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March 11, 2024

The Honorable Caryn Tyson, Chairperson
Senate Committee on Assessment and Taxation
300 SW 10th Avenue, Room 548-S
Topeka, Kansas 66612

Dear Senator Tyson:

SUBJECT: Fiscal Note for SB 539 by Senate Committee on Assessment and Taxation

In accordance with KSA 75-3715a, the following fiscal note concerning SB 539 is respectfully submitted to your committee.

SB 539 would enact the Tax Relief for all Kansans Act. Under current law, the standard deduction for the calculation of Kansas income taxes is set at $3,500 for single individual taxpayers, $8,000 for married filing jointly, and $6,000 for head of household. The bill would set the standard deduction at $4,000 for single individual taxpayers, $8,000 for married filing jointly, and $6,000 for head of household in tax year 2024. The bill would increase the standard deduction for all taxpayers by the cost-of-living adjustment published in the Internal Revenue Code beginning in tax year 2025 and annually thereafter.

Under current law, taxpayers are allowed to claim an exemption of $2,250 for each personal exemption. The bill would set the personal exemption at $22,000 for married filing jointly and $11,000 for all other filing status type in tax year 2024. Each filling status type would be able to claim an additional personal exemption of $3,000 for each dependent. The bill would allow the personal exemption amounts to be increased annually by the cost-of-living adjustment published in the Internal Revenue Code beginning in tax year 2025 and annually thereafter.

Under current law, taxpayers filing as single, head of household, married filing separate, or married filing jointly are allowed to subtract the full amount of Social Security benefits from federal adjusted gross income for Kansas income tax purposes, if the taxpayer has income of $75,000 or less. The bill would exempt Social Security benefits from Kansas income taxes if the taxpayer has income of $100,000 or less. The bill reduces the subtraction modification of Social Security benefits from federal adjusted gross income by a mathematical formula for incomes above the $100,000 threshold and below $125,000 for all taxpayers. This would allow taxpayers with income of $100,000 up to $125,000 to subtract a portion of Social Security benefits from federal adjusted gross income. The changes would go into effect beginning in tax year 2024.

Under current law, individual income tax rates are set at 3.1 percent for income under $15,000 ($30,000 for married filing jointly), 5.25 percent for income between $15,000 and $30,000 (between $30,000 and $60,000 for married filing jointly), and at 5.7 percent for income $30,000 and over ($60,000 and over for married filing jointly). For all taxable income and each filing status type, the bill would set the individual income tax rate at 5.7 percent in tax year 2024, 5.65 percent in tax year 2025, 5.6 percent in tax year 2026, 5.55 percent in tax year 2027, 5.5 percent in tax year 2028, and 5.45 percent in tax year 2029 and all future tax years. The bill would also remove outdated language from previous tax years.

The bill would reduce the privilege normal tax rate for banks from 2.25 percent to 1.94 percent in tax year 2024 and 1.63 percent in tax year 2025. The bill would reduce the privilege normal tax rate for trust companies and savings and loan associations from 2.25 percent to 1.93 percent in tax year 2024 and 1.61 percent in tax year 2025.

The bill would reduce the state retail sales tax and compensating use tax rate for food and food ingredients to 0.0 percent and change the distribution of overall state sales and compensating use tax revenue to 82.0 percent to the State General Fund and 18.0 percent to the State Highway Fund on July 1, 2024. Under current law, the state retail sales tax rates specifically on food and food ingredients and the distribution of overall state sales and compensating use tax revenue are set to be adjusted as follows:

| Date of Rate Change | Tax Rate | Percent to State General Fund | Percent to State Highway Fund |
|---|---|---|---|
| Current law | 2.0 % | 83.0 % | 17.0 % |
| January 1, 2025 | 0.0 | 82.0 | 18.0 |

Under current law, $42,049 of a residential property's appraised valuation is exempt from the state's 20-mill property tax for public schools in tax year 2023, with a statutory increase of the exemption in tax year 2024 based upon the ten-year average percentage change in statewide valuation of all residential real property. The bill would increase the exemption to $80,000 beginning in tax year 2024 and would allow for future exemption increases based on the ten-year average change in residential property values beginning in tax year 2025. The bill would take effect upon publication in the *Kansas Register.*

| Estimated State Fiscal Effect | | | |
|---|---|---|---|
| | FY 2024 | FY 2025 | FY 2026 |
| Expenditures | | | |
| State General Fund | -- | $62,224,778 | $65,600,000 |
| Fee Fund(s) | -- | -- | -- |
| Federal Fund | -- | -- | -- |
| Total Expenditures | -- | $62,224,778 | $65,600,000 |
| Revenues | | | |
| State General Fund | -- | ($377,100,000) | ($327,500,000) |
| State Highway Fund | -- | (13,100,000) | -- |
| School District Finance | -- | (62,100,000) | (65,600,000) |
| Total Revenues | -- | ($452,300,000) | ($393,100,000) |
| FTE Positions | -- | -- | -- |

The Department of Revenue estimates that SB 539 would decrease state revenues by $452.3 million in FY 2025, including reducing State General Fund (SGF) revenues by an estimated $377.1 million, reducing State Highway Fund (SHF) revenues by an estimated $13.1 million, and reducing State School District Finance Fund revenues by an estimated $62.1 million. The estimated fiscal effect by specific tax policy change would be as follows:

| Tax Changes (SGF) | FY 2025 | FY 2026 | FY 2027 |
|---|---|---|---|
| Standard Deduction, Exemption, Rate | ($244,900,000) | ($271,000,000) | ($349,600,000) |
| Social Security Exemption | (61,900,000) | (49,300,000) | (50,800,000) |
| Privilege Tax Rate Reduction | (6,800,000) | (7,200,000) | (7,400,000) |
| State Food Sales Tax Changes | (63,500,000) | -- | -- |
| Total SGF | ($377,100,000) | ($327,500,000) | ($407,800,000) |
| | | | |
| Tax Changes (SHF) | | | |
| State Food Sales Tax Changes | ($13,100,000) | $ -- | $ -- |
| | | | |
| Tax Changes (Property Taxes) | | | |
| 20-mill School Levy Exemption | ($62,100,000) | ($65,600,000) | ($69,200,000) |
| | | | |
| Total (SGF+SHF+Property Taxes) | ($452,300,000) | ($393,100,000) | ($477,000,000) |

To formulate the estimates of the increased standard deduction amounts, increased personal exemption amounts, and flat individual income tax rates, the Department simulated this tax policy change based on actual tax return data from tax year 2021. The Department estimates that the number of tax returns would grow by approximately 1.0 percent each year and the standard deduction and personal exemption amount are assumed to increase by 2.5 percent each year for the cost-of-living adjustment.

To formulate the estimates of the exemption of Social Security benefits from individual income, the Department reviewed data on Social Security benefits from tax year 2020. The Department adjusted the amount of Social Security benefits to account for cost-of-living adjustments that have occurred since tax year 2020. The Department created a simulated tax table for all taxpayers that receive Social Security benefits and considered the $75,000 Social Security benefits exemption that is currently allowed for each tax filing type.

To formulate the estimates of the privilege normal tax rate reduction for banks, trust companies, and savings and loan associations, the Department reviewed financial institutions privilege tax data from tax year 2021.

To formulate the estimates of the sales tax exemption for food and food ingredients, the Department assumes that expenditures on food and food ingredients will be comparable to expenditures observed during calendar year 2023, the first year of the rate reduction. The fiscal note considers the three-year phase-out of state retail sales tax and compensating use tax rate for food and food ingredients that was enacted in 2022 HB 2106.

The Division of the Budget notes that increased revenue reductions for FY 2028 and FY 2029 would likely occur due to the further reductions in the income tax rate and/or the indexing of other components. The Division of the Budget also notes that the estimated reduction in revenues from the 20-mill school levy would require an offsetting appropriation for State Foundation Aid from the State General Fund to keep the Base Aid for Student Excellence (BASE) in the school finance formula at $5,381 for FY 2025, as included in *The FY 2025 Governor's Budget Report*. If this provision of the bill would be enacted without a corresponding increase to the State General Fund appropriation for State Foundation Aid, the Department of Education would have to prorate the BASE by reducing state aid to school districts in FY 2025.

The Department of Revenue indicates that the bill would require $124,778 from the State General Fund in FY 2025 to implement the bill and to modify the automated tax system. 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 Kansas Department of Transportation (KDOT) indicates that the bill would reduce state revenues to the State Highway Fund as noted above. KDOT 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 bill would have no fiscal effect on the operations of the Office of the State Bank Commissioner; however, it has the potential to adjust certain assessment rates. The agency's budget is funded from assessments paid through its licensees and chartered institutions. Its assessments are based on the budgetary needs of the applicable division. For state banks and trust companies, the agency assesses a percentage of each entity's total assets necessary in order to regulate these institutions. The percentage of total assets assessed changes each fiscal year in order to ensure the agency's budgetary needs are met. It is expected that all state banks and trust companies will have an increase in total assets due to lower privilege taxes. If each bank and trust company have an increase in total assets, the agency will lower its percentage of total asset assessment of each state bank and trust company to cover the agency expenses.

The fiscal effects associated with increasing the standard deduction amounts, increasing the income limitation allowing additional Social Security benefits to be exempt from Kansas income taxes, state food sales tax changes, and the 20-mill school levy exemption increase are partially reflected in *The FY 2025 Governor's Budget Report,* which included higher increases to each standard deduction amount, allowed all Social Security benefits to be exempt from Kansas income taxes, moved up the 0.0 state sales tax rate on food and food ingredients to April 1, 2024, and increased the 20-mill school levy exemption to $100,000, but would have eliminated future exemption increases based on the ten-year average change in residential property values. The privilege tax rate reduction is reflected in *The FY 2025 Governor's Budget Report*. No other provisions of SB 539 are reflected in *The FY 2025 Governor's Budget Report*.

The Kansas Association of Counties and the League of Kansas Municipalities indicate the bill would have no fiscal effect on local governments. This bill has the potential to reduce revenues that are pledged to repay STAR bond projects; however, it is unknown what impact the bill would have on the viability of those projects. By lowering the amount of property taxes collected from the statewide mill rate to fund public education, the bill has the potential to reduce revenues that are pledged to repay tax increment financing projects such as redevelopment districts or bioscience development districts if they include any residential housing; however, it is unknown what impact the bill would have on the viability of those projects.

Sincerely,

Adam C. Proffitt
Director of the Budget

cc: Lynn Robinson, Department of Revenue
Gabrielle Hull, Department of Education
Jay Hall, Kansas Association of Counties
Wendi Stark, League of Kansas Municipalities
Brendan Yorkey, Department of Transportation
Barbara Albright, Office of the State Bank Commissioner