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Shawn Sullivan, Director of the Budget

Sam Brownback, Governor

March 20, 2017

The Honorable Steven Johnson, Chairperson
House Committee on Taxation
Statehouse, Room 185-N
Topeka, Kansas 66612

Dear Representative Johnson:

SUBJECT: Fiscal Note for HB 2385 by House Committee on Taxation

In accordance with KSA 75-3715a, the following fiscal note concerning HB 2385 is respectfully submitted to your committee.

Under current law, individual income tax rates are set at 2.7 percent for income under $15,000 ($30,000 for married filing jointly) and at 4.6 percent for income $15,000 and over ($30,000 for married filing jointly) in tax year 2017, and the bottom rate is set to be lowered to 2.6 percent beginning in tax year 2018. HB 2385 would set the individual income tax rate at 3.9 percent for all taxpayers beginning in tax year 2018 and in all future tax years. The bill would eliminate the automatic income tax rate reduction procedure that has the potential to reduce individual income tax rates beginning in tax year 2021. The bill would only allow taxpayers to claim the current non-wage business income tax exemption if the business entity has at least one employee that receives wage income.

Estimated State Fiscal Effect				
	FY 2018 SGF	FY 2018 All Funds	FY 2019 SGF	FY 2019 All Funds
Revenue	$24,600,000	$24,600,000	$82,500,000	$82,500,000
Expenditure	$26,037	$26,037	--	--
FTE Pos.	--	--	--	--

The Department of Revenue estimates that HB 2385 would increase State General Fund revenues by $24.6 million in FY 2018 and $82.5 million in FY 2019. To formulate these estimates, the Department reviewed Kansas and Internal Revenue Service (IRS) data from tax year 2014 and tax year 2015. The Department estimates that only 30.0 percent of all nonwage business income filers would be able to claim the non-wage business income tax exemption. The Department indicated that approximately 28.0 percent of all pass-through entities issued W2s to employees that receive wage income. The shareholders of pass-through entities file Schedule E returns. The Department is unable to verify which Schedule C and Schedule F filers have employees that receive wage income. The Department assumes that 1.0 percent of Schedule C and Schedule F filers have at least one employee that receives wage income. The bill also does not allow federal net operating loss carry forwards. The Department estimates that only allowing taxpayers to claim the current non-wage business income tax exemption if the business entity has at least one employee that receives wage income would generate revenues to the State General Fund of $36.7 million in FY 2018 and $123.0 million in FY 2019. The 3.9 percent flat tax is estimate to reduce State General Fund revenues by $12.1 million in FY 2018 and $40.0 million in FY 2019. Therefore, the bill is estimated to increase State General Fund revenues by $24.6 million in FY 2018 ($36.7 million from non-wage business income minus $12.1 million from the 3.9 percent flat tax) and by $82.5 million in FY 2019 ($122.5 million from non-wage business income minus $40.0 million from the 3.9 percent flat tax).

The Department of Revenue indicates that State General Fund estimates for FY 2018 and FY 2019 are based on the November 2016 Consensus Revenue Estimate. The estimate for FY 2018 includes 30.0 percent of tax year 2018 tax liability. The estimate for FY 2019 includes 70.0 percent of tax year 2018 tax liability and 30.0 percent of tax year 2019 tax liability.

The Department of Revenue indicates that the bill would require $26,037 from the State General Fund in FY 2018 to implement the bill and to modify the automated tax system. The required programming for this bill by itself would be performed by existing staff of the Department of Revenue. However, if the combined effect of implementing this bill and other enacted legislation exceeds the Department's programming resources, or if the time for implementing the changes is too short, additional expenditures for outside contract programmer services beyond the Department's current budget may be required.

The Department of Administration indicates that adjusting state income tax collections has the potential to have a fiscal effect on the amount of revenue collected from its debt setoff program. This program intercepts individual income tax refunds and homestead tax refunds and applies those amounts to debts owed to state agencies, municipalities, district courts, and state agencies in other states. Debts include, but are not limited to child support, taxes, educational expenses, fines, services provided to the debtor, and court ordered restitution. As the dollar amounts of refunds are decreased, the amount available for possible debt setoffs is also reduced. However, the Department is unable to make an estimate of the amount of debt setoffs that will no longer be intercepted as a result of the bill. Any fiscal effect associated with HB 2385 is not reflected in *The FY 2018 Governor's Budget Report*.

Sincerely,

Shawn Sullivan,
Director of the Budget

cc: Lynn Robinson, Department of Revenue
Colleen Becker, Department of Administration