Testimony to House Taxation Committee
HB 2178 Income Tax Increases
February 2, 2017
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Chairman Johnson and Members of the Committee,

We appreciate this opportunity to testify in opposition to HB 2178, which would increase income tax rates, eliminate the so-called 'ratchet' to reduce future tax rates and reinstate deductibility of medical expenses.

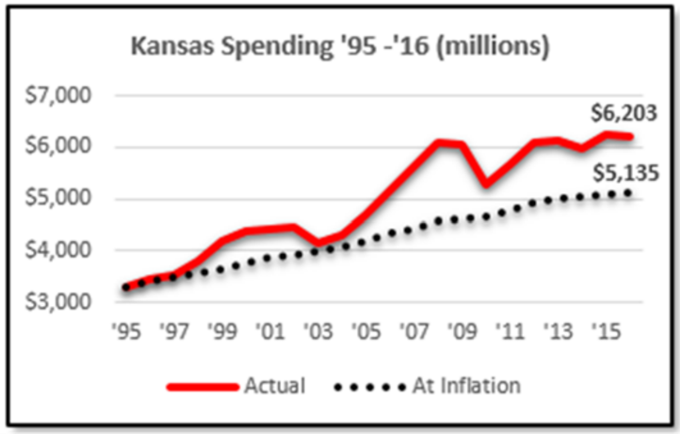
We oppose tax increases because government has a spending problem, not a revenue problem, and we believe no taxes should be increased until government is making efficient use of taxpayer money. In addition to the findings of multiple independent efficiency studies on Kansas state government, there is also the fact that Kansas spends much more per-resident than many other states providing the same basket of services.

Spending data from the National Association of State Budget Officers shows that the states that tax income spent 42 percent more per-resident in 2015 than the states without an income tax; Kansas spent 27 percent more per-resident. It's not access to natural resources or tourism that allows states to keep taxes low; it's simply the spending. The more a state chooses to spend, the more it must tax.

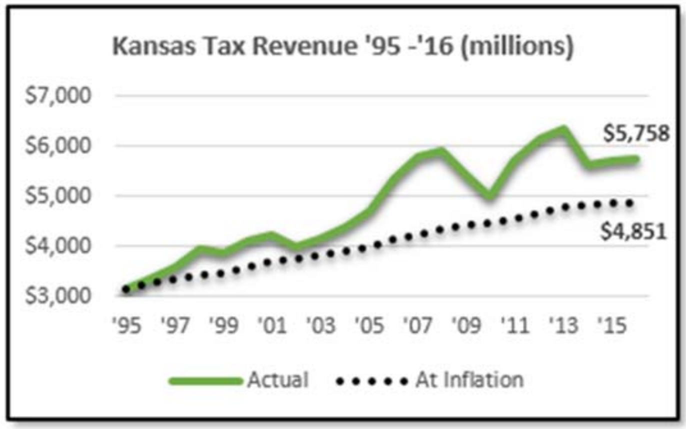
Identifying the savings opportunities takes effort, as explained by former Indiana Governor and no President of Purdue University, Mitch Daniels. He said, "This place was not built to be efficient. [But] you're not going to find many places where you just take a cleaver and hack off a big piece of fat. Just like a cow, it's marbled through the whole enterprise." Governor Daniels was speaking of Purdue but his comment applies universally to government – and also to the private sector.

The Kansas budget problems primarily arise from lack of spending control. The budget could have been balanced following passage of the 2012 legislation by having government operate about 8.5 percent more efficiently; spending thereafter could increase as revenue grew and there always would have been healthy ending balances. The need to adjust spending was well-known, but Democrats and many Republicans refused to make government more efficient, so spending and taxes were increased in 2013...and again in 2015.

Last fiscal year, General Fund spending was $6.203 billion, which is $105 million more than was spent in 2012 when tax relief was passed. Approximately $104 million of school transportation funding was also shifted from the General Fund to the All Funds budgets, so the real increase is even greater.



General Fund spending has also increased well above inflation-adjusted levels since 1995. Had 1995 spending been increased for inflation it would have been $5.135 billion but actual spending was $1.068 billion more.



And even though Kansans have been allowed to keep more of their hard-earned money, General Fund tax revenue is also well above inflation-adjusted levels since 1995. Tax revenue was $5.758 billion last year, which is $907 million more than if 1995 tax revenue had increased for inflation.

It's also unnecessary to raise taxes given the broad range of income, sales and property tax exemptions in Kansas. The income tax exemption on pass-through income creates a legitimate issue of fairness but the Legislature has long approved (and thus far declined to rescind) many other exemptions, including:

- Retirees of state universities and the Board of Regents participating in their 403(b) plan are exempt from state income tax on withdrawals. Private sector citizens are fully taxed on their pension and 401(k) withdrawals.

- Retirees of other state agencies, school districts and local government participate in the Kansas Public Employees Retirement System (KPERS). They are taxed on their personal contributions to the pension program but are never taxed on the majority of their withdrawals, which come from employer contributions and earnings on all contributions.

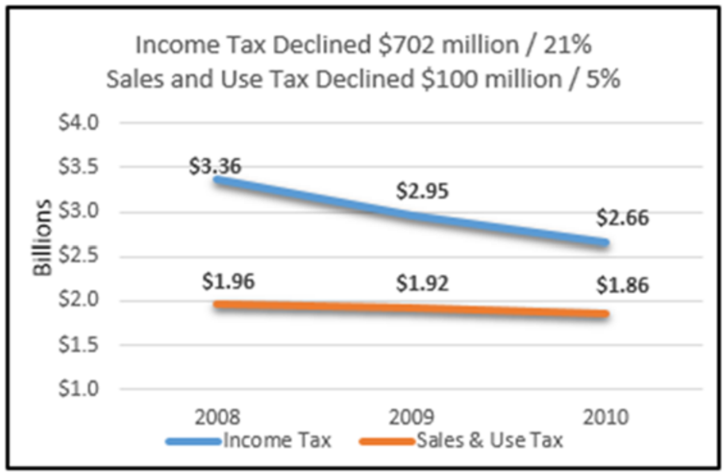
- Legislators get an even better deal. In addition to preferential tax treatment, their pensions are based on having worked a full year and earned about $85,000 instead of what they are actually paid – less than $10,000 per year.

- The Legislature allows local government to exempt chosen businesses from state and local sales tax with the use of STAR bonds and Industrial Revenue Bonds, which results in others being taxed more to make up the difference.

- The Legislature provides sales tax exemptions to a wide array business activities, services, retail purchases and many non-profit organizations (for the record, KPI pays sales tax) totaling more than $5 billion dollars annually. Some of the exempt entities even came to the Legislature one at a time asking for special treatment.

- The State of Kansas' HPIP program exempts businesses selected by government from sales tax and provides income tax credits. The PEAK program allows businesses chosen by government to keep 95 percent of their eligible employees' state income tax withholding for up to 10 years.

We do, however, oppose elimination of the so-called ratchet that would allow marginal income tax rates to decline when revenue surpasses a specified target. Kansas should continue its effort to eliminate the state income tax over time as state government and citizens would be better off funding services through sales and property tax rather than income tax.



The last recession makes this point quite clear. Income tax receipts (individual, corporate and financial institutions) plummeted 21 percent between 2008 and 2010 but retail sales and compensating use tax only declined by 5 percent. To put that in perspective, if those two revenue categories had collectively declined by 5 percent, revenue would have dropped by $266 million over two years instead of $802 million.

Citizens and the economy are also better served by moving away from an income tax. The adjacent table compares multiple private sector economic growth factors between 1998 and 2014; in every instance the states without an income tax have superior economic performance. That's not to say that taxes are the only factor of course, but taxing individuals' and employers' productivity is the most harmful to economic growth.

Private Sector Change		
Economic Measurement	States without Income Tax	States that tax income
Job Growth '98-'14	22.3%	7.8%
Wages & Salaries '98-'14	102.0%	74.0%
GDP '98-'14	121.0%	84.0%
Domestic Migration '98-'15	7.0%	-2.0%
Source: BLS, BEA, Census		

We have no issue with reinstating deductibility of medical expenses, provided that spending is reduced to offset any revenue loss.

We oppose HB 2178 and encourage the Legislature to do so as well.