



February 8, 2022

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Kansas Action for Children
Verbal testimony in opposition to HB 2186
House Taxation Committee

Chairman Smith and members of the Committee:

Thank you for the opportunity to provide testimony in opposition to HB 2186. Kansas Action for Children is a nonprofit advocacy organization working to make Kansas a place where every child has the opportunity to grow up healthy and thrive. We work across the political spectrum to improve the lives of Kansas children through bipartisan advocacy, partnership, and information-sharing on key issues, including early learning and education, health, and economic security for families.

KAC believes the answers to practical questions about taxes – like how high or low should they be, who should pay and how much, and what should be taxed – flow from strong and equitable principles (see Appendix 2). These are broadly recognized as the foundation of a system that works. KAC is opposing HB 2186 because the bill would not ensure:

- **Adequacy:** A single sales factor (SSF) formula usually results in a significant drop in state revenue, which could challenge the state’s ability to maintain adequate funding to meet the state’s needs.
- **Fairness:** An SSF formula would disproportionately favor businesses that have property and employees in Kansas, but little sales.¹ In addition, the bill only allows certain types of industry to elect to use the SSF formula. It picks winners and losers on an inconsistent basis for tax responsibility.
- **Simplicity:** Organizations like the Tax Foundation have made clear the complications of shifting to an SSF method. This proposal creates more taxpayer loopholes when Kansas should work to close loopholes. The current three-factor apportionment formula balances property, sales, and payroll in the state as the determinants of a multistate corporation’s tax obligations to Kansas. The current method is consistent with the fundamental objective of the corporate income tax, which is to ensure that companies support the state services from which they benefit.

The implementation of an elective SSF formula for certain industries would be a step back from fair tax policy for Kansas businesses. Corporations with a substantial physical footprint in the state

¹ Institute on Taxation and Economic Policy. “Corporate Income Tax Apportionment and the ‘Single Sales Factor.’” August 1, 2012. <https://itep.org/corporate-income-tax-apportionment-and-the-single-sales-factor/>



benefit from Kansas-taxpayer-provided infrastructure, yet SSF ignores that footprint in determining their tax liability. An SSF formula would disproportionately favor businesses that have property and employees in Kansas, but little sales.²

A change to an SSF formula does not motivate the creation of jobs. Research³ has found an SSF formula will not attract manufacturing jobs (one of the industries that would be eligible to use the SSF formula) disproving previous research⁴ arguing the opposite. The table at the end of my testimony (Appendix 1), prepared by the Center on Budget and Policy Priorities, demonstrates that SSF is not strongly correlated with manufacturing job creation or retention. States with and without SSF are intermingled. If SSF was associated with an increase in jobs, we should see SSF states clustered at the top of the table and states with three-factor formulas clustered at the bottom. But that is not what the data shows.

It should not be surprising that the latest statistical research and the actual experience of SSF states does not support the claim that the adoption of this formula boosts in-state investment and job creation. The formula simply provides a tax cut for certain corporations that happen to have a disproportionate share of their property and personnel in a state relative to the share of their sales. The reduced tax responsibility is in no way contingent on their future job-creation behavior. Corporations can benefit from the tax change in perpetuity even if they never create a single new job in Kansas. To create jobs, Kansas needs “a more educated workforce, higher quality infrastructure, and other building blocks of a healthy economy.”⁵

Even within the Tax Foundation’s report to the legislative tax committees in 2020, they consider the merits of the traditional three-factor apportionment to the SSF:

“However, lawmakers should bear in mind the potential revenue consequences of any change in the apportionment formula. (States have undisputed authority to tax businesses with property and payroll in their states, but *under federal law, states lack nexus to tax companies that sell into a state but have no other connections to that state. Therefore, an exclusive focus on sales may generate less revenue, since some companies*

² Institute on Taxation and Economic Policy. “Corporate Income Tax Apportionment and the ‘Single Sales Factor.’” August 1, 2012. <https://itep.org/corporate-income-tax-apportionment-and-the-single-sales-factor/>

³ Merriman, David. “A Replication of ‘Coveting Thy Neighbor’s Manufacturing: The Dilemma of State Income Apportionment’ (Journal of Public Economics 2000).” *Public Finance Review* 43, no. 2 (March 2015): 185–205. <https://doi.org/10.1177/1091142114537892>.

⁴ Goolsbee, Austan and Maydew, Edward L., *Coveting Thy Neighbor’s Manufacturing: The Dilemma of State Income Apportionment* (February 1999). Available at SSRN: <https://ssrn.com/abstract=160535> or <http://dx.doi.org/10.2139/ssrn.160535>

⁵ Mazerov, Michael. Center on Budget and Policy Priorities. “Case for ‘Single Sales Factor’ Tax Cut Now Much Weaker.” April 1, 2015. <https://www.cbpp.org/blog/case-for-single-sales-factor-tax-cut-now-much-weaker>



*otherwise captured by that apportionment formula are not, in fact, subject to taxation.)*⁶ (italics and bold mine)

The Tax Foundation report made clear the complications of shifting to an SSF method. More consideration of corporate income tax aspects like the base rate, surtax rate, and other corporate provisions seemed more pressing. Of all the choices to improve corporate income tax, is the SSF the right choice right now?

While KAC opposes this bill and the use of the SSF formula to determine taxable business income, if the committee decides to move forward with this bill, KAC urges you to consider two amendments.

- First, this committee should make SSF apportionment mandatory for the industries named in the current bill, not elective – as all but four (Arizona, New Mexico, North Dakota, and Virginia) of the other states with this formula do. The elective option is the worst possible choice, which would sharply cut and potentially even eliminate (for manufacturers with only out-of-state customers) tax liability for corporations based here while allowing out-of-state businesses to continue using the current three-factor formula that minimizes their Kansas tax liability.

Elective SSF for manufacturers proved so costly to California that voters approved a ballot measure in 2013 to repeal it two years after it took effect.⁷ Out-of-state manufacturing businesses already benefit from a federal law (Public Law 86-272) that exempt them from taxes unless they have a physical presence in the state. If the goal of this bill is to incentivize Kansas job creation, why would we give a tax break to out-of-state businesses that create few (if any) jobs here by allowing them to choose the formula that enable them to pay the lowest tax?

- Second, the committee should enact provisions to ensure businesses that benefit from SSF are investing in the state, like what Kansas had in place previously. As you can read in the bill language, businesses were previously only eligible to make an SSF election if they could demonstrate investment, for example, through construction and paying employees above average wages (starting on pg. 6 of the bill). If the goal of this legislation is to create jobs, the bill language should clarify this expectation as a condition of using SSF. The businesses should only be eligible if they create measurable and significant in-state jobs and investment in the state. While KAC generally does not support tax incentives, we believe targeted tax incentives would be more accountable and cost-effective than this proposed

⁶ Tax Foundation Report on Kansas Tax Modernization from December 2019: <https://taxfoundation.org/kansas-tax-reform/>

⁷ Alan Prohosky, “Revenue Estimates of California’s Apportionment Changes,” State Tax Notes, August 13, 2018.



legislation.

Again, KAC does not support this legislation or the use of an SSF formula. As the bill stands, it serves as an ineffective reduction in corporate tax liability under the belief that corporate tax cuts increase jobs. We urge you to oppose HB 2186. We look forward to working with you to identify better ways to retain and attract jobs and businesses to Kansas, but HB 2186 would fail to do that. Thank you for the opportunity to voice our opposition, and please do not hesitate to contact me at emily@kac.org if you have any questions.



Appendix I: Percent Change in Manufacturing Employment, Dec. 2000–Dec. 2020
in States with Corporate Income Taxes (data not seasonally adjusted)

If greater weighting of the sales factor encouraged manufacturing job growth/retention, states shown in **bold** would be clustered toward the top, and states in *italic* would be clustered toward the bottom.

| | |
|--------------------|---------------|
| Utah | 11.9% |
| North Dakota | 0.4% |
| Idaho | -0.6% |
| Iowa | -9.5% |
| <i>Montana</i> | <i>-11.2%</i> |
| Nebraska | -13.4% |
| <i>Alaska</i> | <i>-17.7%</i> |
| Arizona | -18.6% |
| Florida | -19.3% |
| Oregon | -19.5% |
| Colorado | -19.6% |
| Wisconsin | -20.3% |
| <i>Kansas</i> | <i>-20.5%</i> |
| Kentucky | -21.1% |
| Minnesota | -22.2% |
| South Carolina | -22.2% |
| Indiana | -22.4% |
| Alabama | -22.7% |
| Missouri | -25.5% |
| Georgia | -26.2% |
| Louisiana | -26.5% |
| Tennessee | -30.9% |
| <i>Oklahoma</i> | <i>-31.7%</i> |
| Mississippi | -31.8% |
| Connecticut | -32.7% |
| <i>Hawaii</i> | <i>-33.9%</i> |
| California | -35.0% |
| Illinois | -35.3% |
| Virginia | -35.5% |
| Maryland | -36.8% |
| Pennsylvania | -37.3% |



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|----------------------|---------------|
| Maine | -37.3% |
| West Virginia | -37.4% |
| New Mexico | -37.6% |
| Arkansas | -37.8% |
| New Hampshire | -38.2% |
| Delaware | -39.1% |
| Vermont | -39.7% |
| North Carolina | -40.1% |
| Massachusetts | -41.9% |
| New Jersey | -42.1% |
| Rhode Island | -45.8% |
| New York | -46.2% |

States with Single Sales Factor Formula in Effect Through Period in **Bold**
 States with Equally-Weighted 3-Factor Formula in Effect Throughout Period in *Italic*



Appendix 2: Kansas Action for Children Tax Rubric

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| Adequacy | A tax system needs to pay for the services necessary to promote economic growth and education, to support basic needs, and to provide for many other important functions that contribute to a thriving community. Both short- and long-term adequacy are critical. |
| Fairness | Lower-income households shouldn't pay a higher share of their income in taxes than do high-income households and profitable corporations. People and companies in similar economic situations should pay roughly similar taxes. The fiscal "rules of the game" shouldn't place artificial constraints – like caps on income tax rates – that prevent policymakers from raising the revenue needed to finance public investments and to promote shared prosperity. |
| Equity | Equity needs to be built into fiscal policy. That means recognizing that tax policy is not race-neutral. Every policy impacts racial equity. It is important to assess fiscal policies for their impact on racial equity and to pursue policies that deliver anti-racist outcomes. |
| Simplicity | Tax systems should facilitate compliance by avoiding overly complicated provisions and narrowly applied loopholes. |
| Sustainability | A tax system needs to be constructed in ways that avoid – as much as possible – unpredictable, large fluctuations in the amount of revenue collected each year. |
| Elasticity | The amount of revenue collected should increase as the economy expands, reflecting the increased needs of education, transportation, and many other public services. |