

MEMORANDUM

TO: The Honorable Adam Smith
House Committee on Taxation

FROM: Adam Proffitt, Director of the Budget 

DATE: Wednesday, March 17, 2021

SUBJECT: Testimony for HB 2421 - Opponent

Chairman Smith and members of the committee,

I submit this testimony to you in opposition to HB 2421, which seeks to implement a host of tax cuts, including exempting GILTI from Kansas taxes, provisions for disallowed business interest, and divergence from federal conforming standards to allow itemizing at the state level, even if a filer did not itemize on their federal return.

The fiscal note for HB 2421 shows that this will reduce state revenues by a minimum of \$118.8 million in FY 2022, \$125.6 million in FY 2023 and \$130.5 million in FY 2024. The impacts of the PPP deductions are unknown right now; once those credits are actualized, it will increase the price tag associated with this bill. In total, this bill will come at **a cost of at least \$374.9 million over the first three fiscal years.**

As the state's budget director, I am obligated to inform this body of any fiscal policy that will have a negative impact on our state's long term fiscal health, and this bill could do that in its current form. While our economy and revenues have certainly shown improvement in recent months, I do not believe that now is the time to intentionally reduce revenues to this degree. Most state agencies have already sustained budget cuts to their FY 2022 budgets, some by as much as 10%. Reducing state revenues by an additional \$374.9 million in the coming years would lead to further cuts, limiting the agencies' abilities to fund critical services. The state uses these revenues to fund programs and services that benefit citizens of Kansas all across the state. Programs like public safety, mental health, public education, investment in infrastructure, investment in growing tourism, expanding commerce, and others would all be at risk of losing funding.

The fiscal impact associated with the provision that allows taxpayers to itemize on their state

return, regardless of how they filed their federal return is estimated to be \$65.0 million in FY 2022. However, a report conducted by Dr. Donna Ginther with the KU Institute for Policy & Social Research¹ shows that this provision of the bill will benefit only 6.6% of taxpayers in Kansas, and those taxpayers are among the top 18% income earners in the state. That same study shows that the net effect on revenues of the reduction in Kansas itemization as a result of the 2017 federal tax law changes was only \$15 million. For the majority of Kansas taxpayers, there was a net reduction in total taxes paid, even when they no longer itemized on their state returns. Passage of this bill would reduce revenues by \$65 million, when the revenue increase from the 2017 federal legislation was only \$15 million, and it would only lead to a net tax reduction for 6.6% of Kansas taxpayers. Alternatively, there was a proposal in the Senate that would have closed the tax loophole for digital goods and marketplace facilitators and would increase the standard deduction in Kansas. This proposal would have been revenue neutral to the state but would have provided income tax relief to nearly all taxpayers.

Passage of HB2421 would put the state out of compliance with provisions contained within the American Rescue Plan, which restrict states from using direct state aid as a backfill for tax cuts. Specifically, the legislation states “A State or territory shall not use the funds provided under this section or transferred pursuant to section 603(c)(4) **to either directly or indirectly offset a reduction in the net tax revenue of such State** or territory resulting from a change in law, regulation, or administrative interpretation during the covered period that reduces any tax (by providing for a reduction in a rate, a rebate, a deduction, a credit, or otherwise) or delays the imposition of any tax or tax increase” Failure to comply with this provision is likely to lead to the federal government recouping funds in an amount equal to the reduction in net tax revenue as a result of tax law changes.

I appreciate the committee’s attention on this matter, and I respectfully request that you do not move this bill forward favorably.

1 “The Kansas Economy & Current Tax Proposals” by Donna K. Ginther, PhD, January 29, 2021