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**Testimony on HB 2010**

**Bernie Koch, Kansas Economic Progress Council**  
**February 6, 2013**  
**House Taxation Committee**

Mr. Chairman and members of the committee, thank you for the opportunity to testify. I'm Bernie Koch with the Kansas Economic Progress Council, a statewide not for profit organization of businesses, trade associations, chambers of commerce, and individuals.

Lowering taxes can be an important part of state policies to encourage economic development.

Public policy which supports **economic freedom** through open economies supports higher growth rates. We would include tax structure and business regulation in that definition.

Other factors have been shown by respected empirical studies to be as important, including investment in infrastructure and equipment; human capital and labor efficiency; continuing technological innovation; and reliable legal systems.

The current emphasis on the individual income tax is diverting our attention from other problems within our tax structure that should be addressed.

***Council On State Taxation report***

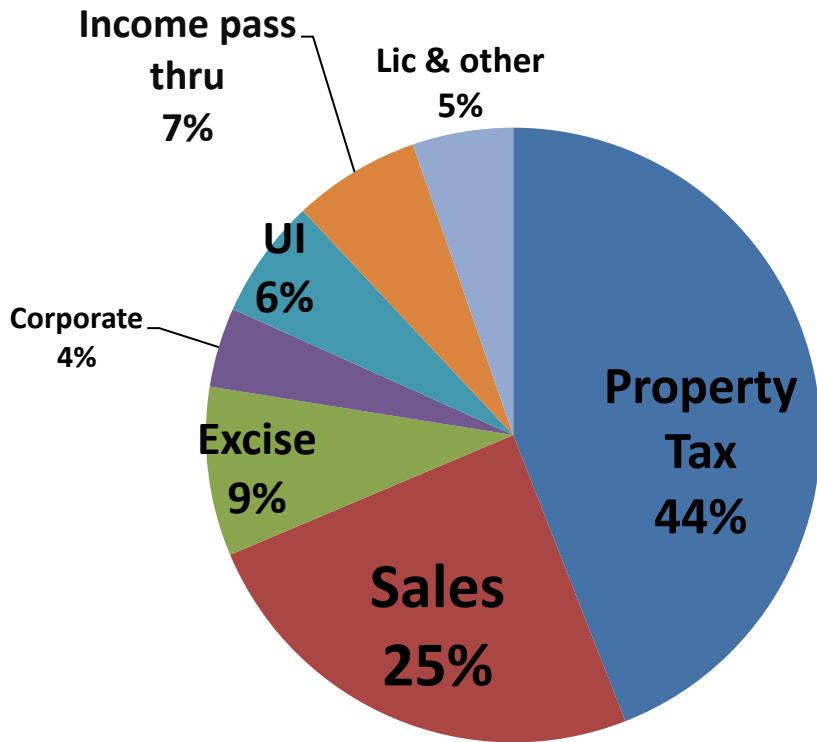
Kansas businesses pay more in property tax than any other tax. Sales tax is the second largest tax paid by business in our state.

The Council On State Taxation reports each on the state and local taxes paid by businesses in every state. Their latest report, released in July, shows tax collections from July 2010 through June of 2011.

44.1 percent of all Kansas local and state business taxes were property taxes. 24.6 percent were sales taxes. Property and sales taxes add up to over 68% of all local and state business taxes paid in Kansas. Only 6.7 percent were individual income taxes on pass-through income, which go away this year under current law. So, even if you totally eliminate individual income taxes, the other 93 percent of state and local taxes on Kansas business still exist.

## Kansas taxes paid by business (State and Local)

### Council on State Taxation FY2011



#### ***Tax Foundation – Location Matters Report***

The Tax Foundation, a nonpartisan tax research group, is often quoted by proponents of eliminating the individual income tax. Their latest study ranks Kansas pretty bad for competitiveness. We are 47<sup>th</sup> for mature operations and 48<sup>th</sup> for newly established operations.

However, if you go to the specific portion of that report concerning Kansas, the study says property and sales taxes give us those low rankings. I have also included that information as an attachment to my testimony. Here's what the Tax Foundation says about manufacturing and Research and Development operations in Kansas:

**“Once again, these operations have one of the highest property tax burdens in the nation along with a top-10 sales tax burden.”**

Our poor tax ranking for mature Research and Development companies should be a major red flag for our efforts to establish the bioscience sector as a pillar of the Kansas economy.

### ***Arkansas Chamber Tax Study***

Another study independent of the Tax Foundation also points to a high effective Kansas tax rate on Research and Development firms. The Arkansas Chamber of Commerce commissioned an Ernst & Young report on seven different types of businesses and their tax liabilities in eight states in the region, including Kansas. The study was released in November of 2011 and reflects taxes at that time.

Kansas had the 2<sup>nd</sup> highest effective tax rate on Research and Development firms in the region with a 12 percent rate. Another red flag in this study was in the category of Business Support Services. The effective tax rate on these types of businesses was 19.7 percent. That's the highest of any state in any category of business.

Different kinds of businesses have different tax burdens. Eliminating the individual income tax may be good for some, but not necessarily for others. We already have a tax structure that puts a different burden on different types of companies.

For example, if you look at the Arkansas study matrix, Kansas has a 4.6 percent effective tax rate on headquarters companies, but a 19.7 percent effective tax rate on business support services. That's a tremendous difference in tax burden.

### ***Arkansas Chamber of Commerce Tax Study***

**Table 6**  
**State and Local Effective Tax Rates Net of Statutory Credits, by Industry and State**

State	Headquarters		Research & Development		Durable Goods Manufacturing		Business Support Services		Food Product Manufacturing		Renewable Energy Equipment Manufacturing		Motor Vehicle Parts Manufacturing	
	ETR	Rank	ETR	Rank	ETR	ETR	ETR	Rank	ETR	Rank	ETR	Rank	ETR	Rank
Arkansas	4.7%	2	9.9%	5	9.2%	4	18.2%	4	8.2%	3	12.5%	4	10.6%	4
Kansas	4.6%	3	12.0%	2	8.1%	6	19.7%	1	7.9%	4	8.0%	7	7.2%	7
Louisiana	6.2%	1	12.7%	1	6.9%	7	14.3%	7	8.9%	2	13.5%	2	12.4%	2
Mississippi	1.5%	7	9.5%	6	10.3%	1	15.0%	6	9.2%	1	14.4%	1	12.0%	3
Missouri	4.1%	6	7.7%	8	5.0%	8	15.0%	5	6.5%	8	6.7%	8	5.9%	8
Oklahoma	4.4%	5	11.4%	3	9.2%	2	18.0%	2	7.2%	6	10.8%	5	8.7%	6
Tennessee	4.6%	4	11.1%	4	9.2%	3	16.8%	3	7.3%	5	9.9%	6	9.2%	5
Texas	0.4%	8	8.4%	7	8.7%	5	13.7%	8	6.5%	7	12.6%	3	13.6%	1
Other States' Avg.	3.7%		10.4%		8.2%		16.1%		7.7%		10.8%		9.9%	

### ***Minnesota Taxpayers Association/ Lincoln Land Institute Property Tax Study 2010***

Rural property taxes on business are another area that needs discussion. A study by the Lincoln Land Institute for the Minnesota Taxpayers Association looked at rural commercial property taxes in all 50 states. It suggests Kansas rural commercial property tax effective rates are probably the highest in the United States.

**Texas Taxpayers and Research Association**

Finally, since we talk so much about becoming like Texas, without an individual income tax, I would like you to see some information from the Texas Taxpayers and Research Association that was given to their legislators this past September. It's about the Mix of Texas Business Taxes and Texas Employment.

It may give us a preview of what to expect if we continue to pursue this course.

**Texas Taxes are not evenly distributed across the economy.**

**Capital-intensive industries (finance, utilities, information, transportation, manufacturing, and mining) account for roughly 68 percent of all business taxes paid, yet account for only 28 percent of the state's private sector employment.**

**Labor-intensive industries (services, wholesale trade, retail trade, construction) account for roughly 32 percent of all business taxes, yet account for 72 percent of the state's private sector employment.**

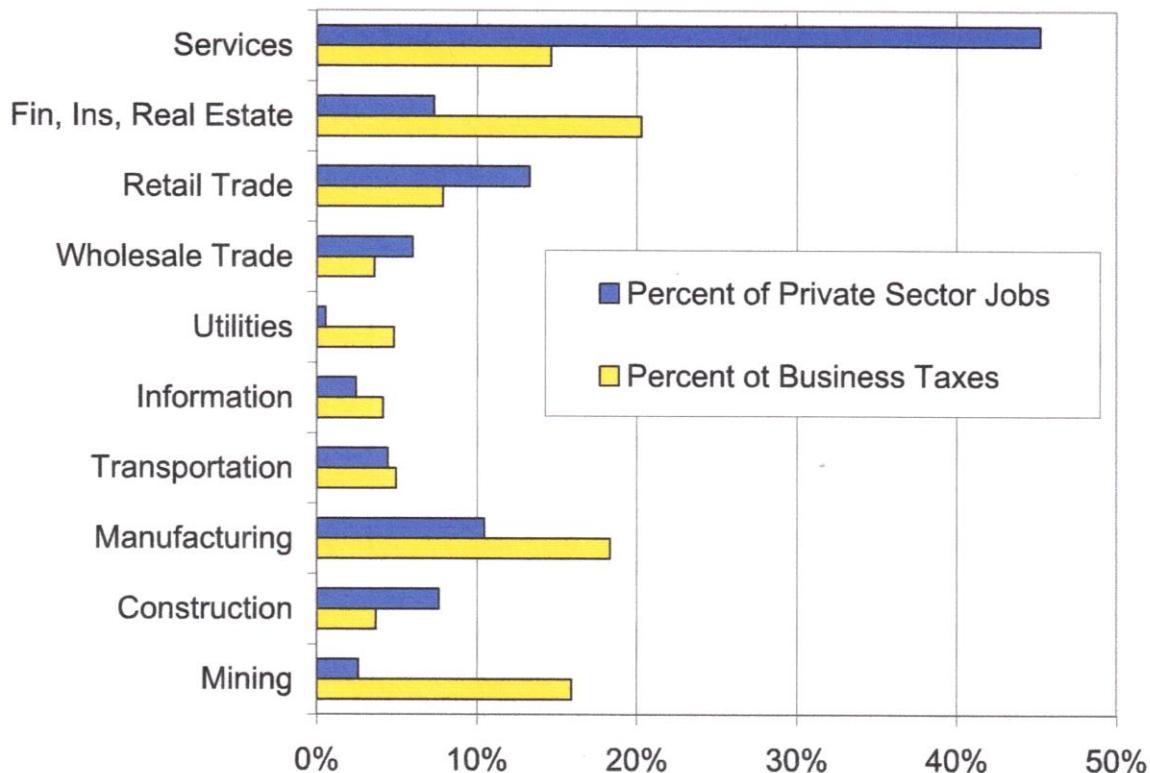
**Over the previous 10 years, the services industry has accounted for two-thirds of the state's job growth.**

If we continue to pursue this course, the tax burden in Kansas could shift to those capital-intensive industries, and a lighter tax burden will fall on labor-intensive industries, particularly services, which aren't always the highest paying jobs.

I think there are two questions that need to be answered: will the tax burden shift among Kansas businesses, and is that what we want?

Thank you for your attention. Thank you for your service to our state and your willingness to deal with the difficult challenges we face.

## The Mix of Texas Business Taxes and Texas Employment



Note: Data is from 2008.

Source: Texas Taxpayers and Research Association and the US Bureau of Labor Statistics.

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## ***Evaluating the Good and the Not-so-good about Texas Taxes on Business***

*Texas has a great deal to offer in attracting new business investment to the state, but our tax system is not necessarily a beneficial part of that evaluation.*

*Because of our heavy reliance on property and sales taxes, Texas' tax system falls heavily on the business community and in particular on capital intensive enterprises—oil and gas extraction, manufacturing, utilities, and real estate—in particular.*

*Our tax system falls relatively lightly on labor intensive enterprises such as services. These enterprises tend to use less capital to produce output.*

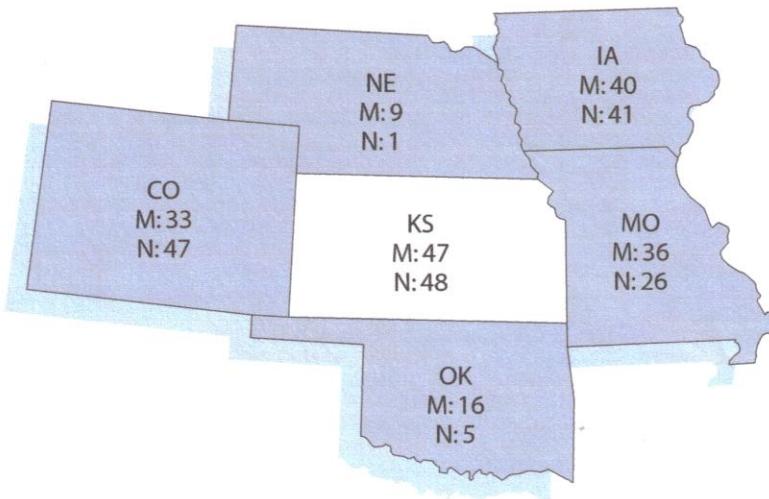
*Texas' lack of a state personal income tax is not solely of benefit to individuals; it also provides certain benefits to the business community, as well. It encourages small business development by allowing retention of capital which can be reinvested into the business. It also, in conjunction with certain favorable aspects of the franchise tax, makes Texas an attractive location for business headquarters. In 2012, 52 Fortune 500 companies were headquartered in Texas—up from 36 in 1998.*

***However, in the absence of a personal income tax, high property and sales taxes mean that Texas is not necessarily an attractive location for manufacturing plants and other capital intensive business operations.***

*Consequently, tax incentives can be an effective tool for mitigating the impacts of our high base level of business taxes. Texas local governments are able to offer new investment projects a temporary property tax abatement or limitation. Cities and counties are able to offer ten year abatement agreements; school districts may offer 8 year limitations on taxable value with a partial credit for the first two years of a project.*

## Kansas

M = Rank for mature firms  
N = Rank for new firms



Kansas ranks 47th overall for mature operations and 48th overall for newly established operations. Specifically:

- In Kansas, all 14 firm types have total tax costs above the national average.
- Kansas ranks 30th for the mature corporate office, which has a total effective tax rate (TETR) of 16.2 percent, just 3 percent larger than the national average. This firm has a fairly low income tax burden due to the state's apportionment formula; however, it faces an above-average sales tax burden and one of the highest property tax burdens in the nation.
- The state ranks 50th for the new distribution center, which has a TETR of 65.4 percent, more than 80 percent above the national average. While this operation has one of the lowest income tax burdens of its type nationally, it

faces the highest property tax burden and fourth-highest sales tax burden.

- For mature operations, Kansas ranks 47th for both labor- and capital-intensive manufacturing and ranks 46th for the mature R&D center. Once again, these operations have one of the highest property tax burdens in the nation along with a top-10 sales tax burden. Although the firm's 7.0 percent corporate income tax rate is not unusually high, its throwback rule gives these operations an above-average income tax burden.
- Kansas offers among the most generous property tax abatements and investment tax credits across most firm types, yet these incentives seem to have little impact on the state's rankings for new operations.