Division of the Budget
Landon State Office Building
900 SW Jackson Street, Room 504
Topeka, KS 66612
Adam Proffitt, Director

Kansas
Division of the Budget

Phone: (785) 296-2436
adam.c.proffitt@ks.gov
http://budget.kansas.gov
Laura Kelly, Governor

March 31, 2021

The Honorable Adam Smith, Chairperson
House Committee on Taxation
Statehouse, Room 185A-N
Topeka, Kansas 66612

Dear Representative Smith:

SUBJECT: Fiscal Note for HB 2446 by House Committee on Taxation

In accordance with KSA 75-3715a, the following fiscal note concerning HB 2446 is respectfully submitted to your committee.

HB 2446 would require marketplace facilitators to start collecting Kansas retail sales and compensating use taxes on sales to Kansas customers on July 1, 2021, if the marketplace facilitator had cumulative gross receipts from retail sales sourced to this state of $50,000 or more from January 1, 2021 through June 30, 2021. The bill defines a "marketplace facilitator" as a person that has an agreement with marketplace sellers to facilitate sales through a physical or electronic marketplace. A marketplace facilitator would not include advertising services. The marketplace facilitator would also be required to collect all other taxes and fees imposed on a retail sale; however, the collection of 911 fees would be delayed until January 1, 2022. The bill would also set up a procedure that would require future marketplace facilitators to start collecting and remitting retail sales and compensating use taxes on sales to Kansas. The Department of Revenue would be allowed to audit sales of marketplace facilitators. The bill would relieve the liability of a marketplace facilitator to collect and remit the correct amount of the tax if an error was due to incorrect or insufficient information from the marketplace seller. Marketplace facilitators would not be responsible to remit any taxes from sales occurring prior to July 1, 2021; however, if a marketplace facilitator already collected these taxes voluntarily prior to that date, then they would not be eligible for a refund.

The bill would require sales taxes to be collected from all sales of digital property and subscription services beginning on July 1, 2021. The bill includes definitions for digital audio-visual works, digital audio works, digital books, digital code, and digital property. The bill also reorders the definitions section in the Kansas Retailers Sales Tax Act.

The bill would exclude unemployment compensation benefits or other compensation benefits from gross income if the benefits were secured with a fraudulent identity and the taxpayer did not receive the benefits. These benefits would not be subject to Kansas income taxes after the Department of Revenue determines the benefits were obtained fraudulently by another individual.

The bill would create a new refundable food sales tax credit and repeal the existing non-refundable food sales tax credit beginning in tax year 2021. The new tax credit amount would be determined by tax filing status and could be claimed by all taxpayers with income at or below the following federal adjusted gross income levels:

Filing Status	Income Level	Credit Amount
Single	$30,000	$ 60
Head of Household	40,000	180
Married Filing Jointly	40,000	240
Married Filing Separate	30,000	60

The bill would allow the income level and tax credit amounts to be adjusted annually beginning in tax year 2022, according to the cost-of-living adjustments from the federal Internal Revenue Service (IRS). The bill would require each county treasurer to include information from the Department of Revenue about claiming the refundable food sales tax credit in the annual property tax statement. The Department of Revenue would have the authority to write rules and regulations to implement the bill.

Calculations for Kansas income taxes are based on the Kansas adjusted gross income, which is calculated by adding or subtracting certain types of income from the federal adjusted gross income. The bill would allow the amount of disallowed business interest expenses to be subtracted from income for Kansas income tax purposes beginning in tax year 2021. Additionally, all deductions from the carry forward amount of disallowed business interest would be added back for Kansas income tax purposes beginning in tax year 2021. This would allow state taxpayers to claim the full amount of business interest expenses on state income tax returns.

The bill would allow 100.0 percent of global intangible low-taxed income (GILTI), before allowable deductions, to be subtracted from income for Kansas income tax purposes beginning in tax year 2021. This would exempt this income from state income taxes. The bill would allow the amount of disallowed meal expenses to be subtracted from income for Kansas income tax purposes beginning in tax year 2021. This would allow state taxpayers to claim the full amount of meal expenses on state income tax returns.

The bill would allow the amounts received from the federal Paycheck Protection Program (PPP) to be subtracted from income for Kansas income tax purposes beginning retroactively in tax year 2020, if these amounts were included in the taxpayer's federal adjusted gross income. All amounts included in the taxpayer's federal adjusted gross income would be exempt from state income taxes. The bill would provide that the expenses from PPP loans that are not allowed as a deduction in determining federal adjusted gross income would be allowed to be subtracted from income for Kansas income tax purposes beginning retroactively in tax year 2020.

Corporate taxpayers would be allowed to exclude contributions to capital from non-shareholders in the calculation of state income taxes beginning in tax year 2021. This provision would exclude contributions by a governmental entity or civic group such as the values of state and local tax incentives from the calculation of income. Deferred foreign income (federal repatriation) would be classified as foreign dividends qualifying for the 80.0 percent deduction.

The bill would increase the standard deduction for single individual taxpayers from $3,000 to $4,250, married filing status from $7,500 to $8,500, and head of household from $5,500 to $6,500 beginning in tax year 2021. The bill would also remove outdated standard deduction language from previous tax years.

Under current law, Kansas corporations, banks, trust companies, and savings and loans can claim the Kansas expensing deduction for investments in qualifying machinery and equipment that are placed into service in Kansas for tax year 2014 and each future tax year. The bill would also allow individual income taxpayers to claim the expensing deduction beginning in tax year 2021. All taxpayers claiming the Kansas expensing deduction would be required to offset the costs of the expensing deductions claimed on the federal return with Section 179 of the Internal Revenue Code.

Estimated State Fiscal Effect				
	FY 2021 SGF	FY 2021 All Funds	FY 2022 SGF	FY 2022 All Funds
Revenue	--	--	($94,300,000)	($77,700,000)
Expenditure	--	--	$951,256	$951,256
FTE Pos.	--	--	--	9.00

The Department of Revenue estimates that HB 2446 would decrease state revenues by $77.7 million in FY 2022. Of that total, the State General Fund is estimated to decrease by $94.3 million in FY 2022, while the State Highway Fund is estimated to increase by $16.6 million in FY 2022. Given that the Department of Revenue does not have data to make precise estimates of some of the tax policy changes, the fiscal note of the bill is likely to be higher. This bill also is estimated to increase local sales tax revenues; however, the specific estimate of higher local sales tax revenues was not calculated by the Department of Revenue. The estimated fiscal effect by specific tax policy change would be as follows:

Tax Policy Changes (SGF Only)	FY 2022	FY 2023	FY 2024
Marketplace Facilitator	$ 43,100,000	$ 49,400,000	$ 51,900,000
Digital Goods	42,700,000	48,900,000	51,400,000
UI Fraud	--	--	--
Refundable Food Tax Credit	(53,900,000)	(55,500,000)	(57,200,000)
Disallowed Business Interest	(30,600,000)	(37,500,000)	(38,600,000)
GILTI	(24,200,000)	(23,500,000)	(23,700,000)
Disallowed Meal Expenses	--	--	(3,000,000)
PPP	Unknown	Unknown	Unknown
Capital Contributions	Negligible	Negligible	Negligible
Deferred Foreign Income	--	--	--
Standard Deduction	(73,700,000)	(57,300,000)	(57,900,000)
Expensing Deduction	2,300,000	2,400,000	2,500,000
Total SGF	($94,300,000)	($73,100,000)	($74,600,000)

Tax Policy Changes (SHF Only)	FY 2022	FY 2023	FY 2024
Marketplace Facilitator	$ 8,400,000	$ 9,600,000	$ 10,100,000
Digital Goods	8,200,000	9,400,000	9,900,000
Total SHF	$ 16,600,000	$ 19,000,000	$ 20,000,000
Total	($77,700,000)	($54,100,000)	($54,600,000)

To formulate the estimates for increased sales tax authority from remote sellers, the Department of Revenue reviewed data from the U.S. Government Accountability Office (GAO) that released a study on sales taxes in November 2017. The report shows that Kansas has the potential to receive an additional $113.0 million to $170.0 million each year in increased state and local sales tax collections with expanded collection authority with out-of-state remote sellers. The numbers quoted from GAO include both state and local sales tax collections and the amounts that the state already receives from Streamlined Sales Tax Volunteer Filers. Making these adjustments, the Department of Revenue estimates that Kansas would likely collect $51.5 million in FY 2022 specifically from marketplace facilitators, including $43.1 million from the State General Fund and $8.4 million from the State Highway Fund. The fiscal effect associated with requiring marketplace facilitators to start collecting retail sales and compensating use taxes is reflected in *The FY 2022 Governor's Budget Report*.

To formulate the estimates for requiring sales taxes for digital property and subscription services, the Department of Revenue reviewed industry data on music, video games, and other online media subscription services, and reviewed data from other states that tax the sale of digital products. The Department indicates that 30 of the 45 states that have a retailer's sales tax, include the sale of digital products in their sales tax base. The fiscal effect associated with requiring sales taxes to be collected from all sales of digital property and subscription services is reflected in *The FY 2022 Governor's Budget Report*.

The Kansas Department of Transportation indicates that the bill would increase state revenues to the State Highway Fund as noted above. The additional revenues would fund additional expenditures for projects funded under the comprehensive transportation plan. The Kansas Association of Counties and the League of Kansas Municipalities indicate that the bill would provide a net increase to local sales tax collections that are used in part to finance local governments.

The Department of Labor and the Department of Revenue both indicate that the provision of the bill that allows taxpayers to exclude fraudulent unemployment compensation benefits from gross income would have no fiscal effect. Victims are not held accountable for taxes on unemployment compensation benefits related to identity theft.

To formulate the estimates from creating a new refundable food sales tax credit and repealing the existing non-refundable food sales tax credit, the Department reviewed tax return data from tax year 2019. The Department created a simulated tax table for all taxpayers that would be eligible for the new refundable food sales tax credit. The Department of Revenue estimates that more than 540,000 tax returns would claim $63.9 million in new refundable food sales tax credits beginning in FY 2022. The Department estimates that the number of tax returns grows approximately 1.0 percent each year and the cost of living adjustment would increase by 2.0 percent each year.

The bill would repeal the current non-refundable food sales tax credit after December 31, 2020. The current non-refundable food sales tax credit is restricted to taxpayers that earn $30,615 or less and are over the age of 55, or disabled or blind, or have at least one dependent under the age of 18 living with them the entire year. Under the provisions of the federal Tax Cut and Jobs Act of 2017, the IRS no longer collects the number of dependent exemptions claimed on federal income tax returns, which places the burden to verify and audit dependent exemption data for the current food sales tax credit on the Department of Revenue. The Department of Revenue indicates that 70,090 taxpayers claimed $9,847,101 in non-refundable food sales tax credits in tax year 2018. Repealing this tax credit would save approximately $10.0 million in State General Fund refunds in FY 2022.

The net effect of repealing the current non-refundable food sales tax credit and creating the new refundable food sales tax credit are estimated to reduce State General Fund receipts by $53.9 million in FY 2022 ($10.0 million for repealing the current non-refundable food sales tax credit minus $63.9 million for the new refundable food sales tax credit).

The Kansas Association of Counties indicates that the new refundable food sales tax credit portion of the bill would require county treasurers to include additional information with the annual property tax statement. The Association indicates that the bill would likely require counties to incur programming and coding costs to include this information with the annual property tax statement. However, the Association did not provide a precise estimate of the amount of additional programming and coding costs for counties.

To formulate the estimates related to decoupling from the Tax Cuts and Jobs Act of 2017 or the CARES Act, the Department of Revenue indicates that it used information from the federal Joint Commission on Taxation to estimate the impact of all federal tax policy changes on Kansas. The Department does not have any data to estimate the fiscal effect of allowing individual taxpayers the ability to deduct GILTI income before any deduction. Meal expenses are currently allowed to be to be subtracted from income at the federal level for tax year 2021 and tax year 2022, so this provision would have no fiscal effect on state income tax receipts until tax year 2023 or FY 2024. The Department is unable to determine the impact of the PPP provisions because it is unclear the amount of the loans that will not be forgiven at the federal level. The exclusion of certain contributions to capital would reduce State General Fund receipts by a negligible amount. Deferred foreign income is already treated as foreign dividends and qualifies for the 80.0 percent deduction, so this provision would have no fiscal effect.

To formulate these estimates for increasing the standard deduction, the Department of Revenue simulated this tax policy change based on actual tax return data from tax year 2019. The estimate for FY 2022 includes 100.0 percent of tax year 2021 tax liability and 30.0 percent of tax year 2022 tax liability. The estimate for FY 2023 includes 70.0 percent of tax year 2022 tax liability and 30.0 percent of tax year 2023 tax liability.

To formulate the estimates on allowing expensing for individual income taxpayers and requiring the Section 179 of the Internal Revenue Code offset, the Department of Revenue reviewed data from tax year 2012, which was the last tax year that individual income taxpayers were allowed to claim the expensing deduction. The Department of Revenue indicates that all State General Fund estimates for FY 2022 are based on the November 2020 Consensus Revenue Estimate. The Department estimates that the number of tax returns would increase by 1.0 percent each year.

The Department of Revenue indicates that it would require a total $951,256 from the State General Fund in FY 2022 to implement the bill and to modify the automated tax system. The bill would require the Department to hire 9.00 new FTE positions to answer questions from taxpayers and to review, process, and audit marketplace facilitator compliance; to review and process state returns that include the new refundable food sales tax credit; and to review, process, and audit additional income tax returns. The required programming for this bill by itself would be performed by existing staff of the Department of Revenue. In addition, 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 increased, the amount available for possible debt setoffs is also increased. However, the Department is unable to make an estimate of the amount of additional debts setoffs that will be intercepted as a result of the bill.

A provision in the federal American Rescue Plan Act of 2021 (ARP) prohibits states or territories from using the federal funds appropriated from ARP "to either directly or indirectly offset a reduction in the net tax revenue of such State or territory resulting from a change in law, regulation, or administrative interpretation during the covered period that reduces any tax (by providing for a reduction in a rate, a rebate, a deduction, a credit, or otherwise) or delays the imposition of any tax or tax increase." If the state fails to comply with this provision by implementing a reduction of net tax revenue through tax year 2024, the U.S. Treasury would be required to recoup ARP funds in the amount of the net tax revenue reduction. If ARP funds are not available, it is presumed that the State General Fund would be used to reimburse the U.S. Treasury.

Sincerely,

Adam Proffitt
Director of the Budget

cc: Lynn Robinson, Department of Revenue
Wendi Stark, League of Municipalities
Jay Hall, Association of Counties
Ben Cleeves, Transportation
Jeff Scannell, Department of Administration
Dawn Palmberg, Department of Labor