Approved: 4-30-10
Date

MINUTES OF THE SENATE COMMERCE COMMITTEE

The meeting was called to order by Chairperson Karin Brownlee at 8:30 a.m. on March 16, 2010, in Room 548-S of the Capitol.

All members were present.

Committee staff present:
Ken Wilke, Office of the Revisor of Statutes
Reed Holwegner, Kansas Legislative Research Department
Kathie Sparks, Kansas Legislative Research Department
Marilyn Arnone, Committee Assistant

Conferees appearing before the Committee:
Katrin Osterhaus, Legislative Division of Post Audit

Others attending:
See attached list.

Chairperson Brownlee welcomed Katrin Osterhaus from Legislative Division of Post Audit to the committee for a review of two Post Audit Reports, Kansas Tax Revenues, Part I: Reviewing Tax Credits and Kansas Tax Revenues, Part II: Reviewing Sales Tax Exemptions. (Attachment 1)

3/16

Ms. Osterhaus stated she would review two parts of the tax audit series dealing with tax credits and sales tax exemptions. Most of the State's $5.3 billion in State General Fund revenues come from income and sales tax collections. However, over the past decades, Kansas has come to rely more heavily on income tax to fund State operations. The shift away from sales tax is attributed to more sales occurring on the internet which is exempt from sales tax, a shift toward a more service oriented economy, and a proliferation of sales tax exemptions. Tax credits reduce State revenues because the credits are subtracted directly from the amount of taxes the taxpayer otherwise would have to pay. These have increased $170 million over the past three years. Sales tax exemptions cost the State an estimated $3 billion in 2003, and have increased to about $4.2 billion in 2009.

The various tax policy considerations were categorized into three broad categories that were used for the Post Audit. The first category includes things that policymakers are required to exempt from taxation because of Federal laws or the State Constitution. The second includes things that policymakers need to exempt from taxation in order to avoid double taxations, or to ensure that taxes are paid on the end product only. The third category includes things that policymakers decide-from a public policy standpoint-to exempt from taxation.

The first question is, " Does Kansas Have Tax Credits that Aren't Accomplishing their Intended Purpose, or Have Outlived Usefulness?" Kansas currently has 47 tax credits as well as two tax refund programs. Thirteen credits had been enacted in 2006 or later, many supporting energy-related businesses. These credits are so new with little activity as yet, and were not evaluated. Eight credits and one refund program appear to be accomplishing the legislature's policy goals. The High Performance Incentive Program (HPIP) credit was evaluated by Dr. Hall from the University of Kansas, who concluded that the benefit of this credit likely justifies the cost.

Eight tax credits were identified that appear to be likely candidates for being repealed because of little or declining use. The Agritourism Liability Insurance credit benefited only about 25 taxpayers each year, and it wasn't determined if these businesses would have started up if they hadn't received the credit. Seven tax credits could be modified. Kansas' Earned Income Tax credit is calculated based on 17% of a taxpayers' federal earned income credit. Other states offer a much lower percentage. The Angel Investor credit has a rate of 50%. This credit likely reduces market barriers for high-risk start-up companies, and reductions in the credit rate may reduce investment levels. The Center for Entrepreneurship credit could be modified. This credit allows a taxpayer to make a contribution for which the state provides a 75% tax credit. The same contribution can also be deducted on the taxpayer's federal income tax return. Kansas currently doesn't require the deduction to be added back in for the Kansas tax return as is required for some other tax credits. This means that the taxpayer can receive a double benefit from the same contribution that was made. Chairperson Brownlee asked if this was the only credit that had a double benefit and the answer was yes it is. Senator Reitz asked about the Homestead Property Tax Refund. Ms. Osterhaus said this tax credit was hard to compare because of the varying property values and the Kansas structure is too different to be compared to other states. Kansas' credit is much higher than surrounding states.

Twelve remaining tax credits were identified tax for consideration. These particular credits would need to be re-evaluated by the Legislature as to whether they provide a good balance between funding needs and public policy goals. Dr. Hall found the Business and Job credit provides too small of an incentive for businesses to make investment decisions based on the credit. For example, a company may receive as little as $100 for $100,000 investment. However, Department of Commerce officials cite this credit as in important part of their economic development toolbox.

The Historic Preservation Credit's transfer option, in addition to being significantly more expensive than expected, makes this credit not cost effective for the state. However, this credit accomplishes its purpose by allowing about 600 projects to be completed. This aids economic development and revitalizes neighborhoods.

The Business Machinery and Equipment credit, the Telecommunications and Railroad credit and the Credit for Salaries Paid to Kansas Employees also fall into this category.

Conducting work on this audit also revealed a couple of issues related to the accuracy of the Department of Revenues' tax credit data. This included a number of data reliability issues within the individual tax credit databases, and inaccurate aggregate cost data for several tax credits, such as understated costs for the Business and Job Development and High Performance Incentive Program Credit. The audit shows that Kansas generally lacks a strong system for reviewing evaluating tax credits. Another finding was that Kansas doesn't routinely merge information about tax credits that are processed by the Department of Revenue and the 20 credits the Insurance Department processes which cost the state about $75million. Without information from both sources, the Legislature doesn't have a complete picture.

Chairperson Brownlee asked what it would take to make the merging of information between the Revenue Department and the Insurance Department happen. Would it require a statute? Ms. Osterhaus did not think it would require a statute but an understanding between the two departments that the information would be included in the Revenue Department.

The Credit for Salaries Paid to Kansas Employees is a tax credit for insurance companies that cost nearly $50 million in 2007. This credit can be claimed by companies even though they don't have staff in Kansas. However, the Insurance Department officials say this credit contributes to insurance companies locating or staying in Kansas.

Chairperson Brownlee asked what was the underlying problem that accurate evaluations were not being made. Is information not being extracted properly? Ms. Osterhaus said that as far as statutes were concerned, things could be fixed by the legislature. It needs to be determined what needs to be evaluated, how information is to be evaluated, what information needs to come out of an evaluation. Those things should be in the statute which means they will have to be followed. Chairperson Brownlee said trying to get these mechanisms in place for tracking has been a frustration for a number of years.

The second question is "What transferable tax credits exist in Kansas, and Are they a Cost-Effective Means of Generating Money to Fund Certain Types of Projects or Causes?" Of the 47 available credits, Kansas has 4 that are transferable which means a taxpayer can sell their tax credit to someone else to use. The transfer feature is cost-effective for three of the four credits for the state. That feature is not cost-effective for the Historic Preservation Credit.

Part II of the presentation deals with sales tax exemptions. The question is, " Does Kansas Have Sales Tax Exemptions that Potentially Should be Considered for Elimination?" Sales Tax exemptions have steadily risen from 30 in 1985 to the 99 currently existing exemptions. In addition to the forgone revenues from exemptions estimated to cost 4.2 billion in fiscal year 2009, the Legislature enacts new exemptions and frequently broadens existing ones. For evaluation, the sales tax exemptions were grouped into the same three groups (must exempt, need to exempt, and decide to exempt as matter of public policy). Six exemptions are legally required including exemption of groceries purchased through the federal food stamp program which cost an estimated $32 million.

The second group includes conceptual exemptions which are those that avoid double taxation and ensure that sales taxes are collected at the point of final sales. Six exemptions in this group account for the majority of the estimated total of lost revenues, at about $3 billion. The next 15 exemptions in this group are those granted to governmental entities which is in line with tax policy considerations. These cost an estimated $460 million.

The remaining sales tax exemptions have been created as a matter of public policy. Two agricultural exemptions are estimated to cost about $50 million, 11 business-related exemption at about $215 million. This group also included charitable, religious or benevolent exemptions. There are several exemptions for consumers, 4 exemptions related to services, and some exemptions relate to health care. There are 44 individually named non-profit organizations as exempt. Four exemptions were identified to not apply to a broad group or class of taxpayers and could create unfair advantages to similar non-profit entities that aren't exempted. A number of exemptions are granted to certain non-profit entities, but not their for-profit counterparts. Last, Kansas currently exempts a number of IRS recognized non-profit organization, but there are still thousands that don't have sales tax exemptions and this inconsistency puts non-profits on an unequal footing.

There are a number of exemptions that could be discontinued to stop the erosion of the state and local tax base. Prescription drugs, labor services, professional, and personal care services are examples of these type of exemptions. However, there are other factors involved for keeping each of these exemptions.

Chairperson Brownlee thanked Ms. Osterhaus for her very helpful and informative presentation.

The next meeting is scheduled for March 17, 2010.

The meeting was adjourned at 09:30 a.m.

COMMERCE COMMITTEE GUEST LIST

DATE: 3-16-10

NAME	REPRESENTING
Marlee Carpenter	KS CPA
Jim Moag	Spirit AeroSystems
Jerri Rose	KCSL
Natalie Haag	Security Benefit
Ashley Dopita	Pinegar, Smith & Assoc.
Chad Austin	KHA
Tom Riederer	SW Johnson County EDC.
Lindsay Holwick	Kansas Bioscience Authority
Kathryn Osterhaus	LPA
Barb Hinton	LPA

Senate Commerce Committee – Tuesday, March 16, 2010; 8:30 a.m.

Thank You, Madam Chair, and members of the Committee!

I'm here to present the first two parts of our tax audit series dealing with tax credits and sales tax exemptions.

I'll cover a few things from the overview, which starts on page 4.

First of all, most of the State's $5.3 billion in State's General Fund revenues come from income and sales tax collections. Over the past several decades, Kansas, as many other states, has become more reliant on income taxes and less reliant on sales taxes to fund State operations. On page 6, you see this graphically, with the black slice of the pie charts shrinking from 1960 to 2009.

This shift away from sales taxes can be attributed to such things as more sales occurring on the internet, for which sales taxes can't always be collected, a shift toward a more service oriented economy, and a proliferation of sales tax exemptions

Tax credits and exemptions significantly reduce the potential tax revenues:

- Tax credits - which government often offers to induce taxpayers to do certain things - reduce the State's revenues because the credits are subtracted directly from the amount of taxes the taxpayer otherwise would have to pay. Forgone revenues from credits have increased from about $500 million in 2004 to almost $670 million in 2007.

- Sales tax exemptions cost the State an estimated $3 billion in 2003, and have increased to about $4.2 billion in 2009. When purchases are exempted from sales taxes, the tax base shrinks. At the current 5.3% tax rate, having less items that are taxed means fewer revenues, unless the tax rate is increased to compensate for the loss.

Because of the large number of tax credits and exemptions involved in this audit series (about 240 in all), we weren't able to do a detailed cost-benefit analysis on each tax credit or exemption. Instead, we reviewed various studies, tax policy guidelines and other tax literature, talked to experts from various entities, and interviewed officials from several state agencies and organizations from Kansas and other states.

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Based on this work, we learned that the fairest tax system is one that can be uniformly applied to the broadest base of people, goods and services, and that exemptions should be the exception not the rule. We also learned that a number of legitimate reasons exist for allowing certain entities or transactions not to be taxed.

In the end, we categorized the various tax policy considerations we learned about into three broad categories which we used to conduct our work.

The first category includes things that policymakers ***are required to*** exempt from taxation because of Federal laws or because of the State Constitution
The second category includes things that policymakers ***need to exempt*** from taxation in order to avoid double taxation, or to ensure that taxes are paid on the end product only
The third category includes things that policymakers ***decide - from a public policy standpoint*** - to exempt from taxation.

If you turn your to page 14, the table shows these tax policy considerations. Aside from the Constitutional or federal laws that require certain tax preferences to exist, the lower part of that figure provides the tax policy considerations we used as part of our evaluation. For example, tax policy considerations that would speak for having a credit or exemption include #4 – reducing market barriers, or #5 encouraging economic growth and development. Down further in the figure, we list tax policy considerations that would favor not having a credit or exemption, for example #1 – not being able to articulate or measure the purpose of the tax preference, or #6 – significantly eroding the State's tax base.

This is the framework we used to evaluate tax credits in this Part I and sales tax exemptions in part II.

This gets me to Question 1, which starts on page 15: Does Kansas Have Tax Credits that Aren't Accomplishing their Intended Purpose, or Have Outlived their Usefulness?

Kansas currently has 47 tax credits as well as two tax refund programs (the Homestead Property Tax Refund and the Food Sales Tax Refund).

We provided a summary of each credit and refund program which starts on page 17 of the report. As you can see, the tax credits are organized by major category (such as assistance for low-income individuals or business/economic development). Within each group, we listed each credit or refund program, its purpose, how it's calculated, and its effective date.

The far-right of the table also shows the number of filers and the cost to the State.

If you flip to page 24-25, you see the credits and refund programs in the same order as in the previous figure, this time showing the tax filer and cost information for 4 years instead of just one.

For the next few minutes, I'll cover our assessment on these tax credits and refunds.

On pages 26-27, we listed 13 numbered credits that had been enacted in 2006 or later , and you'll note that many of these relate to a recent push to support energy-related businesses. Because these credits were so new and had minimal or no activity yet, we couldn't evaluate their effectiveness.

We identified eight credits and one refund program that appear to be accomplishing the legislature's policy goals. They are listed starting on page 27. For example, the "High Performance Incentive Program Credit" was evaluated by Dr. Hall from the University of Kansas, who concluded that the benefit of this credit likely justifies the cost of this credit. Another credit in this list is the regional foundation credit which has been successful at generating an increased amount of contributions to help educate and assist small businesses.

Next, we identified eight tax credits that appear to be likely candidates for being repealed. Most of these tax credits had little to no use, or declining use over time. Forgone revenues from these credits totaled less than $100,000. Figure on page 29 shows more details about these credits. For example, the Agritourism Liability Insurance Credit benefited only around 25 taxpayers each year, and it can't be determined whether the benefitting businesses wouldn't have started up, if they hadn't received the credit.

We identified seven tax credits that could be modified. If you follow along in the report, these credits are listed in ***Figure 1-4*** on pages 30 and 31. On page 30, you'll see six credits that are structured more generously in Kansas compared to similar credits in some of the neighboring states. For example, Kansas' "Earned Income Tax Credit" is calculated based on 17% of a taxpayers' <u>federal</u> earned income credit. Colorado and Nebraska offer a 10% credit, while Oklahoma offers only 5%. If Kansas rolled its credit back to 10%, it would have saved an estimated

$26 million, based on the approximately 198,000 taxpayers using this tax credit in 2007.

Another example is the Angel Investor credit. Kansas' rate for this credit is 50%, while 12 of 18 States that offer this credit established lower rates for this credit. On the other hand, this credit likely reduces market barriers for high-risk start-up companies, and reductions in the credit rate may reduce investment levels. Kansas' Research & Development credit provides a 6.5% credit on applicable expenditures, compared to Colorado's credit which is set up at 3%. One thing to keep in mind is that our comparisons with other states were made tax credits we could readily determine to be similar. The problem is that the comparison state may provide other incentives that Kansas doesn't have.

I did want to highlight the Center for Entrepreneurship credit on page 31 which is included in the group of credits that could be modified. This credit allows a taxpayer to make a contribution for which the State provides a 75% tax credit. The same contribution also can be deducted on the taxpayers' federal income tax return. Kansas currently doesn't require the deduction to be added back in for the Kansas tax return, as is required for several other tax credits. This means that the taxpayer can receive a double benefit from the same contribution he or she has made.

What's left are twelve tax credits. For these credits, we identified tax considerations for both maintaining them, and for not having them. We couldn't substitute our judgment for the Legislature's when it comes to policy decisions. Instead, we summarized the various considerations in a format to allow the Legislature to re-evaluate whether these credits provide a good balance between funding needs and the public policy goals. I'll walk through a few examples next:

These tax credits are shown in the table starting on page 32. The business and job development credit, shown on the bottom of page 32 is listed here because this credit likely doesn't cause, but simply subsidizes business actions. Dr. Art Hall from the University of Kansas found this credit provides too small of an incentive for businesses to make investment decisions based on the credit. For example, a company may receive as little as $100 for a $100,000 investment. At a cost of over $11 million, this credit significantly erodes tax revenues.

On the other hand, Department of Commerce officials cite this credit as an important part of their economic development toolbox, and all surrounding states have similar credits.

On top of page 33, you'll see the Historic Preservation Credit, which has proven to be significantly more expensive than expected. In addition, its transfer option makes this credit not cost effective for the State. However, this credit accomplishes its purpose by allowing about 600 projects to be completed so far, which aids economic development and revitalizes neighborhoods.

For the Business Machinery and Equipment as well as the Telecommunications and Railroad Credit, the primary consideration is their potential to cause competitive inequities between businesses. These inequities are the result of the 100% property tax exemption that was enacted in 2006. In essence, businesses with older equipment can get the credit which reimburses them for 25% of their property tax. Businesses that have purchased new equipment since the property tax exemption was enacted don't have to pay ANY property taxes.

On page 34, I want to cover the Credit for Salaries Paid to Kansas Employees. This is a tax credit for insurance companies and cost nearly $50 million in 2007. Because of this tax credit's affiliate provision, the credit can be claimed by companies even though they don't have staff in Kansas. Further, none of the surrounding states offer this credits. However, Insurance Department officials say this credit contributes to insurance companies locating or staying in Kansas.

While conducting our work for the audit, we also noted a couple of issues related to the accuracy of the Department of Revenues' tax credit data, including a number of data reliability issues within the individual tax credit databases, and inaccurate aggregate cost data for several tax credits, such as understated costs for the Business and Job Development and High Performance Incentive Program Credit.

The figure on page 36 demonstrates several cost and outcome data based on the original and revised data we received for these two credits: For example, the cost for the B&J Development credit was understated by 2.3 million, while the number of created jobs were overstated by 2,122.

We also found that Kansas generally lacks a strong system for reviewing and evaluating tax credits. First, Kansas generally doesn't adhere to best practices when it comes to reviewing and evaluating tax credits – those are outlined starting on page 37, and include:

- The law should set out a specific and measurable purpose for each tax credit

- A designee that's responsible to collect the data needed to help evaluate the success of the credit
- Tax credits and exemptions should have sunset provisions to ensure they are reviewed on occasion
- There should be transparency to allow the public to know who benefits from tax credits.

Secondly, while Kansas has a statute requiring an annual cost-effectiveness study on economic development credits, it doesn't specify which credits are to be included. Additionally, the law doesn't specify details as to the type of evaluation envisioned. Other states provide more guidance on what such evaluations should involve.

Our last finding in this question is that Kansas doesn't routinely merge information about tax credits that are processed by the Department of Revenue and the 20 credits the Insurance Department processes, which cost the State about $75 million. Without information from both sources, the Legislature doesn't have a complete picture.

Next, I'll cover our main findings from Question 2: What transferable tax credits exist in Kansas, and Are they a Cost-Effective Means of Generating Money To Fund Certain Types of Projects or Causes? This question starts on page 42, if you follow along in the report.

Of the 47 currently available credits, Kansas has 4 that are transferable. This means a taxpayer can sell his or her tax credit to someone else to use.

We found that the transfer feature for three of the four credits is cost-effective for the State, while that feature is not cost effective when it comes to the Historic Preservation Credit. When those credits are transferred, only about 85 cents of the money the State gives up actually reaches the project. If you flip to page 48, the graphic shows the process for this credit. It starts with a historical rehabilitation project plan that must be approved by the State Historical Society.

Once the agency approves the plan, the developer can use the anticipated tax credit as collateral to secure financing from the bank. In our graphic, the hypothetical project costs $1 million with a potential tax credit of $250,000. The bank typically purchases the anticipated credit at a discounted amount, let's say $215,000. The project developer uses the $215,000 in addition to other financing to complete the project. If all goes as planned, the State issues the $250,000 credit when the project is complete. However, only $215,000 of the State's tax credit reaches the project.

On page 49, we show that between 2001 and 2009, the State has issued $58.1 million in tax credits for 570 completed projects thus far. Of this amount, $51 million has been transferred, generating $43.4 million, which translates to about 85 cents on the dollar.

Aside from this primary analysis, we also reviewed additional data because of the concerns related to the rising cost of this credit. If you flip to page 50, the left part of ***Figure 2-7*** shows that the amount of approved project costs approached $312 million so far. At 25%, the amount of tax credits those projects will generate is about $78 million. In the next column, we show that so far, $58 million of tax credits have been issued. In the far right column, you see that only about $44.2 million of these tax credits have actually been claimed through tax returns so far.

As a result, the State will be on the hook to issue tax credits on historic preservation projects that *have already been approved*, and taxpayers will be able to claim tax credits that ***haven't*** been claimed thus far.

The second point to take away from that figure is that the Historic Preservation credit has quickly surpassed the annual cost of $1 million that was estimated for fiscal note purposes. As the last column shows, this credit reached $8.5 million in 2007, and preliminary cost data show its cost at $10.5 million for 2008.

As in question 1, we found some data reliability issues for the Historic Preservation and Angel tax credits, which are described in more detail on page 51. In essence, staff responsible for entering these tax credits hadn't recorded all of the credits in the agency's databases, even though they had been claimed on tax returns.

With that I conclude my presentation and stand for any questions.

My next presentation covers part II, dealing with sales tax exemptions. The question starts on page 15: **Does Kansas Have Sales Tax Exemptions that Potentially Should Be Considered for Elimination?**

In 1985, Kansas had 30 sales tax exemptions, which steadily increased to reach the currently 99 existing exemptions. The State's forgone revenues from the exemptions are estimated to cost $4.2 billion in fiscal year 2009. Besides enacting new exemptions, the Legislature frequently broadens existing ones, which is graphically shown on page 16 of the report.

To evaluate the large number of exemptions, we first grouped them into the three main categories I touched on earlier (must exempt, need to exempt, and decide to exempt as matter of public policy).

Starting on page 18, we show a comprehensive table of all 99 sales tax exemptions. This table is organized into various categories I want to cover briefly: The first six exemptions are those that are ***legally required***, and therefore fall into the "must exempt" group. For example you see #3 there which is designed to exempt groceries purchased through the federal food stamp program. Exemptions in this group cost an estimated $32 million.

The second group includes ***conceptual*** exemptions which are those that avoid double taxation and ensure that sales taxes are collected at the point of final sales. These exemptions are needed according to tax policy considerations. It's also important to recognize that the six exemptions in this group, especially #8, account for the majority of the estimated TOTAL lost revenues, at about $3 billion.

The next group of exemptions are those granted to governmental entities, which is in line with tax policy considerations. The 15 exemptions in this group are estimated to cost about $460 million.

The rest of the figure lists the remaining sales tax exemptions that have been created **as a matter of public policy**: Starting at the bottom of page 19, we show two agricultural exemptions that are estimated to cost about $50 million. Page 20 shows 11 business-related exemptions at about $215 million in total. The next two groups are those targeted to charitable, religious or benevolent exemptions.

On page 23, you see several exemptions for consumers, costing the State an estimated $351 million. At the bottom of the page you'll see a couple of exemptions that are related to education, which cost about $60 million.

On page 24, we list 4 exemptions related to services, while the last group of exemptions relates to health care, which are estimated to cost about $83 million.

In evaluating the sales tax exemptions that are enacted as a matter of public policy, we noted that a number of them provide unequal treatment for similar types of taxpayers or services. Specifically, Kansas currently exempts 44 individually named non-profit organizations. We also identified 4 exemptions that, while they don't name a specific entity, are written very narrowly. These exemptions are shown in ***Figure 1-3*** on page 27. Because they don't apply to a <u>broad group or class of taxpayers</u>, and could create unfair advantages to similar non-profit entities that aren't exempted, they go against good tax policy principles.

Similarly, the exemption for coin-operated laundries appears to create an unfair advantage to those businesses, compared to other businesses involved with laundries, or other coin-operated businesses such as car-washes.

Next, we identified a number of exemptions that are granted to certain "non-profit" entities, but not their "for-profit" counterparts. The five exemptions in this area are listed in the middle on page 26. For example, the first one is medical supplies and equipment purchased for certain non-profit nursing homes, while for-profit nursing homes have to pay sales tax on the same items.

Last, we found that Kansas currently exempts a number of IRS recognized non-profit organizations, but there are still thousands that ***<u>don't</u>*** have sales tax exemptions. This inconsistency puts non-profits on an unequal footing, mainly as a result of Kansas exemptions having been created in a piece-meal fashion over time, and because the Legislature doesn't have a clear public policy goal that helps guide what services or entities should be exempted from paying sales taxes.

Another way of looking at these exemptions is by how much they cost. In fiscal year 2009, the 13 largest sales tax exemptions accounted for $4.1 billion, or 96% of forgone revenues. ***Figure 1-4*** on page 29 summarizes these exemptions. The *<u>top</u>* portion of the figure includes six exemptions that are considered necessary given various tax policy considerations, and cost an estimated $3.4 billion.

The seven exemptions listed in the *bottom* portion include those that were enacted as a matter of public policy. As you can see, this portion includes three exemptions related to machinery and equipment, one exemption geared toward educational and youth activities, one exemption on specific labor services related to construction, an exemption on utilities used in residences or by farms, and a health care exemption related to prescription drugs. Altogether, these seven exemptions cost nearly $700 million.

As with tax credits, we attempted to provide additional information that may aid the Legislature in considering whether these exemptions should continue to be maintained, given that they were created decades ago, and weren't as costly then.

Those discussions can be found on page 30. For example, the prescription drug exemption at the bottom of the page significantly erodes the state and local tax base, but makes the tax system more regressive. Additionally, all four neighboring states allow a similar sales tax exemption. Another exemption in this table I want to touch on is the one on labor services. This is a costly exemption at $182 million, but taxing these services could have a dampening effect on the construction industry.

This actually brings me to my last point which deals with professional, personal care, or other services. These include such things such as accounting or tax services, haircuts or manicures. Similar to other 42 other states, Kansas doesn't tax those services. However, because they aren't specifically exempted, they were outside our scope of the audit.

With that, I conclude my presentation and stand for any questions you may have.