Neutral Testimony on HB2844
Modifying Income Rates, Increasing the Standard Deduction,
Modifying Income Tax on Social Security, Modifying the
Property Tax and Eliminating the Local Ad Valorem Tax
Reduction Fund

Donna K. Ginther
Director, Institute for Policy & Social Research
Roy A. Roberts & Regents Distinguished Professor of Economics
University of Kansas
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Background and Summary:

I have served as the chief academic adviser to the Governor's Tax Reform Council starting in 2019. This testimony addresses the provisions of HB 2844 on changing the Kansas tax code.

This testimony is **Neutral** on House Bill 2844 because the fiscal note is not well-understood. I will discuss my evaluation of each of the provisions of the bill.

The *Governor's Council on Tax Reform Final Report* made several recommendations that are directly related to HB2844. The recommendations included:

The Council strongly endorses Governor Kelly's Axe the Food Tax proposal and calls on the state legislature to immediately seize this historic opportunity to eliminate the state sales tax on food.

Expand the $42,049 homestead exemption from the statewide mill levy to target property tax reduction to residential homeowners.

Expand the standard deduction to provide additional income tax relief. Expanding the standard deduction impacts the largest number of Kansas individual income taxpayers.

Fund the Local Ad Valorem Tax Reduction Fund (LAVTRF) demand transfer to support reductions in local property tax levies.

I now turn to the specific provisions of the bill.

Positive: Increasing the Standard Deduction and Personal Exemptions

Compared to surrounding states, Kansas has a low standard deduction. Table 1 shows the standard deductions and personal exemptions by state in tax year 2023. Kansas has the second-lowest standard deduction while having the highest personal exemption.

HB2844 would increase the standard deduction to $3,605 for individuals, $8,240 for married filing jointly. The personal exemption would increase to $2,320 and be similarly indexed.
A change in the standard deduction and personal exemptions for a married couple filing jointly with two children reduces taxable income by $520. At the 5.7% tax rate, this provides $29.64 in tax savings to this household. After 2025, these would be indexed to the cost of living. This index

would be revised every two years. In contrast, SB 377 would increase the standard deduction for a married couple filing jointly to $10,000, reducing taxable income by $2000. At a 5.7% tax rate, this provides $114 in tax relief.

Table 1: Comparison of Standard Deductions and Personal Exemptions, Tax Year 2023

	Standard Deduction		Personal Exemption		
State	Single	Couple	Single	Couple	Dependent
Colorado	$13,850	$27,700			
Iowa (a)			$40	$80	$40
Kansas	$3,500	$8,000	$2,250	$4,500	$2,250
Missouri	$13,850	$27,700			
Nebraska (a)	$7,900	$15,800	$157	$314	$157
Oklahoma	$6,350	$12,700	$1,000	$2,000	$1,000

(a) These are tax credits in Iowa and Nebraska.
Source: Tax Foundation.

Neutral/Positive: Creating a 0% Bracket, and Reducing Marginal Tax Rates to 5.2% and 5.65%

Table 2 shows the change in tax brackets under HB 2844 for Married Filing Jointly.

Table 2 Current Law and HB 2844 for Married Filing Jointly

Current Law Income Levels	Current Law Rates	HB 2844 Income Levels	HB 2844 Rates
.01 - $30,000	3.1%	0 - $14,000	0%
$30,000.01 - $60,000	$930 + 5.25% of Excess over $30,000	$14,001 - $60,000	5.2% of excess over $14,000
$60,000.01 +	$2,505 + 5.7% of excess over $60,000	$60,000.01 +	$2,392 + 5.65% of excess over $60,000

Below, we analyze the total effect of this rate changes in the hypothetical taxpayer model. Depending on the size of the fiscal note which is not available at the time of drafting this testimony, I would be positive for these changes.

Neutral: Social Security State Income Tax Elimination

Kansas completely exempts Social Security income from taxation for most senior taxpayers. Kansas employs a taxable-nontaxable switch for Social Security income. If federal adjusted gross income (AGI) is less than or equal to $75,000, none of the Social Security payment is taxable. If AGI exceeds $75,000, the amount of Social Security that is taxable at the federal level is also taxable in Kansas. A difference of even $1 in federal AGI can mean a difference of several thousand dollars in Kansas AGI. The sudden jump in Kansas AGI income is known as a tax "cliff." A tax cliff will exist for any AGI cutoff level because the Kansas tax system does not ease in the taxability of Social Security income. Clearly the legislature should consider adjustments to ameliorate or eliminate the Social Security tax cliff.

Instead, HB 2844 phases out the income tax on Social Security income over four years. Based on the fiscal note for SB 377, the total cost would of eliminate the income tax on Social Security would be $128.1 million in FY 2028. Approximately 93,000 Kansans would have a tax break from this provision (7% of the taxpayers in the state). I am concerned about the overall price tag of this provision.

Positive: Increasing the School Levy Property Tax Exemption

Property values increased significantly in Kansas following the COVID-19 pandemic. According to Redfin, median Kansas housing prices have increased by almost 17% since December 2020. Housing prices peaked in Kansas in July 2023 and have come down to being unchanged since December 2022. HB 2844 would increase the residential exemption from $42,049 to $80,000 beginning in Tax year 2024. The $80,000 exemption would be adjusted starting in 2025 by the change in residential valuation over the previous 10 years. This provision would provide much-needed property tax relief to property owners whose valuations have increased dramatically these past three years.

Negative: Reducing State Property Tax to 18 Mills

I oppose this provision of HB 2844 because it gives much larger property tax cuts for people who own a higher-value home.

Negative: Eliminating the Local Ad Valorem Tax Relief

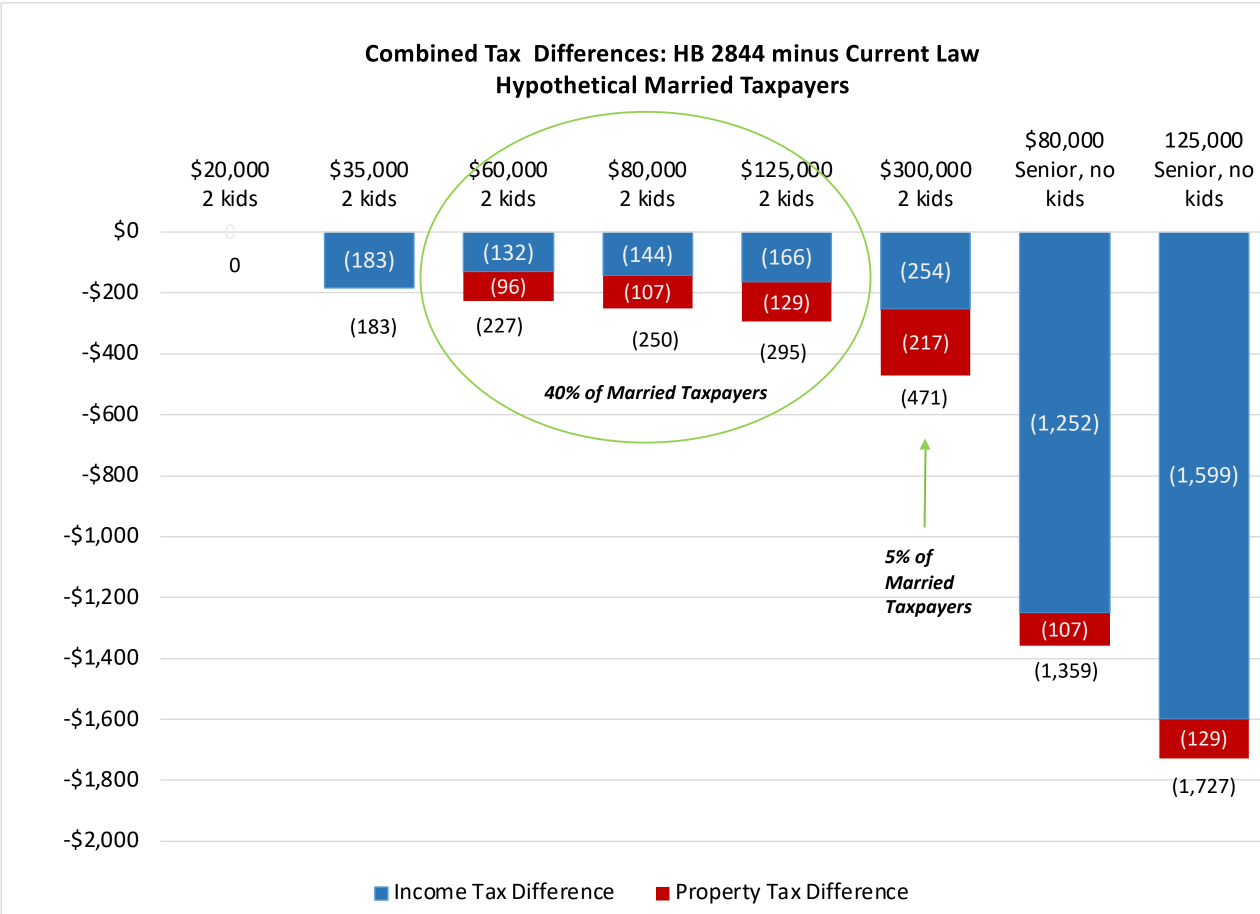
The LATVRF has not been funded for the past twenty years. However, Governor Kelly included funds for LATVRF in her budget. LATVRF funds are used by local governments to reduce the local property tax burden. Given that some counties have a much smaller tax base, the LATVRF has the potential to reduce local property tax burdens.

Putting It All Together with the Hypothetical Taxpayer Model for Married Filing Jointly

We used our hypothetical taxpayer model to calculate the tax benefits accruing by income level for a married couple household with two children who are under the age of 12. Both parents are assumed to work, and the children are in daycare. Based on total income levels, we completed federal and state tax returns under the current law and with the changes to income taxes in HB 2844. We also assumed that the house of this couple was located in Saline County and that the house value changed by income level. Couples $35,000 or less in income were assumed to be renters. Figure 1 shows the reduction in income and property taxes under HB 2284. Please note that we are showing the tax cuts from fully eliminating the state tax on Social Security.

The average tax cuts range for a low of $183 dollars to a high of $471 dollars for married households with two children. A fully phased in elimination of taxes on social security results in large tax cuts for older adult households ranging from $1252 to $1599 depending on income.

These tax cuts favor high-income households earning $300,000 a year relative to households earning $80,000 per year. Roughly 40% of married taxpayers earn between $60,000 to $125,000 per year, while only 5% of married taxpayers earn $300,000 or more.



Additional Considerations

The Bi-Partisan tax cut plan in SB 377 provided sales, property and income tax cuts. Like this bill, it eliminates the income tax on social security. Instead of changing tax rates, the standard deduction for married households increases to $10,000. The property tax exemption is higher (at $100,000) but the state mill levy remains the same. The bill doubles the child and dependent care tax credit refund, accelerates the elimination of the state sales tax on groceries, and eliminates the sales tax on diapers and feminine hygiene products. The doubling of the child and dependent care tax credit provides an additional $300 in tax cuts to households with both children in daycare. As a result, the tax cuts to married households with children under the age of 12 are close to double what is provided by HB 2844. Approximately $250 in sales tax relief was also provided to these households under SB 377.

The committee should consider accelerating the elimination of the grocery sales tax and eliminating the tax on diapers and feminine hygiene products. Depending on the overall fiscal note, increasing the child and dependent care tax credit and creating a child tax credit should also be considered.