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Shawn Sullivan, Director of the Budget

Sam Brownback, Governor

February 2, 2017

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

Dear Representative Johnson:

SUBJECT: Fiscal Note for HB 2178 by House Committee on Taxation

In accordance with KSA 75-3715a, the following fiscal note concerning HB 2178 is respectfully submitted to your committee.

Under current law, individual income tax rates are set at 2.7 percent for income under $15,000 ($30,000 for married filing jointly) and at 4.6 percent for income $15,000 and over ($30,000 for married filing jointly) in tax year 2017 and the bottom rate is set to be lowered to 2.6 percent beginning in tax year 2018. HB 2178 would freeze the bottom rate for all taxpayers at 2.7 percent and increase the top rate for all taxpayers to 5.25 percent beginning in tax year 2017 and in all future tax years. The bill would eliminate the automatic income tax rate reduction procedure that has the potential to reduce individual income tax rates beginning in tax year 2021. The bill would prohibit any penalties or interest from the underpayment of taxes from the change in tax rate in tax year 2017, as long as the taxes are paid by April 15, 2018. The bill would also allow taxpayers to claim 100.0 percent of the total amount of medical care expenses as an itemized deduction.

Estimated State Fiscal Effect				
	FY 2018 SGF	FY 2018 All Funds	FY 2019 SGF	FY 2019 All Funds
Revenue	$280,100,000	$280,100,000	$225,000,000	$225,000,000
Expenditure	$76,326	$76,326	--	--
FTE Pos.	--	--	--	--

The Department of Revenue estimates that HB 2178 would increase State General Fund revenues by $280.1 million in FY 2018 and by $225.0 million in FY 2019. The fiscal effect to state revenues during subsequent years would be as follows:

	FY 2020	FY 2021	FY 2022
State General Fund	$227,000,000	$230,300,000	$235,400,000

To formulate these estimates, the Department of Revenue reviewed Kansas and Internal Revenue Service (IRS) data from tax year 2014 and tax year 2015. The Department indicates that freezing the bottom rate for all taxpayers at 2.7 percent and increasing the top rate for all taxpayers to 5.25 percent would generate $302.9 million in FY 2018, $247.8 million in FY 2019, $250.5 million in FY 2020, $253.1 million in FY 2021, and $258.2 million in FY 2022. The Department indicates that in tax year 2014, there were 8,606,481 filers in the U.S. that used the federal itemized medical care deduction totaling $83.8 billion in expenses. The Department indicates that the State of Kansas historically accounts for 1.0 percent of IRS information. Based off that assumption, it is estimated that 86,065 Kansas taxpayers would claim approximately $830.0 million from this deduction that would reduce State General Fund revenue by $22.8 million each tax year based on an effective tax rate of 2.75 percent. The specific changes in State General Fund revenues for FY 2018, FY 2019, and FY 2020 are shown in the following table:

	FY 2018	FY 2019	FY 2020
Rate Changes	$302,900,000	$247,800,000	$250,500,000
Medical Deduction	(22,800,000)	(22,800,000)	(22,800,000)
Total SGF Changes	$280,100,000	$225,000,000	$227,700,000

The Department of Revenue indicates that State General Fund estimates for FY 2018 and FY 2019 are based on the November 2016 Consensus Revenue Estimate. State General Fund revenues in the out years assume a 1.0 percent annual growth rate. The bill is retroactive and the fiscal effect is based on adjusted the income tax rates and allowing itemized deduction on medical care expenses beginning on January 1, 2017. The estimate for FY 2018 includes 100.0 percent of tax year 2017 tax liability and 30.0 percent of tax year 2018 tax liability. The estimate for FY 2019 includes 70.0 percent of tax year 2018 tax liability and 30.0 percent of tax year 2019 tax liability.

The Department indicates that the bill would require $76,326 from the State General Fund in FY 2018 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. However, 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 Department of Administration indicates that adjusting state income tax collections has the potential to have a fiscal effect on the amount of revenue collected from its debt setoff program. This program intercepts individual income tax refunds and homestead tax refunds and applies those amounts to debts owed to state agencies, municipalities, district courts, and state agencies in other states. Debts include, but are not limited to child support, taxes, educational expenses, fines, services provided to the debtor, and court ordered restitution. As the dollar amounts of refunds are decreased, the amount available for possible debt setoffs is also reduced. However, the Department is unable to make an estimate of the amount of debts setoffs that will no longer be intercepted as a result of the bill. Any fiscal effect associated with HB 2178 is not reflected in *The FY 2018 Governor's Budget Report*.

Sincerely,

Shawn Sullivan,
Director of the Budget

cc: Jack Smith, Department of Revenue
Colleen Becker, Department of Administration