Report of the Special Committee on Taxation to the 2023 Kansas Legislature

CHAIRPERSON: Representative Adam Smith

VICE-CHAIRPERSON: Senator Caryn Tyson

OTHER MEMBERS: Senators Renee Erickson, Tom Holland, Virgil Peck, and Gene Suellentrop; and Representatives Mike Amyx, Tom Kessler, Les Mason, Vic Miller, and Carl Turner

STUDY TOPIC

The Committee is directed to study and make recommendations concerning:

- The effective implementation of the *Kansas Constitution's* requirement of statewide uniformity in assessment of property for *ad valorem* tax purposes;

- The continued necessity and utility of Kansas' membership in the Streamlined Sales and Use Tax Agreement;

- The individual income taxation of retirement plan income and Social Security benefits; and

- Any inactive taxing jurisdictions or unused tax provisions that may be ripe for repeal.

Special Committee on Taxation

Report

Conclusions and Recommendations

The Committee recommends the 2023 Legislature:

- Eliminate the tax "cliff" and marriage penalty related to the income taxation of Social Security benefits;
- Consider eliminating the income taxation of Social Security benefits, including review of the formulaic elimination of the taxation previously included in the Conference Committee Report for 2022 HB 2597;
- Explore gradually reducing or eliminating the income taxation on retirement plan income, including the approach previously considered in the Conference Committee Report for 2022 HB 2597. The Committee specifically recommended the Legislature consider the equity of taxation of retirement income, specifically certain plans for employees of Kansas Board of Regents institutions that result in no tax being paid on retirement income;
- Discuss the property valuation process throughout the state, including statutory requirements, constitutional assessment ratios, the administrative process used by the Division of Property Valuation, and the practices of county appraisers;
- Clarify statutes to specify the voting procedure or the Kansas delegation to the Streamlined Sales and Use Tax Agreement (SSUTA);
- Continue to evaluate the impact of the SSUTA on Kansans and Kansas businesses;
- Evaluate the $100,000 threshold of taxable sales for use taxes prior to remote sellers being required to collect and remit use taxes to consider the equity of the policy on in-state businesses and consider implementing a similar policy for in-state retailers;
- Consider re-adding the compensating use tax line to the Kansas individual income tax return; and
- Evaluate any expired and unused taxing provisions and consider them for possible repeal.

Proposed Legislation: None.

Background

The Special Committee on Taxation (Committee) was created by the Legislative Coordinating Council to study Kansas income taxation of Social Security benefits and retirement income, Kansas' continued participation in the Streamlined Sales and Use Tax Agreement (SSUTA), the effective implementation of the *Kansas Constitution's* requirements related to

uniformity of valuation for property tax purposes, and any unused or inactive tax provisions in Kansas statutes. The Committee was authorized to meet for two days.

Committee Activities

The Committee met at the Statehouse on November 18 and December 12, 2022. At the November 18 meeting, the Committee reviewed information related to income taxation of Social Security benefits and retirement income, unused and inactive taxing provisions, and property valuation uniformity. At the December 12 meeting, the Committee reviewed information related to the SSUTA and made recommendations to the 2023 Legislature.

November 18, 2022, Meeting

Consensus Revenue Estimates

The Senior Economist, Kansas Legislative Research Department (KLRD), presented the most recent economic and revenue forecasts of the Consensus Revenue Estimating Group, made on November 9, 2022. The presentation noted the Kansas economy is expecting to have modest real growth throughout calendar years 2022, 2023, and 2024, but that elevated levels of inflation will result in robust nominal economic growth, leading to continued growth in tax revenues through the end of FY 2024. Tax receipts are expected to grow by 3.1 percent in FY 2023 and a further 0.9 percent in FY 2024. Non-tax revenues are anticipated to be volatile throughout the forecast period as extraordinary transfers out of the State General Fund are provided for in each year. Accordingly, total receipts are projected to grow by 22.6 percent in FY 2023 and a further 4.4 percent in FY 2024.

Income Taxation of Social Security Benefits and Retirement Income

KLRD staff provided an overview and history of the federal and Kansas income taxation of Social Security benefits and retirement plan income.

A representative of the Tax Foundation provided information about tax policy. The representative noted that for states levying a broad-based income tax, the ideal neutral tax policy is to treat all retirement income, including Social Security benefits, as ordinary income. However, if a state chooses to provide non-neutral taxation of such income, the representative advised that Kansas should modify its tax treatment by ensuring that the current tax "cliff" related to Social Security benefits is converted to a phaseout and by ensuring the tax code contains no marriage penalties or bonuses as it relates to retirement income.

A representative of the Kansas Department of Revenue (Department) provided estimates of the impact on state revenues of various possible changes to tax policy related to Social Security benefits and retirement income. The Department representative noted that the current policy regarding Social Security benefits is estimated to reduce state receipts by approximately $31 million per year. Fully exempting such benefits would reduce state receipts by an additional amount of approximately $117 million per year once fully implemented. The Department representative noted that fully exempting retirement plan income would reduce state receipts by an estimated $267 million per year once fully implemented.

Inactive and Unused Tax Provisions

Department representatives provided detailed information concerning Kansas tax credits and their utilization and expiration, Kansas sales tax exemptions and their utilization, and local sales tax authority in Kansas and its utilization.

Property Valuation Uniformity

KLRD staff provided an overview of the *Kansas Constitution's* requirements concerning the uniformity of valuation and taxation of property under the state's general *ad valorem* property tax.

The Director of Property Valuation from the Department presented information concerning the constitutional and statutory requirements related to property valuation, the current status of the Division of Property Valuation and County Appraisers, the annual appraisal compliance review process, and current legal and technological issues within property valuation.

Staff from the Office of the Revisor of Statutes provided an overview of the Kansas Supreme

Court case, *In the Matter of the Walmart Stores*, which pertained to evidentiary issues related to the valuation of "big box" retail stores and mentioned the issue of the "dark store theory" of property valuation.

The Court's ruling overturned a previous case prohibiting the Board of Tax Appeals from considering unadjusted build-to-suit leases in determining the value of a property and remanded the matters back to the Board of Tax Appeals for further consideration under the evidentiary standard. The Director of Property Valuation indicated that the matter had since been settled between the parties with the property values being stipulated.

December 12, 2022, Meeting

Streamlined Sales and Use Tax Agreement

KLRD staff presented a history of Kansas' legislative actions concerning the SSUTA. The Legislature's work on the topic began in 2000, and the SSTUA was entered into in 2002. Legislation enacted in 2003 generally brought Kansas' tax laws into compliance with the SSUTA's provisions and 2007, and 2010 legislation updated Kansas law to remain in compliance with the SSUTA following amendments thereto.

The Secretary of Revenue presented information to the Committee concerning the administration of the SSUTA by the Department and the revenue received by Kansas pursuant to it. In calendar year 2021, Kansas received $68.4 million of state and local tax pursuant to the SSUTA and allowed SSUTA customer service providers to retain $2.0 million under the terms of the agreement. In FY 2022, Kansas' member dues for the SSUTA were $35,805.

The Executive Director of the SSUTA and representatives from the Council on State Taxation presented information to the Committee concerning the agreement; its history and governance; its goals, results, and key features; the burdens on retailers imposed by sales taxes and how the SSUTA seeks to minimize those burdens; recent U.S. Supreme Court decisions and their impact on the SSUTA; and the organization's successes and current projects.

Conclusions and Recommendations

The Committee held preliminary discussion of possible recommendations at the conclusion of its November 18 meeting, with further discussion and agreement on final recommendations at the conclusion of its December 12 meeting.

The Committee recommends the 2023 Legislature:

- Eliminate the tax "cliff" and marriage penalty related to the income taxation of Social Security benefits;

- Consider eliminating the income taxation of Social Security benefits, including review of the formulaic elimination of the taxation previously included in the Conference Committee Report for 2022 HB 2597;

- Explore gradually reducing or eliminating the income taxation on retirement plan income, including the approach previously considered in the Conference Committee Report for 2022 HB 2597. The Committee specifically recommends the Legislature consider the equity of taxation of retirement income, specifically certain plans for employees of Kansas Board of Regents institutions that result in no tax being paid on retirement income;

- Discuss the property valuation process throughout the state, including statutory requirements, constitutional assessment ratios, the administrative process used by the Division of Property Valuation, and the practices of county appraisers;

- Clarify statutes to specify the voting procedure or the Kansas delegation to the SSUTA;

- Continue to evaluate the impact of the SSUTA on Kansans and Kansas businesses;

- Evaluate the $100,000 threshold of taxable sales for use taxes prior to remote sellers

being required to collect and remit use taxes to consider the equity of the policy on in-state businesses and consider implementing a similar policy for in-state retailers;

- Consider re-adding the compensating use tax line to the Kansas individual income tax return; and

- Evaluate any expired and unused taxing provisions and consider them for possible repeal.