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MEMORANDUM

TO: Governor's Council on Tax Reform

FROM: Mark A. Burghart, Secretary
Kansas Department of Revenue

RE: Legislative Update

DATE: August 26, 2020

Thank you for the opportunity to discuss the 2020 legislation recommended by the Governor's Council on Tax Reform (Council). The Council made seven specific recommendations in its Interim Report. Four of those recommendations required the introduction of legislation, the history of which is summarized below.

I. 2020 LEGISLATION

A. DIGITAL GOODS

1. Council Recommendation

Changes in technology have allowed what once were taxable sales of tangible personal property to avoid tax merely because the property is delivered in digital format. The technological advances in the delivery of products were never contemplated 82 years ago when the state sales and use tax was enacted in 1937. The state and local sales tax base continues to shrink in light of these unintended exclusions. The Council believes that the current treatment of digital asset sales is not fair and equitable. The inclusion of digital products in the sales and use tax base would be another step toward leveling the playing field between brick-and-mortar stores and retailers selling digital products. The Council recommends that the 2020 Kansas Legislature join the other 29 states to include the sale of digital products in the state and local sales tax base.

2. Council Bills

2020 S.B. 397 – Died in Senate Committee on Assessment and Taxation
2020 H.B. 2685 – Died in House Committee on Taxation

3. Summary of Legislation

S.B. 397 and H.B. 2685 would tax all sales of digital products and subscription services, including digital audio-visual works, digital audio works, digital books, artwork, digital photographs and pictures, periodicals, newspapers, magazines, video, audio and other greeting cards, graphics, templates, patterns, desktop applications, mobile applications, web applications, cloud based

applications, native applications, online games, video games, electronic games, any digital code related to any of the above items and any streaming services related to the above items.

4. Other Bills

2019 H.B. 2352 – Died in House Committee on Taxation

5. Fiscal Note

FY 2021 -- \$45.6 Million (all funds)

FY 2022 -- \$50.4 Million (all funds)

B. MARKETPLACE FACILITATOR

1. Council Recommendation

K.S.A. 79-3705c allows Kansas to require out-of-state retailers to register and collect and remit compensating use tax on sales of tangible personal property into the State of Kansas. The Department of Revenue issued notice No. 19-04 on August 1, 2019 notifying out-of-state retailers to register with the State of Kansas. The existing statutory scheme does not allow Kansas to require marketplace facilitators to do the same. A marketplace facilitator is a person who facilitates sales by an internet retailer through a physical or electronic marketplace. Kansas is one of only five states that has not enacted a marketplace facilitator provision. The Council recommends that the 2020 Legislature consider and pass legislation that would require marketplace facilitators to register and begin collecting compensating use tax on sales to Kansas customers. This legislation would further level the tax playing field that has for 52 years been skewed in favor of out-of-state retailers and against in-state main street Kansas retailers.

2. Council Bills

2020 S.B. 399 – Died in Senate Committee on Assessment and Taxation

2020 H.B. 2657 – Died in House Committee on Taxation

3. Summary of Legislation

S.B. 399 and H.B. 2657 would require marketplace facilitators to begin collecting and remitting sales and use tax on goods sold into the State of Kansas. The bill contains a comprehensive definition of marketplace facilitator which generally includes a person that has an agreement with marketplace sellers to facilitate sales through a physical or electronic marketplace.

4. Other Bills

2020 House Sub. – Died on House Calendar
for S.B. 266

2020 S.B. 369 – Died in Senate Committee on Assessment and Taxation

2020 H.B. 2513 – Died in House Committee on Taxation

2020 H.B. 2014 – Introduced by Representative Stephen Johnson;
*Special Session Died in House Committee on Taxation

5. Fiscal Note

FY 2021 -- \$30.4 Million (all funds)

FY 2022 -- \$33.6 Million (all funds)

The fiscal note for House Sub. for S.B. 266 is \$19.4 Million for FY2021 due to the \$100,000 *de minimis* threshold established by the bill.

C. FOOD SALES TAX REFUNDABLE INCOME TAX CREDIT

1. Council Recommendation

In order to reduce the regressivity of the sales tax on food, the Council recommends consideration of a new refundable food sales income tax credit that will benefit as many as 400,000 Kansas households to help offset state and local sales tax paid on groceries. Elimination of the prior food sales tax rebate program in 2012 coupled with sales tax rate increases exacerbated the overall regressivity of the Kansas tax structure. The Council notes that targeting this relief to low and moderate-income taxpayers would be a more effective way of providing relief to those who need it the most than would lowering the rate by one cent on all food purchases. The Council recognizes that proposals to reduce the food sales tax rate are likely to be considered during the 2020 Legislative Session and notes that the hypothetical taxpayer models being developed by Dr. Ginther will assist in evaluating such proposals compared to refundable credit options.

2. Council Bills

2020 S.B. 398 – Died in Senate Committee on Assessment and Taxation

2020 H.B. 2720 – Died in House Committee on Taxation

3. Summary of Legislation

H.B. 2720 would create a new refundable food sales tax credit and repeal the existing non-refundable food sales tax credit. The new tax credit amount would be determined by tax filing status and could be claimed by all taxpayers with income at or above the following federal adjusted gross income levels:

<u>Filing Status</u>	<u>Income Level</u>	<u>Credit Amount</u>
Single	\$30,000	\$ 60
Head of Household	\$40,000	\$180
Married Filing Jointly	\$40,000	\$240
Married Filing Separate	\$30,000	\$ 60

The bill would allow the income level and tax credit amounts to be adjusted annually, according to the cost-of-living adjustments from the federal Internal Revenue Service (IRS).

4. Fiscal Note

FY 2021 – (\$53.2) Million (all funds)

FY 2022 – (\$54.8) Million (all funds)

D. PROPERTY TAX LID EXEMPTION

1. Council Recommendation

An issue of critical importance to the continued cost-share approach to transportation projects concerns the local property tax lid. The Council recommends consideration of legislation that would provide an exemption from the tax lid for cities and counties for transportation costs that would allow the local units to participate in the funding of infrastructure projects as partners with the state.

2. Council Bill

2020 H.B. 2696 – Died in House Committee on Taxation

3. Summary of Legislation

H.B. 2696 authorizes the governing body of any city or county to increase property taxes, without voter approval, for expenses related to transportation construction projects.

4. Fiscal Note

FY 2021 – No fiscal effect on state property tax revenues

II. TOPICS FOR FURTHER REVIEW

In its Interim Report, the Council noted that it would continue to meet in 2020 to again make recommendations in advance of the 2021 Legislative Session. The Council's work during the remainder of 2020 would include a review of the following:

- proposals to broaden the tax base by examining the continued efficacy of certain exemptions and exclusions;
- an examination of the nature of the Kansas tax structure to determine its progressivity or regressivity to be conducted by expert economists;
- a review of the earned income tax credit;
- an examination of the current property tax lid and the policy issues associated with the lid;
- continued review of the issue of imposing sales tax on food;
- implications of 2017 federal tax reform as they relate to itemized deductions and the taxation of foreign source income;
- a comparison of the Kansas tax structure and those surrounding states; and
- a general review of the property tax system and options for relief from excessive valuations and levies.