

SESSION OF 2012

**SUPPLEMENTAL NOTE ON HOUSE SUBSTITUTE FOR
SENATE BILL NO. 177**

As Recommended by House Committee on
Taxation

Brief*

House Sub. for SB 177 would implement a number of major changes in income taxes; expand the Rural Opportunity Zone (ROZ) program; repeal a severance tax exemption; and make various amendments to provisions relating to the disposition of sales and use tax revenues.

Income Tax Provisions

Rate Rollbacks

One major part of the bill would provide for formulaic individual income tax rate reductions beginning in tax year 2013 based on the extent to which a certain specified group of State General Fund (SGF) tax sources have increased over the previous fiscal year.

The Director of Legislative Research would be required to certify at the conclusion of each fiscal year beginning with FY 2012 the amount by which a specific set of SGF tax receipts – generally most major income, privilege, and excise taxes – has grown over the prior year. The Secretary of Revenue would then be required to compute that percentage growth above 2 percent and reduce the middle individual income tax bracket for the upcoming tax year (beginning with tax year 2013) by that percentage, reduce the upper bracket

*Supplemental notes are prepared by the Legislative Research Department and do not express legislative intent. The supplemental note and fiscal note for this bill may be accessed on the Internet at <http://www.kslegislature.org>

by that percentage minus 0.5 percent, and reduce the bottom bracket by that percentage plus 0.5 percent. Language in the bill would provide that when the bottom bracket is computed to fall below a rate of 0.4 percent, it would be repealed altogether. This provision subsequently would apply to the remaining two brackets. After the individual income tax is completely repealed, the formulaic rate rollback provisions would be applied to the corporation income tax surtax. When the corporation surtax is repealed, adjustments would begin to the corporation base rate and to financial institution privilege tax rates.

For a fiscal year when the selected set of tax sources has not grown by 2 percent or more, no rate reductions would be triggered for the upcoming tax year.

The Secretary of Revenue would be required to report all income tax rate reductions triggered under the formula to the Governor, the Chairperson of the Senate Assessment and Taxation Committee, and the Chairperson of the House Taxation Committee, and to publish such reductions in the *Kansas Register* prior to September 15.

Business Income Exemption

The bill would totally exempt certain non-wage business income that under current law is subject to individual income tax (income reported by LLC's, Subchapter S corporations, and sole proprietorships on lines 12, 17, and 18 of federal form 1040). The exemption would be applicable to the first \$100,000 of qualifying non-wage business income for tax years 2013-2015; the first \$250,000 for tax years 2016-2017; and all qualifying non-wage business income beginning in tax year 2018.

ROZ Expansion

The bill would add an additional 23 counties (Allen, Anderson, Bourbon, Brown, Chase, Cherokee, Clay, Coffey,

Doniphan, Ellsworth, Grant, Haskell, Labette, Linn, Marshall, Meade, Morris, Nemaha, Neosho, Osage, Ottawa, Rice, and Wabaunsee) to the ROZ program (bringing the total number of eligible counties to 73), which effectively provides an income tax exemption for certain out-of-state taxpayers who relocate to those counties. (The program also authorizes counties to participate in a state-matching program to repay student loans of up to \$15,000 for certain students who establish domicile in ROZ counties.)

Tax Credits, Other Provisions

The bill also would reduce the state earned income tax credit (EITC) beginning in tax year 2014 to 9 percent of the federal EITC. The Kansas EITC is currently set at 18 percent and is scheduled to be reduced to 17 percent in tax year 2013.

An additional provision would take a number of currently refundable income tax credits (EITC, food sales tax rebates, community service, farm net-operating-loss carryback, employer child day care assistance, declared disaster capital investment, disabled access, historic site contribution, individual development account, regional foundation contribution, small employer health care, telecommunications and railroad machinery and equipment) and make them non-refundable beginning in tax year 2013.

Also in tax year 2014, the standard deduction for heads of household would be increased from \$4,500 to \$9,000.

Severance Tax Provisions

The two-year new pool severance tax exemption would be repealed relative to oil production in excess of 250 barrels per day or more occurring on and after July 1, 2012.

Sales and Use Tax Provisions

Disposition of revenue statutes would be adjusted to effectively freeze the amount of sales and use taxes deposited in the State Highway Fund (SHF) during FY 2014 and FY 2015 at the FY 2013 level. Based on current estimates, this would divert an additional \$351.117 million more during those two years into the SGF. Beginning in FY 2016 and continuing through FY 2022, the SHF would be reimbursed the \$351.117 million in equal installments by diverting away from the SGF an additional \$50.160 million more than the amount anticipated under current law and revenue estimates.

Background

The original SB 177 dealt with the statute of limitations relative to claiming sales tax exemption claims. (Those provisions ultimately were enacted in 2011 through another bill.) The House Taxation Committee on February 20 removed the bill's original subject matter; inserted all of the tax reform provisions hereinbefore described; and recommended that a substitute bill be created. The substitute bill contains a number of policy issues also found in HB 2747. Chairman Richard Carlson had appeared as the lead proponent for HB 2747.

Based on a number of different models developed by the Kansas Department of Revenue, the bill would be expected to have the following impact on SGF receipts and individual income tax rates over the upcoming years:

SGF RECEIPTS (\$ IN MILLIONS)

	<u>Total</u>	<u>Income</u>	<u>Sales/Use</u>	<u>Severance</u>
FY 2013	\$ -40.7	\$ -40.7	\$ 0.0	\$ 0.0
FY 2014	-12.0	-171.6	159.6	0.0
FY 2015	-63.6	-256.6	191.5	1.5
FY 2016	-343.8	-296.6	-50.2	3.0
FY 2017	-392.4	-348.2	-50.2	6.0
5-yr total	<u>\$ -852.5</u>	<u>\$ -1113.7</u>	<u>\$ 250.7</u>	<u>\$ 10.5</u>

INDIVIDUAL INCOME TAX RATES

<u>Joint</u>	<u>Current Law</u>	<u>TY 2013</u>	<u>TY 2014</u>	<u>TY 2015</u>	<u>TY 2016</u>	<u>TY 2017</u>
\$0-30k	3.50%	3.34%	3.24%	3.24%	3.21%	3.21%
\$30k-60k	6.25%	5.99%	5.85%	5.85%	5.83%	5.83%
\$60k+	6.45%	6.21%	6.10%	6.10%	6.10%	6.10%