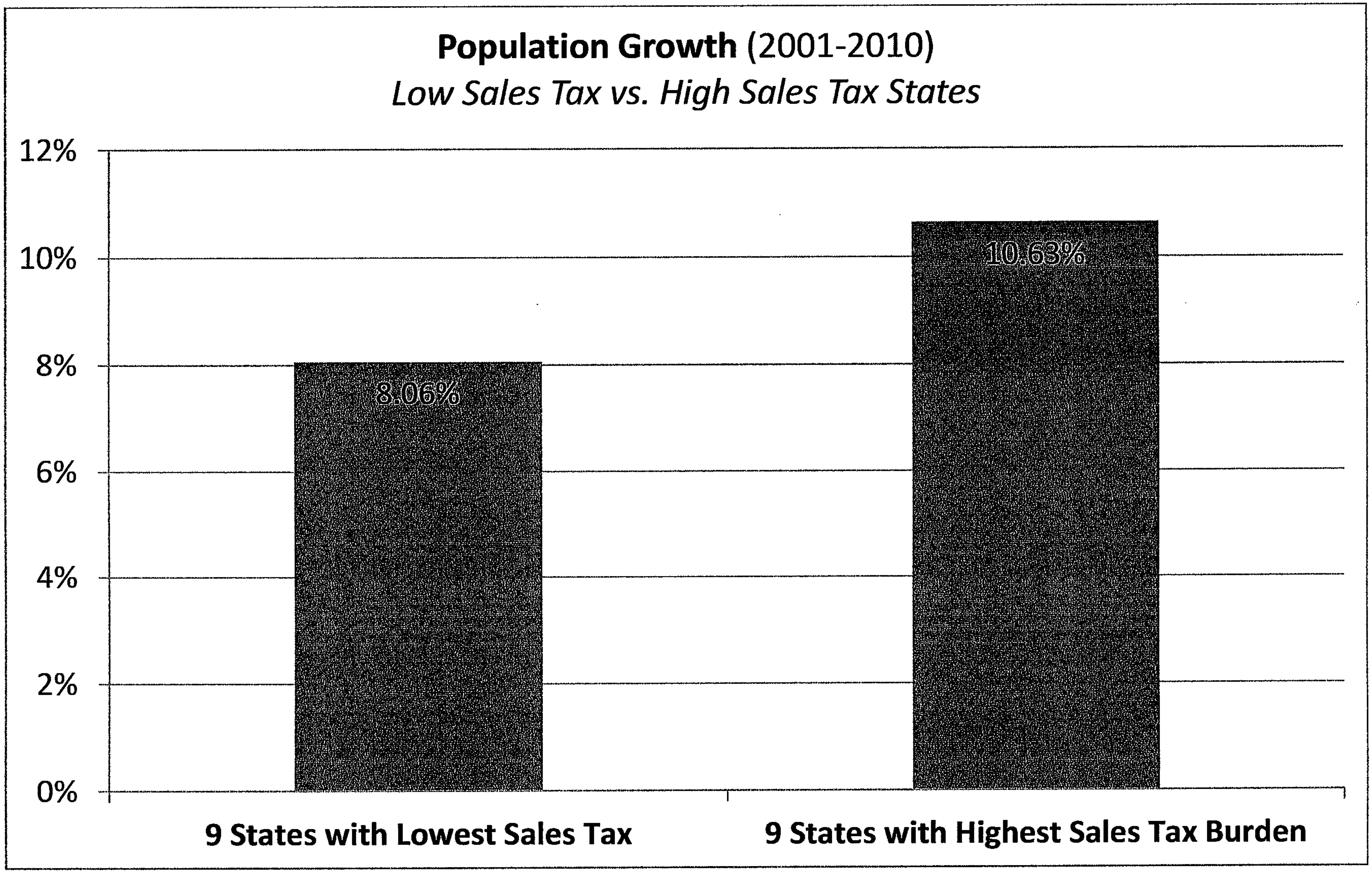


Source: Laffer Associates

Att. 4-15



Source: Laffer Associates

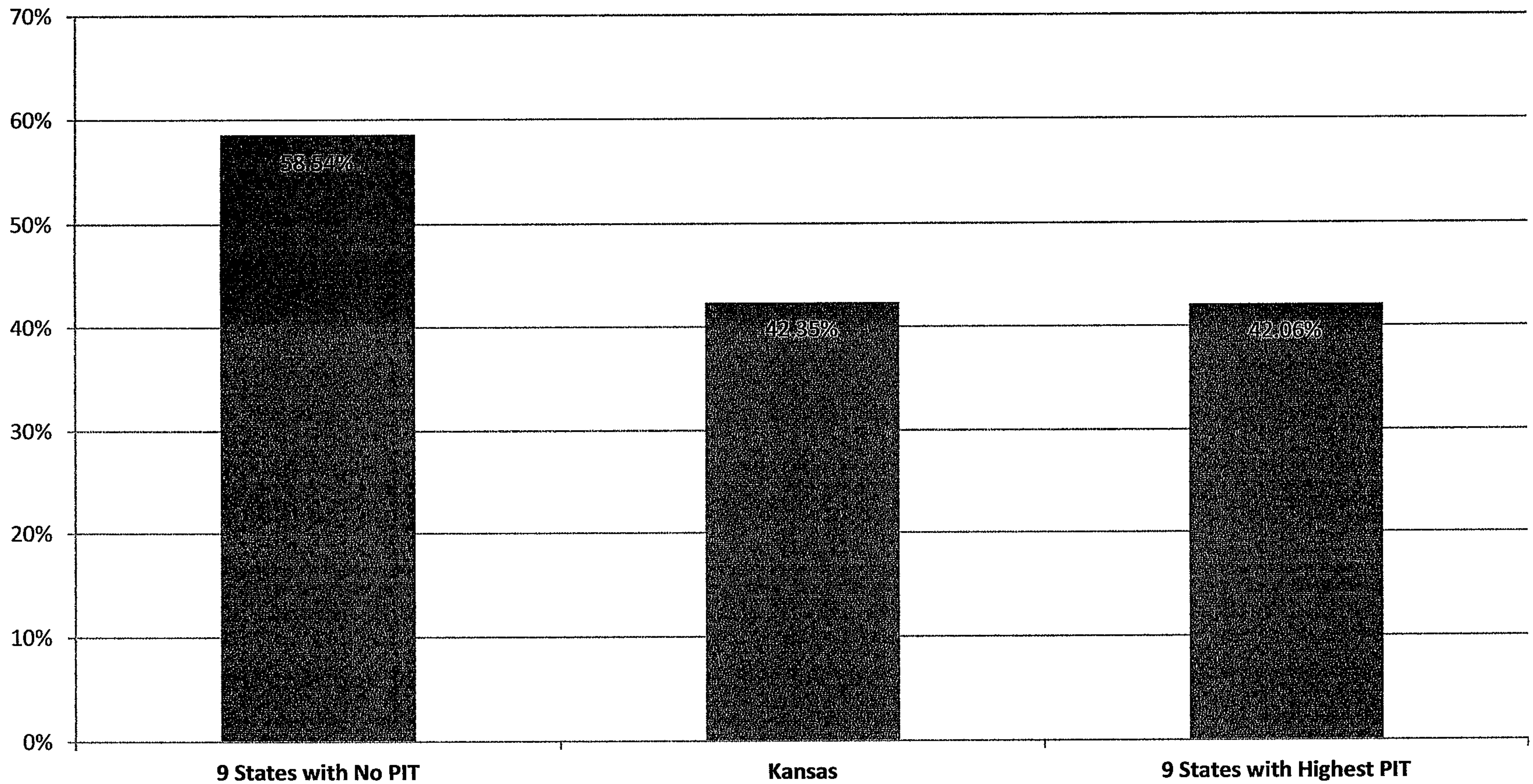


Source: Laffer Associates

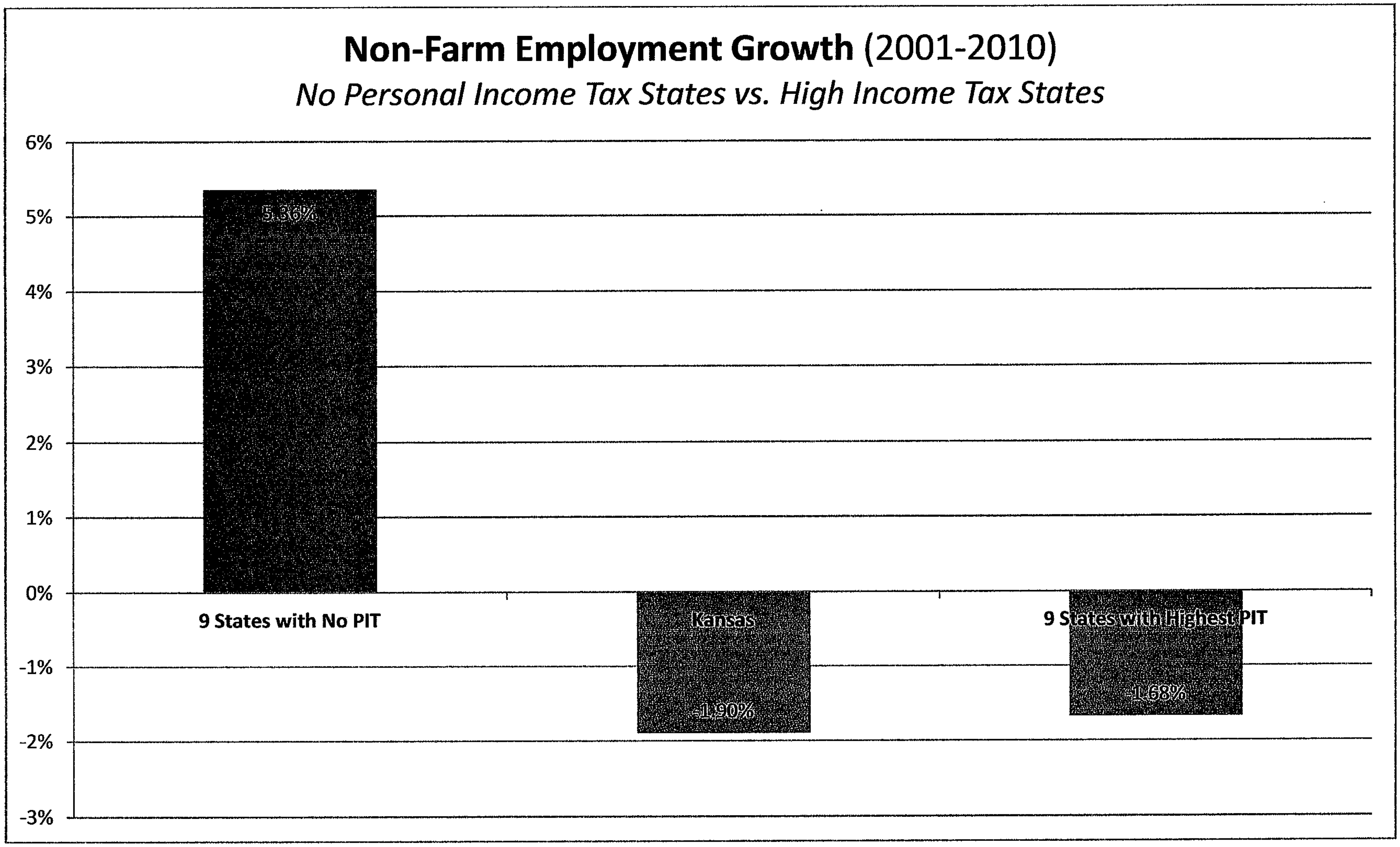
Att. 4-16

Gross State Product Growth (2001-2010)

No Personal Income Tax States vs. High Income Tax States

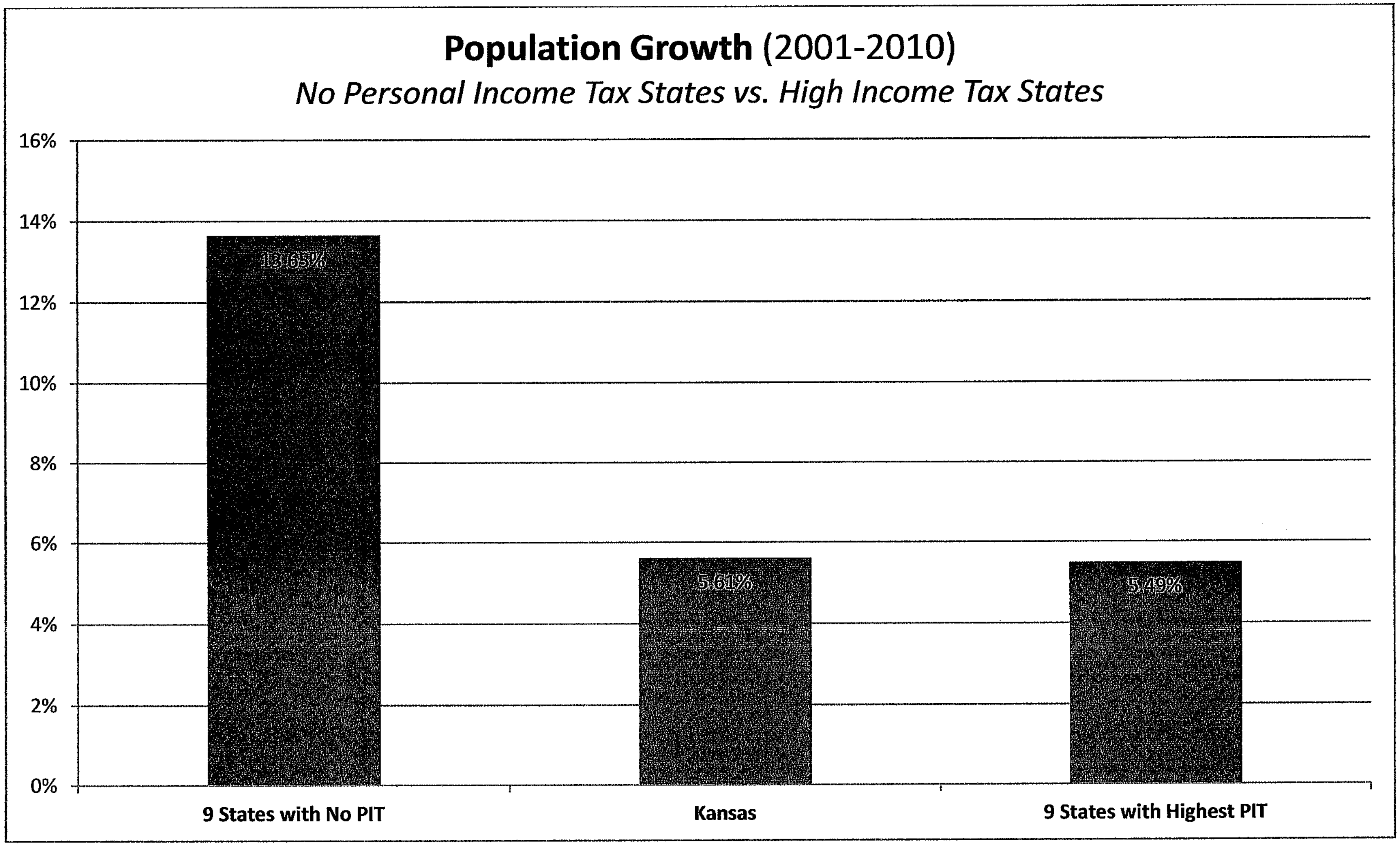


Source: Laffer Associates



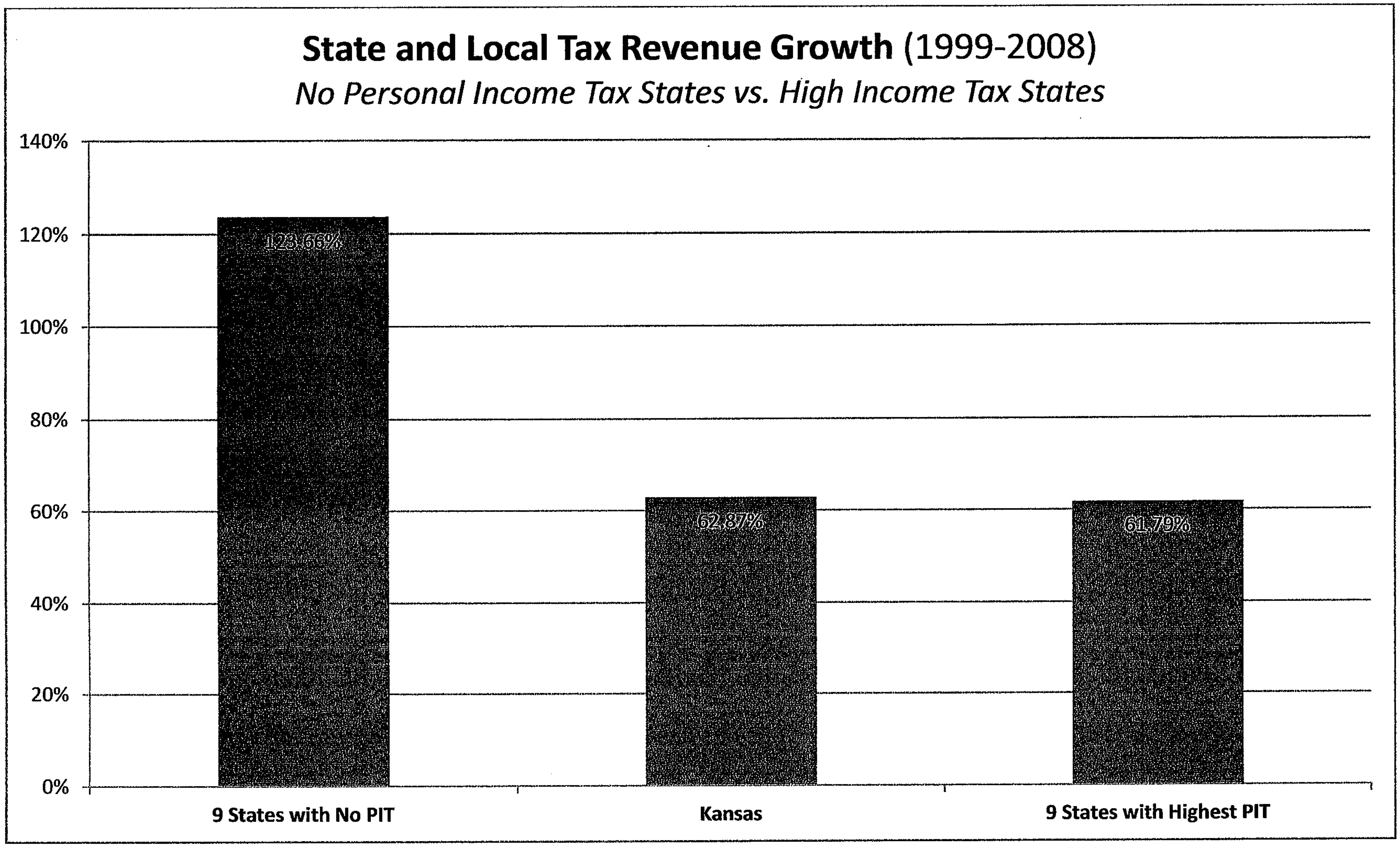
Source: Laffer Associates

Att. 4-18



Source: Laffer Associates

Att. 4-19



Source: Laffer Associates