

March 9, 2020

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

Dear Representative Johnson:

SUBJECT: Fiscal Note for HB 2616 by Representative Croft

In accordance with KSA 75-3715a, the following fiscal note concerning HB 2616 is respectfully submitted to your committee.

HB 2616 would reduce the state retail sales tax and compensating use tax rate for food and food ingredients based on a formula. Food and food ingredients are defined as substances, whether in liquid, concentrated, solid, frozen, dried, or dehydrated form, that are sold for ingestion or chewing by humans and are consumed for their taste or nutritional value. Food and food ingredients would not include alcoholic beverages, dietary supplements, tobacco or certain prepared foods. Food and food ingredients would specifically include bottled water, candy, food sold through vending machines, and soft drinks. The bill provides specific definitions for bottled water, candy, food sold through vending machines, prepared food, soft drinks, and dietary supplements. The bill does not adjust the distribution of state retail sales tax and compensating use tax revenue, which would remain the same as current law: 83.846 percent to the State General Fund and 16.154 percent to the State Highway Fund.

The formula to adjust the state retail sales tax and compensating use tax rate for food and food ingredients is based on the amount of compensating use tax receipts collected each fiscal year above 3.0 percent from the base year of FY 2018. That amount would be certified by the Director of Legislative Research and the Secretary of Revenue would be required to calculate the rate reduction based on the certified amount reduced to the nearest 0.1 percent. The first rate reduction would occur on July 1, 2020, and subsequent rate reductions would occur on January 1st in future years after the new rate is published by October 1st of the previous year. Once the state sales tax is eliminated on food and food ingredients, local governments would no longer be able to charge a local sales tax on food and food ingredients.

Estimated State Fiscal Effect				
	FY 2020 SGF	FY 2020 All Funds	FY 2021 SGF	FY 2021 All Funds
Revenue	--	--	(\$11,900,000)	(\$14,200,000)
Expenditure	--	--	\$764,543	\$764,543
FTE Pos.	--	--	--	6.00

The Department of Revenue estimates that HB 2616 would decrease state revenues by \$14.2 million in FY 2021. Of that total, the State General Fund is estimated to decrease by \$11.9 million in FY 2021, while the State Highway Fund is estimated to decrease by \$2.3 million in FY 2021. The fiscal effect to state revenues during subsequent years would be as follows:

	<u>FY 2022</u>	<u>FY 2023</u>	<u>FY 2024</u>	<u>FY 2025</u>
State General Fund	(\$35,600,000)	(\$51,100,000)	(\$66,000,000)	(\$84,200,000)
State Highway Fund	<u>(6,900,000)</u>	<u>(9,800,000)</u>	<u>(12,800,000)</u>	<u>(16,200,000)</u>
	(\$42,500,000)	(\$60,900,000)	(\$78,800,000)	(\$100,400,000)

This bill would not have a fiscal effect on local sales tax revenues until after state sales tax is eliminated, when local governments would no longer be able to charge a local sales tax on food and food ingredients; however, the specific estimate of lower local sales tax revenues was not calculated by the Department of Revenue. The Streamlined Sales Tax Agreement requires once a taxable item is fully exempt from state sales taxes, it would also be exempt from local sales taxes.

To formulate the estimates of the sales tax exemption for food and food ingredients, the Department assumes that 15.0 percent of all current sales tax collections are collected on food and food ingredients. The Department indicates that State General Fund estimates for FY 2021 are based on the November 2019 Consensus Revenue Estimate. Retailers would be required to collect sales or compensating use tax at two different rates depending on the products sold. The bill would also require food retailers to file two returns each month, one for food sales only subject to the local tax (similar to the current utility return) and the current return for items subject to the state and local sales tax. The Department indicates these additional requirements may be burdensome to some retailers.

The Department of Revenue indicates that it would require a total \$764,543 from the State General Fund in FY 2021 to implement the bill and to modify the sales tax system. The bill would require the Department to hire 6.00 new FTE positions to review, process, and audit sales tax returns. The Department estimates that ongoing expenses for salary and wages for the 6.00 FTE positions and overhead expenses would total \$472,461 from the State General Fund in FY 2022. The current composite jurisdiction sales tax system does not accommodate a second state sales tax rate. The required programming for this bill by itself would be performed by existing staff of the Department of Revenue and outside contract programmer services. 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. Due to the required programming necessary to implement the bill, the Department may not be able to implement the food sales tax rate reduction on July 1, 2020.

The Kansas Department of Transportation indicates that the bill would reduce state revenues to the State Highway Fund as noted above. The Kansas Department of Transportation indicates that when the state receives lower State Highway Fund dollars it may be required to make corresponding reductions to planned expenditures for projects funded under the comprehensive transportation plan. The League of Kansas Municipalities and Kansas Association of Counties indicate the bill would have no fiscal effect on local governments until the state eliminates the sales tax on food and food ingredients. Once that occurs, the bill would provide a significant net reduction to local sales tax collections that are used in part to finance local governments. Any fiscal effect associated with HB 2616 is not reflected in *The FY 2021 Governor's Budget Report*.

Sincerely,

A handwritten signature in black ink, appearing to read "L. L. Campbell". The signature is fluid and cursive, with the first name "L." and last name "Campbell" clearly visible.

Larry L. Campbell
Director of the Budget

cc: Trey Cocking, League of Municipalities
Jay Hall, Association of Counties
Lynn Robinson, Department of Revenue
Ben Cleaves, Transportation