

MINUTES OF THE HOUSE COMMITTEE ON TAXATION.

The meeting was called to order by Chairperson Keith Roe at 9:00 a.m. on February 17, 1993 in Room 519-S of the Capitol.

All members were present except:

Committee staff present: Tom Severn, Legislative Research Department
Chris Courtwright, Legislative Research Department
Don Hayward, Revisor of Statutes
Bill Edds, Revisor of Statutes
Lenore Olson, Committee Secretary

Conferees appearing before the committee:

Representative Phill Kline
Dr. Darwin Daicoff, University of Kansas
Representative Jene Vickrey
Gerry Ray, City of Overland Park
Harold Teague, Teague Electric
Bob Corkins, Kansas Chamber of Commerce and Industry
Dan Morgan, Kansas Associated General Contractors
Larry Knott, Allen, Gibbs & Houlik, Wichita
Alan Alderson, Home Builders Association of Greater Kansas City
Don Popejoy, Kansas Contractors Association
Gus Meyer, Rau Construction Company
Karen France, Kansas Association of Realtors

Others attending: See attached list

Chairperson Roe opened the hearing on HB 2148.

<u>HB 2148</u>	Sales tax exemption for services associated with original construction of a building or facility.
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Representative Phill Kline testified in support of HB 2148, stating that as a result of this tax, about 2,200 Kansas construction jobs will be lost each year which equals a loss in gross payroll of \$48.4 million (Attachment 1).

Dr. Darwin Daicoff, University of Kansas, presented an economic analysis of the effect of taxing services associated with original construction of a building or facility. Dr. Daicoff said that while it cannot be claimed that the imposition of the sales tax on construction services has been the only factor impacting the construction industry in Kansas, the new sales tax is surely a major factor (Attachment 2). Dr. Daicoff responded to questions and said that construction services have also been recently affected by increases in lumber prices and by interest rate moves.

Representative Jene Vickrey testified in support of HB 2148, stating that none of the states bordering Kansas penalizes new economic growth with service taxes on labor as does Kansas.

Gerry Ray, City of Overland Park, testified in support of HB 2148. She stated that in the Kansas City area, many subcontractors are considering moving their businesses to Missouri and some general contractors have threatened to hire only Missouri subcontractors (Attachment 3).

Harold Teague, Teague Electric, testified in support of HB 2148. He said that the administrative nightmare caused by this tax forced him to look at alternatives to restructure and relocate his business (Attachment 4).

CONTINUATION SHEET

MINUTES OF THE HOUSE COMMITTEE ON TAXATION, Room 519-S Statehouse, at 9:00 a.m. on February 17, 1993.

Bob Corkins, Kansas Chamber of Commerce and Industry, testified in support of HB 2148, stating that Kansas cannot afford isolated taxes which stick out like sore thumbs in this part of the country. He said that KCCI advocates an increase in the state sales tax rate to replace the recently broadened sales tax base (Attachment 5).

Dan Morgan, Kansas Associated General Contractors, testified in support of HB 2148. Mr. Morgan said that there is no question that this tax on new construction labor services has placed the State of Kansas at a serious competitive disadvantage when competing against neighboring states for new business, expansion and economic development (Attachment 6).

Larry Knott, Allen, Gibbs & Houlik, testified in support of HB 2148, stating that this tax is a major factor for the homeowner, is almost unenforceable, and the revenue estimates that have been given for this tax are fundamentally flawed (Attachment 7).

Alan Alderson, Home Builders Association of Greater Kansas City, testified in support of HB 2148, stating that the imposition of sales tax on original construction labor services has created more difficulties for contractors than the amount of revenue being collected could ever possibly justify (Attachment 8).

Don Popejoy, Kansas Contractors Association, testified in support of HB 2148. He stated that the Association believes this tax was inadvertently added to the school finance measure and they do not believe the intent of the Legislature was to have it affect the highway industry (Attachment 9).

Gus Meyer, Rau Construction Company, testified in support of HB 2148. Mr. Meyer stated that the sales tax on construction services is a disaster to economic development in Kansas and is driving the people who have a choice away from Kansas (Attachment 10).

Karen France, Kansas Association of Realtors, testified in support of HB 2148, stating that placing a sales tax on new construction is a self-defeating effort on the part of the state of Kansas (Attachment 11).

Written testimony in support of HB 2148 was submitted by:

Tom Riederer, Lenexa Chamber of Commerce (Attachment 12)

Chris Beal, Greater Kansas City Chamber of Commerce (Attachment 13)

Mark McCrory, McCrory Construction, Inc. (Attachment 14)

Gordon Garrett, Commercial Property Association of Kansas (Attachment 15).

Roger Schultz, Schultz Construction, Inc. (Attachment 16)

James E. Dunning, Certified Public Accountant, Wichita (Attachment 17)

Wess Galyon, Wichita Area Builders Association (Attachment 18)

Water District No. 1 of Johnson County (Attachment 19)

Chairperson Roe closed the hearing on HB 2148.

The meeting adjourned at 10:57 a.m.

The next meeting is scheduled for February 18, 1993.

Date: 2/17/93

GUEST REGISTER

HOUSE COMMITTEE ON
ASSESSMENT AND TAXATION

NAME	ORGANIZATION	ADDRESS	PHONE
HAROLD PITTS	AARP- CCTF	Topeka	
Tom Slattery	AGC of Ks	TOP	
DAN MORGAN	KC Chpts, AGC	KC	
Gus Meyer	Rau Construction	Overland Park	
JENE VICKREY	Rep. 6th Dist	Louisburg Kc	
Forrest Gossett	Allen, Gibbs & Houlik	Wichita	
Larry Knott	Allen, Gibbs. + Houlik	Wichita	
Tom Robben	Water District No 1 of Johnson Co	Mission	
Laurie Krause	Water District No 1 of Jo. Co.	Shawnee	
Robert Trautzo	Ks Gov Consulting	Topeka	
Frank Stukla	NBA of Ks	Topeka	
Mark McCrory	Homebuilders	Topeka	
Devin V. Darriff	KO	Lawrence	
KAREN FRANCE	KAR	TOPS KA	
Carol Sader	Legislature	P.V.	
Bob Corkins	KCCI	Topeka	
ALAN ANDERSON	HOME BUILDERS ASS'N OF ^{GREATER} K.C.	TOPEKA	
Bill Anderson	Water Dist #1 of Jo Co	Mission	
Mark Larsson	Interfaith Impact	Lawrence	
Catherine Hotdeman	Wichita	Wichita	
ART BROWN	TOPEKA ICS ICS President	topeka	
SUSAN SONGERS	KSCPA	Topeka	

Date: 2/17/93

GUEST REGISTER

HOUSE COMMITTEE ON ASSESSMENT AND TAXATION

NAME

ORGANIZATION

ADDRESS

PHONE

Linda Kemp	KS Interfaith Impact	Topeka	
ROBERT D. CAREY	" " "	MOLENE	
Harold E. Schmitt	" "	Joling	
William Doner	" " " "	Pittsburg	
DON POPEJOY	Kansas Contractors Assn	Ulysses	
BUTCH SPRAY	✓ ✓ ✓	GREAT BEND	
DAN RAMLOW	" " "	TOPEKA	
Jim Wottoff	Kansas AFL-CIO	Topeka	
Jack Evans	Ok USA	Viola	
John Weil	Horn, Ebert & Rosch	Topeka	
KEN TBERG	Interfaith Impact	Louisburg	
Ron Eslinger	KS Interfaith Impact	Topeka	
Reed W Davis	KDOT	Topeka	
Becky Berg	Ks. Interfaith IMPACT	Louisburg	
Nelsie Sweeney	Overland Park Chamber	Overland Park	
Chris Bal	Greater K.C. Chamber	Kansas City	
BRAD SMOOT	NBA of KC	Topeka	
Sara Corless	NBA of KC	Reynolds	
Gerry Ray	City of Overland Park & Johnson County	Overland Park	
Tom Riboord	Overland Chamber of Commerce	Overland	
Steve Stotts	Revenue	Topeka	
MARK CIARDULLO	REVENUE	TOPEKA	

PHILL KLINE
REPRESENTATIVE, 18TH DISTRICT
10624 W. 61ST ST.
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913-268-5402

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TOPEKA, KANSAS 66612-1504
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TOPEKA

HOUSE OF REPRESENTATIVES

42807

MEMORANDUM

COMMITTEE ASSIGNMENTS

MEMBER: EDUCATION
FEDERAL & STATE AFFAIRS
JOINT COMMITTEE ON ADMINISTRATIVE
RULES & REGULATIONS

TO: HOUSE TAXATION COMMITTEE

FROM: PHILL KLINE

RE: H.B. 2148

DATE: FEB. 17, 1993

Thank for the opportunity to speak with you regarding the need to restore the sales tax exemption for labor on new construction.

THE TAX IS A DRAG ON THE KANSAS ECONOMY

Testimony will be provided that indicates that 2,200 Kansas construction jobs a year are lost as a result of the tax.

A. Lost Income Tax Revenue from Lost Construction Jobs

LOSS = \$1.694 MILLION

This equals a loss in gross payroll of \$48.4 million. Applying the Kansas lowest income tax rate to this figure demonstrates that the loss of these jobs results in the loss of \$1.694 million in state income tax revenue. (Based on industry average income of \$22,000).

B. Lost Sales Tax Revenue from Lost Construction Jobs

LOSS = \$1,422,690

The U.S. Department of Commerce estimates that the average family uses 60% of their gross income as discretionary income. Accordingly, state sales tax would apply to 60% of the gross payroll loss. Applying the state sales tax of 4.9% to 60% of the gross payroll loss demonstrates lost sales tax revenue of \$1,422,690.

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House Taxation Cmte
Attachment 1

C. Lost Housing Units

LOSS = 2,340 \$100,000 HOUSING UNITS ANNUALLY

1. Lost property tax = \$926,640. Computed by applying 12% assessed value and statewide 33 school mill. Does not include 1 1/2 mill building fund loss.

D. Lost Growth in Sales and Income Tax

LOSS INCOME TAX = \$2.457 MILLION

LOST SALES TAX = \$2,063,880

Based on loss of 2,340 families with average gross income of \$30,000 (minimum amount necessary to qualify for a \$100,000 home.)

E. The Retail Ripple

Gross retail purchasing power lost = \$71,160,000.
Multiply by .175 (percentage of retail dollar applied to payroll, CERI) = \$12,453,000 payroll loss. This equals a loss of \$435,000 in income tax revenue and \$366,118 in sales tax revenue.

The average retail salary is \$15,000 (Department of Commerce Economic Statistics Administration for 1990 with growth factor of .12) and, therefore, the loss of over 830.2 jobs.

This ripple continues but lessens significantly.

F. NOTE

These figures do not include commercial property, the ripple effect on the service industry and resulting loss of income and sales tax revenue, or lost corporate tax etc.

TOTAL = over \$8 million

Testimony of Dr. Darwin W. Daicoff before the Kansas House
Assessment and Taxation Committee, February 17, 1993.

I have conducted an economic analysis of the Kansas construction industry. The purpose of the analysis is to determine what has happened to this industry since the imposition of a sales tax on original construction services, which took effect on July 1, 1992. This is accomplished by examining total construction activity as measured by construction permits and construction employment. Particular attention is directed to the size distribution of Kansas construction firms. The analysis concludes with a detailed review of housing construction.

Building Permits

The dollar value of construction permits issued in 33 major Kansas cities are available from the Center for Economic Development and Business Research at The Wichita State University, see Table 1. These consistent data provide a measure of construction activity (including commercial, housing, and other) from January 1989 through November 1992. It should be noted that, in general, 1992 was a better year for construction than the three prior years. However, because the focus of this economic analysis is since July 1992, a more detailed examination is needed. What is needed is a measure of how well the industry has done from July 1992 through November 1992, compared to how it had been doing earlier. For the first half of 1992, monthly construction permits averaged \$108.5 million and in the latter five months the average

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Attachment 2

was \$102.7 million. Thus, construction activity, by this measure, fell by 5.3% after the sales tax increase. This decline is not a typical seasonal factor. This fact is made clear by observing that during 1989, 1990 and 1991 average monthly construction building permit dollar values were 1.3% larger in the July-November time period than they had been in the January-June time period. Had such growth occurred in 1992 permits would have averaged \$109.9 million. Then the monthly "loss" (vs. the actual of \$102.7 million) was \$7.2 million, or \$36.0 million in total construction activity for the five months.

Employment

Kansas construction activity also can be measured by employment. Employment information is available from the Labor Market Information Services of the Kansas Department of Human Resources. Again, consistent data from January 1989 through November 1992 are employed for this analysis, see Table 2.

In 1992 construction employment showed an improvement over 1989, 1990 and 1991. Breaking 1992 into two time periods (before and after the sales tax) is necessary. For the first six months of 1992, Kansas construction employment averaged 44.1 thousand and for the next five months averaged 47.8 thousand. This is a 8.4% increase. While there was an increase in the latter part of the year, this increase was less than the increase in either 1989, 1990 or 1991; for these three years the increase averaged 12.3%. Had the July through November 1992 Kansas construction employment

increased (from the first six months of 1992) at its historical rate it would have averaged 49.6 thousand. By this measure, since the sales tax increase, 1.8 thousand construction jobs were "lost" - actual employment less historically projected.

Size Distribution

Regulations regarding the collection of the sales tax on original construction may place small Kansas construction firms at a disadvantage relative to out-of-state firms that compete for construction subcontracts. These firms are typical of SIC 17 firms and include plumbing, heating, air conditioning; painting and paper hanging; electrical work; carpentry and floor work; etc.

The U. S. Department of Commerce publishes information on the size of establishments by industry detail. These County Business Pattern data are for 1990. There are 3,617 establishments for this industry in Kansas. Their employment is 26,155; with an annual payroll of \$592 million. Most of these firms are small--2,277 (63.0% of the total) having less than 5 employees and 3,003 (83.5% of the total) have less than ten employees. Only a few firms (71 or 2.0% of the total) have 50 or more employees. Two subindustries are noteworthy in that they have a very large portion of small establishments. These are painting and paper hanging and carpentry and floor work, where 89.7% and 92.1%, respectively, of the establishments have less than ten employees.

Then, to the extent of the competitive disadvantage, there is a very large portion of existing Kansas special trade construction firms at jeopardy to out-of-state subcontractors.

Housing Units

Housing construction is a component of the construction industry that merits particular attention. Fortunately, the U. S. Department of Commerce publishes data on Housing Units Authorized by Building Permits; monthly data are available for Kansas and other states, through November 1992. These data report for more Kansas permit issuing places than the WSU data.

Influenced by lower interest rates, this component of the Kansas construction industry did better in 1992 than in 1989, 1990, or 1991. Both the number of units (single and multi unit) and dollar value (single and multi unit) exhibit an increase. During the first six months of 1989, 1990 and 1991 permits were issued for a monthly average of 650 housing units in Kansas, see Table 3. For July through November of these years the comparable figure was 9.0% larger. In 1992 a different situation prevailed. The latter five months recorded a 14.2% decline from the first six months of the year.

Had Kansas maintained the historical 9.0% increase in the July through November 1992 time period, 916 housing units permits would have been issued; the actual figure was 721. Thus, after the sales

tax change 195 housing units were "lost" per month or 974 for the five month period.

A comparison can be made between Kansas housing activity and that activity in other states. In order not to be influenced by large states some distance from Kansas and subject to quite different economic influences, this analysis consists of comparing Kansas to bordering states, where economic factors are more similar. The bordering states are Missouri, Nebraska, Oklahoma, and Colorado, see Table 4.

Housing construction activity can be measured by the total number of units, the number of 1-unit units, total dollar valuation and 1-unit dollar valuation. Comparisons can be made by expressing the Kansas statistics as a percentage of the comparable figure for each of the four bordering states and the sum of the four bordering states. A comparison can be made for the July 1992 through November 1992 time period against the prates change period of that year--January 1992 through June 1992, see Table 5. For each of the comparisons, twenty in all, Kansas housing construction was a much smaller portion of each of the states in the region and all the bordering states in the latter part of 1992. Thus, whatever economic forces were operating in the Kansas region, in the last five months of 1992 Kansas housing construction was depressed relative to housing construction in the Kansas region.

Just before the sales tax imposition, by various measures, Kansas housing construction was between 17.3 and 17.5 percent of the bordering state total. After the sales tax increase, the

Kansas share slipped to between 14.2 and 14.9 percent of the bordering states. For total housing units, the decline was from 17.5% to 14.2% and from 17.3% to 14.6% for the total housing value. For single unit housing the decline was from 17.3% to 14.4% and 17.3% to 14.9% in value.

Had the Kansas percentage remained the same after the sales tax increase as Kansas recorded in the first half of 1992, permits for 838 additional housing units (with 626 of them 1-unit) with a permit value of \$60.5 million (with 1-unit value of \$56.0 million) would have been issued between July 1992 and November 1992.

Conclusion

While it cannot be claimed that the imposition of the sales tax on construction services has been the only factor impacting the construction industry in Kansas, the new sales tax is surely a major factor. The measures employed in this analysis produce a fairly consistent pattern. It is clear that 1992 was a relatively good year for Kansas construction, at least relative to depressed years of 1989, 1990, and 1991.

However, the last part of the year, July through November, was worse (or less good) than the first six months of the year. The WSU data point to a \$36.0 million construction permit "loss". Human Resources data are consistent with a construction job loss of 1,800. A very large portion of the construction industry, where subcontracting is common, are small (less than ten employees per

firm) and may be at jeopardy. U. S. Department of Commerce data permits a comparison of Kansas to its historical trends and to regional construction activity. Based on historical Kansas housing permit information, Kansas total housing unit permits were reduced by 974. Regional comparisons produce estimates of a Kansas "lost" of 838 housing units with a permit value of \$60.5 million in the July-November 1992 time period. Then, either a historical or a regional approach produce estimates of significant "loss".

TABLE 1

DOLLAR VALUE OF KANSAS CONSTRUCTION PERMITS

	1989	1990	1991	AVERAGE 1989-1991	1992
JAN	93,512,775	84,985,859	37,220,018	71,906,217	102,769,275
FEB	97,014,951	61,748,166	72,772,652	77,178,590	100,552,622
MAR	109,727,994	110,720,547	78,452,389	99,633,643	98,501,013
APR	81,549,000	98,545,027	89,696,447	89,930,158	116,454,520
MAY	120,225,757	113,169,876	90,755,637	108,050,423	128,604,836
JUN	128,922,984	99,646,145	97,568,302	108,712,477	103,980,448
JAN-JUN	105,158,910	94,802,603	77,744,241	92,568,585	108,477,119
JUL	97,680,765	83,400,525	96,700,749	92,594,013	119,538,495
AUG	113,043,934	106,539,142	73,565,766	97,716,281	106,103,957
SEP	71,756,056	123,359,640	87,703,563	94,273,086	101,308,068
OCT	113,698,488	96,305,669	94,241,170	101,415,109	109,990,899
NOV	95,898,603	70,381,372	72,133,280	79,471,085	76,678,239
DEC	78,322,907	76,366,995	64,808,972	73,166,291	
JUL-NOV	98,415,569	95,997,270	84,868,906	93,093,915	102,723,932
JUL-DEC	95,066,792	92,725,557	81,525,583	89,772,644	
JAN-DEC	100,112,851	93,764,080	79,634,912	91,170,615	105,862,034
RATIO	-6.41	1.26	9.16	1.34	-5.30

SOURCE: Center for Economic Development and Business Research, Wichita State University.

RATIO is the percentage change from the first six months to the July through November time period.

TABLE 2

KANSAS CONSTRUCTION EMPLOYMENT

	1989	1990	1991	AVERAGE 1989-1991 (thousand)	1992
JAN	35.2	36.6	33.7	35.2	40.5
FEB	33.4	36.1	35.5	35.0	41.1
MAR	36.5	38.0	37.4	37.3	42.6
APR	39.2	40.7	40.9	40.3	45.5
MAY	41.1	42.4	42.3	41.9	46.7
JUN	43.0	45.3	44.3	44.2	48.1
JAN-JUN	38.1	39.9	39.0	39.0	44.1
JUL	43.6	45.1	44.9	44.5	49.0
AUG	44.0	45.0	44.8	44.6	48.4
SEP	41.9	43.8	44.7	43.5	47.7
OCT	43.0	43.3	44.4	43.6	47.4
NOV	42.2	42.3	43.3	42.6	46.4
DEC	38.4	40.4	43.1	40.6	
JUL-NOV	42.9	43.9	44.4	43.8	47.8
JUL-DEC	42.2	43.3	44.2	43.2	
JAN-DEC	40.1	41.6	41.6	41.1	45.8
RATIO	12.80	10.16	13.85	12.27	8.39

SOURCE: Labor Market Information Services, Kansas Department of Human Resources.

RATIO is the percentage change from the first six months to the July through November time period.

TABLE 3

KANSAS TOTAL HOUSING UNIT PERMITS

	1989	1990	1991	AVERAGE 1989-1991	1992
JAN	533	437	288	419	629
FEB	473	442	528	481	776
MAR	818	775	684	759	855
APR	785	820	780	795	924
MAY	749	700	758	736	1,021
JUN	755	688	678	707	833
JAN-JUN	686	644	619	650	840
JUL	764	672	735	724	733
AUG	697	685	610	664	723
SEP	981	550	640	724	686
OCT	809	691	634	711	730
NOV	969	716	508	731	732
DEC	879	352	597	609	
JUL-NOV	844	663	625	711	721
JUL-DEC	850	611	621	694	
JAN-DEC	768	627	620	672	786
RATIO	23.12	2.97	0.98	9.02	-14.16

SOURCE: U.S. Bureau of the Census, Housing Units Authorized by Building Permits.

RATIO is the percentage change from the first six months to the July through November time period.

TABLE 4

KANSAS HOUSING PERMITS AS % OF BORDERING STATES

1992	Total (units)	1-unit (units)	Total (thousand dollars)	1-unit (thousand dollars)
JAN	18.54	19.98	19.99	21.34
FEB	19.34	17.55	17.99	17.93
MAR	16.77	16.39	16.67	16.79
APR	16.29	16.57	15.96	16.29
MAY	19.37	18.77	18.76	18.35
JUN	15.38	15.95	15.93	15.94
JAN-JUN	17.45	17.33	17.32	17.31
JUL	13.09	15.56	15.52	16.71
AUG	14.17	16.90	15.71	16.93
SEP	12.05	13.06	12.99	13.61
OCT	13.40	11.98	13.07	12.32
NOV	20.20	15.42	16.63	12.96
JUL	14.17	14.41	14.63	14.91

SOURCE: see Table 3.

RATIO see Table 3.

TABLE 5

KANSAS HOUSING PERMITS AS PERCENTAGE OF STATES AND REGION

	Total (units)	1-unit (units)	Total (thousand dollars)	1-unit (thousand dollars)
January 1992 through June 1992				
MISSOURI	45.05	47.18	53.66	55.34
NEBRASKA	142.24	159.99	186.09	196.47
OKLAHOMA	138.79	120.05	143.32	135.12
COLORADO	47.94	45.62	37.40	36.77
BORDERING	17.45	17.33	17.32	17.31

July 1992 through November 1992

MISSOURI	39.42	42.35	48.41	51.06
NEBRASKA	119.29	142.99	168.83	174.87
OKLAHOMA	123.48	105.97	132.45	125.22
COLORADO	34.83	34.05	29.23	29.61
BORDERING	14.17	14.41	14.63	14.91

SOURCE: see Table 3.

RATIO see Table 3.

2-12



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Testimony before the House Taxation Committee

Keith Roe, Chairman

Good morning, Chairman Roe and members of the House Taxation Committee. My name is ^{Gerry Ray} ~~Ed Eilert~~, ~~Mayor of the~~ City of Overland Park. I am here today to speak in favor of House Bill 2148, repealing the sales tax on original construction of buildings and facilities.

In our initial analysis of this tax it became evident that numerous loopholes, inequities, and opportunities for "creative tax avoidance" existed. A majority of these loopholes favored the larger contractors over smaller ones. Some examples include:

- . The Department of Revenue, Division of Taxation, advises that original construction labor services performed by a general contractor prior to entering a written binding contract with the purchaser of the home are exempt from sales tax. The larger contractors who can afford to finance and build a home in advance of having a contract for sale are not impacted by this tax.

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Attachment 3

- A general contractor may accept in good faith an invoice or bid from a subcontractor that states "all applicable sales tax is included." The general contractor will be absolved from any further liability for the sales tax by accepting in good faith the subcontractor's invoice or bid. The burden and liability for collecting this tax rests with the subcontractor.
- The 1992 Legislature passed legislation that revised the Kansas Enterprise Zone Act to extend development incentives to businesses through the entire State of Kansas. No longer do businesses have to locate or expand in a predesignated "zone" to be eligible for benefits.

Manufacturing firms creating 2 or more jobs or non-retail firms that create 5 or more jobs may qualify for a sales tax exemption on construction materials and services. The bottom line is that large commercial operations are exempted from paying the tax, but the homeowner who has no means of avoiding the tax is left to bear the additional burden.

The issue of whether or not to expand the base and impose a sales tax on professional services was considered by the Legislature. Proponents of this legislation were not successful. However, recent administrative rulings by the Department of Revenue now conclude that professional services, such as architecture, engineering, or surveying, performed by a contractor, in addition to the taxable

services performed by the same contractor, are not excludable from the taxable base. It appears someone has cleverly found a way to back-door a tax on professional services.

- Pursuant to KSA 12-191, the labor, profit and overhead portion of a total contract under \$10,000 is subject to the contractor's business site sales tax rate in addition to the state sales tax. If a business location does not exist in Kansas and the total contract is under \$10,000, the labor, profit, and overhead is subject to the state sales tax rate only. In essence, no city sales tax will be collected unless the business is domiciled in Overland Park.

The above-mentioned provision is cause for great concern, because of the potential loss of local jobs that may occur. It has not been a full year since the implementation of this tax, but three things are already occurring that will eventually result in the loss of local jobs.

- (1) Kansas subcontractors are considering relocating their billable offices to Missouri to take advantage of this loophole and to avoid paying this tax.
- (2) In an attempt to keep the cost down on a new home, general contractors have threatened to hire only Missouri subcontractors..

- (3) Other local subcontractors are planning to move outside the corporate limits of any city into unincorporated areas just to avoid the 1% local tax.

The continued imposition of the sales tax on construction places an additional burden on smaller contractors, because the costs of compliance associated with this new legislation are proportionately greater for smaller firms and make up a greater percentage of their total sales.

Placing the burden on smaller contractors is not economically rational, because it is the smaller contractors who are largely responsible for the growth in construction employment. According to Dun and Bradstreet, 46% of the residential construction firms in Johnson County employ 2 or fewer employees; 59% have 3 or fewer employees. These entrepreneurs are not only the backbone of the construction industry in Johnson County, but also of the State of Kansas. The continued imposition of this tax places an undue burden and will have a disparate impact on the firms that are contributing heavily to our economy.

I reiterate my support for the repeal of this tax because of its inherent inequities. I am not convinced that it was the intent of this Legislature to create a tax policy that will result in the loss of local jobs and increased economic development for the State of Missouri.

I am also not convinced that the slight increase in sales tax revenue is enough to compensate for the lack of fairness in how this tax is applied. I sincerely believe that if a cost/benefit analysis were conducted on this tax, the cost of loopholes, inequities, confusion and loss of jobs would certainly far outweigh the benefits (\$1.5 million in revenue for the first six months). We urge your careful reconsideration of this matter and trust that you will conclude that a complete repeal is the best solution toward correcting a system so inundated with flaws.

Thank you for this opportunity. I would be happy to respond to questions.



Electric Construction, Inc.

TESTIMONY PROVIDED TO THE HOUSE TAXATION COMMITTEE

REGARDING THE CONSTRUCTION SALES TAX

Chairman Roe and Members of the Committee:

My name is Harold Teague. I am the owner of Teague Electric Construction, Inc. of Lenexa, Kansas. My business has been in operation in Kansas for approximately 15 years and in Lenexa for the last 13 years. I have 68 employees on my payroll and am a resident of Overland Park, Kansas. In 1992, my business paid state, federal and local taxes on the more than \$ 5 million in business we did.

As a result of the actions of the 1992 Kansas Legislature, my business was forced to quickly respond to the new law requiring the collection of sales tax on "labor services" in new construction implemented in June. About that same time, I had an opportunity to bid on a job in Overland Park. My bid was \$ 41,698.37 of which included \$ 2,544.97 in sales tax to cover tax on the materials, labor, profit and overhead as required by the printed guidelines of the Kansas Department of Revenue. Unfortunately, I lost the bid to a Texas contractor. After some checking, I was later told that the additional sales tax made the difference between getting the job and losing it. The Texas contractor made it clear to the company offering the job that they would not have to pay the tax.

For this reason and the ensuing administrative nightmare that was created by the Kansas Department of Revenue, I was forced to look at alternatives to restructure and relocate my business. I am negotiating for a building in Grandview, Missouri. I will meet again on Friday with the building owners to firm up my plans. I am in the process of obtaining the appraisal and finalizing my decision.

2/17/93

House Taxation Comte

Attachment 4

cont. page 2

Your decision today or sometime in the next few months may come too late to change my plans, but I would urge you to take a common sense solution to your need for revenue. Kansas needs the kind of jobs my employees have. Good jobs are hard to find as many discovered in the last two to three years. I hope you will do your best to repeal this tax that has put Kansas construction at a distinct disadvantage.

Thank you for your interest. I would be happy to answer any of your questions.

Sincerely,

TEAGUE ELECTRIC CONSTRUCTION, INC.



Harold A. Teague
President

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LEGISLATIVE TESTIMONY

Kansas Chamber of Commerce and Industry

500 Bank IV Tower One Townsite Plaza Topeka, KS 66603-3460 (913) 357-6321



A consolidation of the
Kansas State Chamber
of Commerce,
Associated Industries
of Kansas,
Kansas Retail Council

HB 2148

February 17, 1993

KANSAS CHAMBER OF COMMERCE AND INDUSTRY

Testimony Before the
House Committee on Taxation

by

Bob Corkins
Director of Taxation

Mr. Chairman and members of the Committee:

My name is Bob Corkins, director of taxation for the Kansas Chamber of Commerce and Industry. Thank you for the opportunity to speak today. For years, I've been arguing the Chamber's position that we strongly oppose **any** expansion of Kansas' sales tax base. Now, our members are committed to removing that expansion which was suffered through passage of the 1992 school finance reforms...in particular, the tax upon original construction services. We therefore support HB 2148.

The Kansas Chamber of Commerce and Industry (KCCI) is a statewide organization dedicated to the promotion of economic growth and job creation within Kansas, and to the protection and support of the private competitive enterprise system.

KCCI is comprised of more than 3,000 businesses which includes 200 local and regional chambers of commerce and trade organizations which represent over 161,000 business men and women. The organization represents both large and small employers in Kansas, with 55% of KCCI's members having less than 25 employees, and 86% having less than 100 employees. KCCI receives no government funding.

The KCCI Board of Directors establishes policies through the work of hundreds of the organization's members who make up its various committees. These policies are the guiding principles of the organization and translate into views such as those expressed here.

2/17/93

House Taxation Committee
Attachment 5

KCCI's guiding tax objective is to achieve an overall Kansas tax structure which is competitive with neighboring states. We need not be the lowest tax state, but we cannot be the highest, and we cannot afford isolated taxes which stick out like sore thumbs in this part of the country.

If this assessment of tax policy sounds familiar to you, it may be because Mr. Redwood and Ms. Oslund of Kansas University's IPPBR delivered the same analysis to you last month. My point to you today is that our sales tax on original construction services is a "sore thumb." None of our surrounding states imposes a similar burden on this industry which has historically led us out of regional and national economic recessions.

I cannot provide hard numbers which prove that the tax has resulted in a specific statistic of lost jobs, more business emigrations, fewer construction permits, delayed business expansions, and higher consumer prices. I can confidently say that these results are inevitable to varying degrees and that the tax has **unquestionably** fed the perception of Kansas as having an unstable tax climate for business -- another of the tax policy red flags forewarned by the university economists.

Some argue that businesses are responsive to their bottom lines and that property tax relief has counterbalanced the negative effects of the new sales taxes which fund it. This premise is true, but the actual result has not been evenly experienced. By repealing sales tax exemptions you target specific sectors of taxpayers for tax increases. Since property tax relief has not been uniformly enjoyed, specific businesses which did not receive a significant property tax cut, and which are particularly hurt by the repeal of the exemption for construction services, have been net losers.

That's why KCCI advocated, and now still advocates, an increase in the state sales tax **rate** to replace the recently broadened sales tax **base**. An increase in the rate would be more evenly borne by all Kansas residents instead of the isolated sector which was most directly burdened by the tax on original construction services.

We believe that state legislation implementing this change is necessary and justified. I thank you again for this forum and stand available for any questions you may have.

**TESTIMONY BEFORE THE HOUSE
ASSESSMENT & TAXATION COMMITTEE**

regarding

REPEAL OF SALES TAX ON NEW CONSTRUCTION LABOR SERVICES

by Dan Morgan

Kansas City Chapter, Associated General Contractors

and

The Builders' Association

February 17, 1993

Thank you Mister Chairman and members of the committee. My name is Dan Morgan and I appear today in support of House Bill 2148 on behalf of the Kansas City Chapter, Associated General Contractors and the Builders' Association. Together, these associations represent nearly 750 general contractors, subcontractors and material or service suppliers engaged in commercial and industrial building construction throughout western Missouri and northeastern Kansas. Approximately 150 of our members are domiciled in Kansas and another 200 or so Missouri-based members perform work in Kansas in the metropolitan Kansas City area.

We welcome the opportunity to address the issue of sales tax on "labor services" in new construction which we very much oppose. As you know, the tax on new construction labor services was made a part of the school finance/property tax relief plan at the "eleventh hour" in last year's legislative session. We are convinced that most legislators simply did not understand the problems that would result from taxing a core industry like construction when they approved the substitute for House Bill 2892 last session. While placing a tax on new construction may have seemed an expedient way to help fund school finance and provide property tax relief to many parts of the state, we submit that doing so was both unfair to our industry and counterproductive to the economic development interests of the state.

There is no question that this tax on new construction labor services has placed the State of Kansas at a serious competitive disadvantage when competing against neighboring states for new business, business expansion and economic development. And nowhere in the state will the consequences be felt more keenly than in Johnson and Wyandotte Counties which must compete with Kansas City metro area counties in Missouri where corporate income taxes, individual income taxes, sales taxes and commercial, industrial and residential taxes are lower and where labor services are not taxed on either new or remodel construction.¹ These are very important considerations to owners or developers who are deciding whether to build an office building on College Boulevard, for example in Overland Park, Kansas or on Ward Parkway in Kansas City, Missouri.

2/17/93

House Taxation Cmte

¹Based on the 1992 Study of Business Taxes in Kansas and Nearby States by Institute for Public Policy and Business Research, Anthony L. Redwood, Executive Director.

Attachment 6

There is no question that, fueled by the Fed's monetary policy to lower interest rates, the single-family residential construction market did experience a boom in Johnson County and the metropolitan Kansas City area counties in Missouri in 1992. However, 1992 multi-family building starts were anemic in Johnson County and commercial building construction was extremely flat. Overall, the value of combined commercial/residential construction contracts recorded in the county was nearly 20% below the ten-year, inflation-adjusted average for the period.

Commercial building construction in the Kansas City area has declined by 45-50% from three or four years ago due to changes in federal tax laws, tight lending practices and a sluggish economy. The new construction labor services tax is an added deterrent to growth on the Kansas side of the metropolitan Kansas City area and to the state generally.

Many people believe that commercial building construction is not really impacted by this tax because of the new enterprise zone law in Kansas but that law basically pertains to manufacturing construction. Retail construction does not benefit from this act unless you are in a town with less than 2,500 population. Of course most large retail construction projects will likely be funded with IRB's, but the bulk of retail construction, i.e. that done for small and medium-sized businesses will be impacted by this tax on new construction labor services.

An example will demonstrate the impact of the new labor services tax on a new \$2,000,000 commercial project in Johnson County. First of all, please recognize that the term "labor services" includes much more than the actual labor performed on the job. Simply put, "labor services" include the cost of virtually everything in the total construction contract price, except for materials. Labor services on a commercial building project would typically amount to 60 percent of the total contract price and materials would be 40 percent. Under previous law, the sales tax on a \$2,000,000 project would have been \$52,000 (i.e. \$800,000 x 6.5%, i.e. combined 4.9% state and 1.6% local tax). With the new labor services tax there is now an additional \$49,200 tax burden on the same structure (i.e. \$1,200,000 x 4.1%, i.e. combined 2.5% state and 1.6% local tax) built in Kansas. It will now cost an owner or developer nearly \$50,000 more to build that building in Kansas rather than just across the state line in Missouri. That is a very serious disadvantage for Kansas.

Construction is an engine of economic growth. Construction activity has a direct economic impact on over forty related industries and an indirect impact on many more. With new buildings come new or expanded businesses, new employees and residents to the state and new homes in our communities. The resultant business and payroll dollars flow down through every sector of the economy. This generates more economic growth and that growth generates additional tax income for state and local government. Much of this is lost when business and industry are forced to locate elsewhere because of prohibitively high tax levels at home.

believe very strongly that it would be wrong to continue to impose a tax on labor services on new construction in Kansas rather than to use a more broad-based tax to help fund school finance. We feel the 1992 Kansas Legislature made a somewhat hasty and basically uninformed decision when it included a construction labor services tax in the funding formula for school finance and property tax relief in the closing days of the 1992 legislative session.

Left in place, this new tax will cost the state and its political subdivisions far more in lost revenues from lost economic development and associated sales, income and property taxes than it will produce for school finance and property tax relief. Common sense dictates that it must be repealed and another source of funding, if necessary, should be found. We ask your support for HB 2148 and thank you for this opportunity to be heard.

TESTIMONY OF LARRY S. KNOTT, ALLEN, GIBBS & HOULIK, WICHITA.

MR. CHAIRMAN, MEMBERS OF THE HOUSE TAX COMMITTEE, GOOD MORNING. MY NAME IS LARRY KNOTT. I AM A CERTIFIED PUBLIC ACCOUNTANT AND A TAX PARTNER FOR THE FIRM OF ALLEN, GIBBS & HOULIK IN WICHITA. I AM ALSO A MEMBER OF THE NATIONAL TAX AND FISCAL AFFAIRS COMMITTEE OF THE ASSOCIATED GENERAL CONTRACTORS ASSOCIATION AND I AM A MEMBER OF THE CONSTRUCTION FINANCIAL MANAGEMENT ASSOCIATION. AS A CPA, I PROVIDE TAX AND MANAGEMENT ADVICE TO A NUMBER OF CLIENTS IN THE CONSTRUCTION INDUSTRY IN SOUTH CENTRAL KANSAS. THESE CLIENTS RANGE FROM LARGE HIGHWAY CONTRACTORS EMPLOYING MORE THAN 100 PEOPLE TO SMALL HOME BUILDING CONTRACTORS EMPLOYING FEWER THAN 10 PEOPLE ON A YEAR-ROUND AVERAGE.

LAST YEAR, AS PART OF A COMPROMISE TO PAY FOR A NEW SCHOOL FINANCE PLAN, THE KANSAS LEGISLATURE ELECTED TO IMPOSE A 2.5 PERCENT SALES TAX ON SERVICES IN NEW CONSTRUCTION. NEARLY ALL THESE SERVICES IN NEW CONSTRUCTION RELATE TO LABOR COSTS. LEGISLATIVE BUDGET COMMITTEES ARE NOW OPERATING UNDER THE ASSUMPTION THAT THIS NEW CONSTRUCTION INDUSTRY TAX WILL GENERATE \$25 MILLION FOR THE STATE GENERAL FUND IN FISCAL 1994, AND THAT THIS SOURCE OF REVENUE WILL CONTINUE TO GROW IN THE FUTURE.

I AM HERE TODAY TO ASK YOU TO SUPPORT THE REPEAL OF THIS NEW, COSTLY TAX TO THE CONSTRUCTION INDUSTRY. HOUSE BILL 2148 DESERVES TO BE PASSED. THIS TAX PLACES OUR CONSTRUCTION INDUSTRY, PARTICULARLY OUR HOUSING CONSTRUCTION INDUSTRY, AT AN UNFAIR COMPETITIVE DISADVANTAGE. SECOND, THE TAX ADDS TO THE COST OF BUILDING A NEW HOME AND ADDS TO THE OVERALL INFLATION RATE OF NEW HOME CONSTRUCTION. THIRD, THE REVENUE ESTIMATES THAT HAVE BEEN GIVEN FOR THIS TAX ARE FUNDAMENTALLY FLAWED. LAST WEEK, I PARTICIPATED IN A PANEL CONVENED BY CHARLES WARREN, PRESIDENT OF KANSAS, INC., THAT CLOSELY STUDIED THE REVENUE ESTIMATES OF THIS TAX. THIS BIPARTISAN PANEL COULD IN NO WAY MATCH THOSE REVENUE ESTIMATES TO THE REALITY OF THE CONSTRUCTION INDUSTRY IN KANSAS. FOURTH, THIS TAX IS CONFUSING AND BORDERLINE UNCOLLECTIBLE. AND LAST, THIS TAX, IN THE OPINION OF MANY PEOPLE ASSOCIATED WITH THE CONSTRUCTION INDUSTRY IN KANSAS, IS NOT GOOD PUBLIC POLICY.

I WILL TRY TO BRIEFLY COVER MY MAIN POINTS. I WILL THEN BE MORE THAN HAPPY TO STAND FOR QUESTIONS.

DR. DARWIN DAICOFF OF THE UNIVERSITY OF KANSAS HAS PRESENTED TO THE SENATE TAX COMMITTEE A STUDY THAT HE SAYS SHOWS CONCLUSIVELY THAT HOUSING CONSTRUCTION IN KANSAS IS SUFFERING BECAUSE OF THIS NEW TAX. HIS STUDY SHOWS THAT IN THE FIRST FIVE MONTHS THE TAX WAS COLLECTED, KANSAS HAD ABOUT \$36 MILLION

LESS IN CONSTRUCTION CONTRACTS THAN WOULD HAVE BEEN GRANTED WITHOUT THE CONSTRUCTION INDUSTRY TAX. I UNDERSTAND THAT SOME MEMBERS OF THIS COMMITTEE HAVE QUESTIONED THE ACCURACY OF DR. DAICOFF'S STUDY. I AM NOT HERE TO DEFEND DR. DAICOFF'S STUDY, BUT I CAN TELL YOU THAT HIS STUDY IS CONSISTENT WITH WHAT WE HAVE FOUND WITH OUR CLIENTS. EVEN WHEN YOU CONSIDER THE RUSH TO SIGN CONSTRUCTION CONTRACTS BEFORE THE DATE THE TAX BECAME EFFECTIVE LAST JUNE 1ST, THE EVIDENCE IS PRETTY CONVINCING THAT THIS ADDITIONAL COST HAS BEEN SOMEWHAT DAMAGING FOR THE CONSTRUCTION INDUSTRY.

THERE IS NO DOUBT THAT LOWER INTEREST RATES HAVE A MUCH BIGGER IMPACT ON HOUSING THAN JUST ABOUT ANY OTHER FACTOR. BUT DON'T FORGET, THE ONLY REASON THAT INTEREST RATES ARE THIS LOW IS BECAUSE OF HOW POORLY THE NATIONAL ECONOMY HAS FARED OVER THE LAST TWO YEARS. IN KANSAS, WE HAVE BEEN LUCKY, BUT EVEN THAT LUCK COULD CHANGE. THERE ARE NO ASSURANCES THE HOUSING CONSTRUCTION INDUSTRY WILL REMAIN AT CURRENT LEVELS.

THE OTHER FACTOR TO THIS TAX IS THE COST FOR THE HOMEOWNER. THE FACT OF THE MATTER IS THAT THIS CONSTRUCTION INDUSTRY TAX CAN ADD ABOUT \$800 TO \$1,000 TO THE COST OF A TYPICAL \$90,000 HOUSE IN THE WICHITA MARKET. NOW SOME HAVE SUGGESTED THAT IF AN EXTRA \$1,000 MAKES A DIFFERENCE IN WHETHER A PERSON BUILDS A HOUSE, THEY PROBABLY DON'T NEED A HOUSE THAT COSTS \$90,000 OR

WHATEVER. HOWEVER, ANY OF US WHO HAVE BOUGHT AND SOLD HOMES IN OUR LIFETIME - AND I'M SURE THAT INCLUDES MANY OF YOU - KNOW FULL WELL THAT MANY A DEAL HAS FALLEN THROUGH OVER A DIFFERENCE OF AS LITTLE AS \$1,000.

HOWEVER, ONE OF THE MAJOR PROBLEMS WITH THIS NEW TAX IS THE REVENUE ESTIMATE ITSELF. WHEN YOU STARTED THE 1993 SESSION OF THE LEGISLATURE, YOU WERE TOLD TO EXPECT \$25 MILLION IN FISCAL 1994 FROM THIS REVENUE SOURCE. MANY PEOPLE HAVE SPENT TIME TRYING TO FIGURE HOW THIS REVENUE ESTIMATE WAS CALCULATED. IN A MEETING CONVENED AT KANSAS, INC. LAST WEEK, A PANEL OF ECONOMISTS, UTILITY COMPANY EXECUTIVES, CONSTRUCTION INDUSTRY REPRESENTATIVES AND A MERE CPA FROM WICHITA GATHERED TO DISCUSS THESE REVENUE ESTIMATES. IN OUR RESEARCH PRIOR TO THE MEETING AND IN SUBSEQUENT DISCUSSIONS, WE CALCULATED A MUCH LOWER REVENUE ESTIMATE FOR THE TAX - ABOUT \$9 MILLION, AND THAT IS IF YOU ARE LUCKY AND EVERYONE WHO SHOULD PAY THE TAX PAYS THE TAX. I HAVE ATTACHED A COPY OF MR. WARREN'S REPORT TO SENATE PRESIDENT BUD BURKE TO MY TESTIMONY.

I AM GOING TO HAVE TO TALK IN SOME BROAD ESTIMATES HERE BECAUSE THAT IS ABOUT ALL THAT IS AVAILABLE. FIRST, IF THE \$25 MILLION REVENUE ESTIMATE WERE CORRECT, OR EVEN CLOSE, THAT WOULD ASSUME A WILDLY SUCCESSFUL CONSTRUCTION INDUSTRY IN KANSAS OF ABOUT \$5 BILLION A YEAR. HERE'S HOW WE ARRIVE AT THAT

NUMBER: THE TAX IS FOR SERVICES IN NEW CONSTRUCTION. THAT EXEMPTS REMODELING AND REFURBISHING AND GOVERNMENT-EXEMPT CONTRACTS. ROUGHLY HALF THE CONSTRUCTION CONTRACTS ARE FOR REMODELING AND GOVERNMENT EXEMPT CONTRACTS, AT LEAST ACCORDING TO FIGURES THAT ARE TRACKED BY THE STATE AND VARIOUS ECONOMIC DATA GATHERING UNITS AT THE STATE'S UNIVERSITIES. THAT WOULD LEAVE \$2.5 BILLION FOR NEW CONSTRUCTION. BUILDING CONTRACTORS - AND EVEN STATE REVENUE ESTIMATORS - AGREE THAT CONSTRUCTION LABOR AND OTHER SERVICES ACCOUNT, ON AVERAGE, FOR ABOUT 40 PERCENT OF THE TYPICAL CONSTRUCTION CONTRACT. THAT WOULD LEAVE ABOUT \$1 BILLION FOR CONSTRUCTION LABOR AND SERVICES, AND 2.5 PERCENT OF THAT FIGURE IS \$25 MILLION. HOWEVER, THAT DOES NOT TAKE INTO ACCOUNT THE CONFUSION OF WHO SHOULD PAY THE TAX NOR OF CONSTRUCTION IN ENTERPRISE ZONES.

THAT'S THE BACKGROUND OF HOW WE THINK THAT THE \$25 MILLION ESTIMATE WAS CALCULATED. NOW LET ME TELL YOU THE REALITY OF CONSTRUCTION IN KANSAS. BASED ON BUILDING PERMITS AND CONSTRUCTION CONTRACTS, THERE IS NO WAY THAT WE HAVE A \$5 BILLION PLUS CONSTRUCTION INDUSTRY IN KANSAS. I WISH WE DID. THE REALITY IS THAT THE INDUSTRY MAY BE ABOUT HALF THAT AMOUNT. USING DATA FROM CERi, WICHITA STATE UNIVERSITY AND THE STATE OF KANSAS, OUR GROUP CALCULATED THAT AT THE OUTSIDE, THE VALUE OF NEW CONSTRUCTION IN KANSAS MAY BE \$1.3 BILLION A YEAR.

OF THAT, POTENTIALLY \$500 MILLION MAY BE SUBJECT TO THE NEW CONSTRUCTION INDUSTRY TAX. IN A PERFECT WORLD, YOU MIGHT BE ABLE TO ESTIMATE COLLECTIONS OF THAT TAX AT \$12.5 MILLION. THE MORE REAL FIGURE IS SOMEPLACE BETWEEN \$6 MILLION AND \$9 MILLION, AND MAYBE EVEN LESS.

WHILE ON THIS TOPIC, LET ME GIVE YOU ONE MORE EXAMPLE. IN 1991, ACCORDING TO THE KANSAS DEPARTMENT OF HUMAN RESOURCES, THE AVERAGE ANNUAL EMPLOYMENT IN THE KANSAS CONSTRUCTION INDUSTRY WAS 41,753 PEOPLE. THOSE WORKERS WERE PAID TOTAL WAGES OF \$947,702,118, UP SLIGHTLY FROM 1990. THOSE WAGES ARE WHERE YOU WILL GET THE VAST MAJORITY OF THIS NEW TAX. IF 40 PERCENT OF THOSE WAGES ARE PAID FOR NEW CONSTRUCTION PROJECTS AND IF THE TAX WAS COLLECTED FOR ALL THOSE PROJECTS, YOU'RE LOOKING AT ABOUT \$9 MILLION. AGAIN, THAT IGNORES EXEMPT PROJECTS AND SLIPPAGE FROM PEOPLE TRYING TO AVOID COLLECTION.

FINALLY, THIS TAX IS ALMOST UNENFORCEABLE. ACCORDING TO THE DEPARTMENT OF REVENUE, ONLY \$1.5 MILLION WAS COLLECTED IN THE FIRST SIX MONTHS UNDER THE LAW. AGAIN, SOME OF THAT LOW NUMBER MAY BE BECAUSE OF THE CONTRACTS THAT WERE SIGNED BEFORE THE LAW TOOK EFFECT, BUT OUR GROUP AT KANSAS INC. AND CONTRACTORS IN THE INDUSTRY BELIEVE THE REASONS ARE MUCH DEEPER. THERE IS CONSIDERABLE CONFUSION OUT THERE ABOUT THE TAX. IT IS CONFUSING. IT IS UNCLEAR WHO SHOULD BE PAYING THE TAX

AND WHAT IT IS THAT'S ACTUALLY SUBJECT TO THE TAX. FOR INSTANCE, SOME LAW FIRMS IN THE KANSAS CITY AREA HAVE TOLD THEIR CLIENTS THAT THIS TAX DOES NOT APPLY TO OUT-OF-STATE SUBCONTRACTORS. MEMBERS OF THIS COMMITTEE MAY ARGUE THAT EXEMPTING OUT-OF-STATE CONTRACTORS WAS NOT YOUR INTENT. PERHAPS YOU ARE RIGHT, BUT CLEARLY, IT WILL TAKE A COURT TO DECIDE THE ISSUE. MOREOVER, YOU DO NOT HAVE A MECHANISM IN PLACE TO ENFORCE COLLECTION OF THIS TAX. IT IS CONFUSING AND IT IS TOO EASY TO AVOID PAYING THE TAX. THAT MEANS THE PEOPLE WHO ARE TRYING TO FOLLOW THE RULES - AND THERE ARE A NUMBER OF CONTRACTORS WHO ARE TRYING TO FOLLOW THE RULES - ARE AT AN UNFAIR COMPETITIVE DISADVANTAGE.

THERE ARE ALSO MAJOR PROBLEMS IN IMPLEMENTING THE TAX ON THE PART OF THE CONTRACTORS. MOST CONSTRUCTION CONTRACTORS ARE SMALL OPERATIONS. THEY OPERATE WITH THIN PROFIT MARGINS - LESS THAN 5 PERCENT ON AVERAGE. WHEN YOU ADD THE INCREASED COST OF MATERIALS THIS PAST YEAR - AND THAT COST HAS BEEN CONSIDERABLE - THIS NEW TAX AND THE ADMINISTRATIVE COST OF FIGURING OUT HOW TO COLLECT THE TAX, IT BECOMES QUITE A BURDEN. NOW I AM NOT GOING TO STAND HERE AND PAINT AN ALARMIST PICTURE AND TELL YOU THAT YOU ARE DRIVING CONTRACTORS OUT OF BUSINESS.

BUT I WILL TELL YOU THAT THIS IS JUST ANOTHER MEASURE THAT DRIVES DOWN ALREADY THIN PROFIT MARGINS, THEREBY LIMITING

FUTURE REINVESTMENT IN THE BUSINESS. I REALIZE THAT THE STATE IS IN A SEVERE CRUNCH FOR MONEY OVER THE NEXT FEW YEARS, AND I KNOW THAT MANY SOURCES WILL BE TAPPED FOR REVENUE; SO DO THE PEOPLE I SERVE IN THE CONSTRUCTION INDUSTRY. NO ONE EXPECTS A FREE LUNCH. BUT I ALSO BELIEVE THAT THIS CONSTRUCTION TAX IS NOT THE BEST POLICY, AND I BELIEVE THAT IT IS UNWORKABLE. I URGE YOU TO PASS HOUSE BILL 2148. OVER THE LONG-TERM, HELPING BUILD A STRONG CONSTRUCTION INDUSTRY WILL HELP THE STATE'S ECONOMY, AND TAX COLLECTIONS, FAR MORE THAN THE 2.5 PERCENT TAX ON SERVICES IN NEW CONSTRUCTION. THANK YOU. I WILL BE HAPPY TO ANSWER ANY QUESTIONS.

KANSAS inc.

February 9, 1993

Senator Paul Burke
President of the Senate
The Kansas Legislature
The Statehouse
Topeka, Kansas

Board of Directors

GOVERNOR JOAN FINNEY
THOMAS CLEVINGER
Co-Chairmen

PAUL "BUD" BURKE
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JACK WEMPE
BILL WOHLFORD

Charles R. Warren
President

632 S.W. Van Buren, Suite 100
Topeka, Kansas 66603
(913) 296-1460
fax - (913) 296-1463

Dear Senator Burke:

At your request, Kansas Inc. convened a meeting of informed and expert individuals to analyze the potential fiscal impact of Senate Bill 240 now pending before the Senate Assessments and Taxation Committee. The three legislative measures considered are: restoring the exemption of utilities consumed in production, property tax credit for the severance tax on natural gas, and restoring the exemption on services used in original construction. The meeting took place on Monday, February 8.

The following individuals participated:

Dr. David Collins, Kansas Geological Survey,
Lawrence.
Dr. Darwin Daicoff, University of Kansas,
Lawrence.
Doug Davidson, CERI, Johnson County.
Shannon Green, Tax Attorney, Kansas City Power
and Light, Kansas City, Missouri.
Pat Hurley, Pete McGill and Associates, Topeka.
Larry Knott and Forrest Gossett, Allen, Gibbs
and Houlik, Certified Public Accountants and
Consultants, Wichita.
Ed Schaub, Western Resources, Inc., Topeka.
Janet Stubbs, Kansas Home Builders Association,
Topeka.
Jeff Waggaman, Administrative Assistant to the
Senate President, Topeka.
Dr. Charles Warren, President, Kansas Inc.

Background

The 1993 Kansas Legislature enacted a 2.5% sales tax on utilities used in production and on services used original construction. The Interim Committee on Taxation recommended a reduction in the severance tax on natural gas from 7 percent to 4.33 percent on a phased-in basis and

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recommended the repeal of the sales tax on utilities used in production.

Estimated Fiscal Impacts

The participants reviewed the fiscal impacts that had been prepared and based on data provided and review and discussion of experience with the taxes, fiscal estimates were derived. The fiscal notes prepared by Legislative Research and the Administration are listed below in column A and the conclusions reached in our meeting are in Column B. The assumptions and conclusions reached at the meeting yesterday are provided in some detail below.

	A Current Fiscal Note (dollar amounts in millions)	B Kansas Inc. Estimates
Utilities Tax	\$17.0	\$13.0
Construction Services Tax	25.0	9.0
Natural Gas Severance Tax	7.0	8.0
Totals	\$49.0	\$30.0

The Kansas Inc. participants concluded that the current fiscal notes over-estimate revenues from these three tax sources combined by 19 million dollars.

The assumptions and conclusions reached individually on each of the three tax measures are presented in the attached summary of the discussion.

Sincerely,

Charles R. Warren
President

attachments

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SUMMARY OF DISCUSSION
KANSAS INC. MEETING ON FISCAL IMPACTS OF S.B. 240

Revenue Experience:

The participants noted that in a letter from Secretary of Revenue Nancy Parrish to James R. Cobler, Division of Accounts and Reports, the revenues collected on the new 2.5% taxes were certified as follows for the period July to December 1992:

2.5% tax on services on new construction	\$1,471,000
2.5% tax on "utilities consumed in production"	\$6,561,000

In FY 1992, the severance tax collections on natural gas were:

	\$55,477,000
less receipts previous year's liability:	- 1,400,000
FY1992 total:	\$54,077,000

Severance Tax Fiscal Impact

Legislative Research provided the following fiscal note estimates:

	Interim Note	January 26 Note
FY1994	\$ 7,527,000	\$ 7,000,000
FY1995	16,560,000	15,400,000
FY1996	23,109,000	21,500,000
FY1997	24,117,000	22,400,000

The estimates in the fiscal note regarding price per MCF and production levels were derived from the November revenue estimates. According to The Governor's Budget Report, Volume 1, p. 12: "Kansas natural gas production and price will remain stable during the forecast period. The price is expected to average \$1.60 per MCF in FY 1993 and \$1.55 per MCF in FY 1994. This estimate compares to an average price of \$1.33 for FY 1992."

These revenue estimates are believed to assume a constant production level for fiscal years 1994 through 1997 of 630 BCF (billion cubic feet) annually with a gross value of \$903 million dollars per year and an average price of \$155 per MCF. These production and price levels would yield annual revenues of \$63 million at a 7 percent rate and \$57 million at a 6 percent rate in FY94, thus the \$7 million fiscal note the first rate. The tax rate reaches 4.33 percent by FY1997.

Because of the national outlook for natural gas and the likely increased production, along with actions underway by the Kansas Corporation Commission to increase allowables and thus production

in the Hugoton field, an estimate of 650 BCF was viewed as a more likely and conservative production level. Because of the trend toward rising gas prices, a \$1.60 per MCF figure was viewed as most likely. This production would yield a gross value of \$1,040 billion with .925 of that gross value taxable yielding \$962 million subject to the 7 percent rate. This results in natural gas severance tax revenues, holding each year constant, of \$67.34 million. A one percent revenue "loss" of \$9.62 million is reduced due to timing of collections, therefore 10/12 of that amount, or \$8.02 million would be the FY1994 fiscal note.

It should be noted that an independent estimate of the trend and projections for natural gas prices was obtained from a petroleum firm in Wichita that indicated the range in price for FY93 was \$1.55 to \$1.65 per MCF and that the most probable price per MCF in FY94 was an average of \$1.70. This industry observer noted that natural gas is not sold on an MCF but rather on a BTU (British Thermal Unit) basis. Kansas gas has a higher BTU and the average price of \$1.70 for 94 should be adjusted by a factor of 1.050 yielding an average price of \$1.79 per MCF. The assumption that natural gas prices would decline from FY93 to FY94 is considered highly unlikely given the trends and prospects for natural gas. The \$1.60 per MCF price used in the Kansas Inc. estimate is therefore overly conservative.

Sales Tax on Utilities Consumed in Production:

As noted earlier, actual revenues realized from the 2.5% sales tax on utilities consumed in production was \$6,561,000 for the period from July to December 1992. Western Resources, Inc. provided extensive detail on the sales taxes collected on utilities in their service area on a county-by-county basis. See attachment. Western Resources, Inc. shows actual state sales tax collections for the June to December 1992 period of \$3,082,942.66. On an annualized basis, they calculated the sales tax collections to be \$5,944,519.00. Kansas City Power and Light estimates sales tax on utilities consumed in their service area to be approximately \$750,000.00. The revenues from these two major utilities would then approximate \$6.75 million annually. Other major utilities in Kansas are BPU in Wyandotte County, Sunflower, Midwest Energy and the municipal utilities. The other major consumers affected would be the Kansas oil and gas industry. The consensus of the participants was that these other utilities could produce sales tax collections of an additional \$6.25 million. It should be noted that the major industrial users in Kansas lie within the Western Resources and KPL service areas. There is not considered to be any seasonal or cyclical factor that would require adjustments in estimates derived from the actual experience data.

Based on this actual data and estimates of the participants, the 2.5% sales tax on utilities can be anticipated to yield state revenues of \$13 million annually. \$13 million is an annualized

amount based on current, actual collections. The participants do not believe a revenue estimate of \$17 million is probable.

Tax on Services for Original Construction:

As previously noted, the sales tax on services for original construction has yielded \$1.471 million through December 1992.

To arrive at a fiscal estimate for construction sales tax, it is first necessary to estimate the total value of taxable original construction in Kansas in Fiscal Year 1994. CERI developed a total taxable value of \$1,851,000,000 based on data from F.W. Dodge, Value of Construction Contracts, for calendar year 1992. This number is arrived at by assuming that 25 percent of the value of commercial and residential construction is rehabilitation and thus already subject to sales taxation. And, that 25 percent of the non-building construction contracts were for government and not subject to taxation. Dr. Daicoff noted that the U.S. Department of Commerce data shows a total value of taxable original construction of \$1.3 billion. The group agreed on a total for original construction value of \$1.3 billion after considerable discussion. This amount was based on Dr. Daicoff's conclusions (See attached testimony by Dr. Daicoff before the Kansas Senate Assessment and Taxation Committee of February 2, 1993). Dr. Daicoff estimates a 5.3 percent monthly loss of taxable construction due to the imposition of the 2.5% sales tax.

After more discussion, the participants estimated that 40 percent of the value of taxable original construction would be allocated to labor and services. ($\$1.3 \text{ billion} \times .40 = \$520,000,000$ of labor subject to taxation.) From this amount, \$20 million was subtracted because of enterprise zone exemptions of sales tax on original construction. Thus, the total value of labor and services on original construction that represents the maximum potential subject to taxation is considered to be \$500,000,000. A 2.5 percent tax on this amount would yield \$12.5 million.

In attempt to understand why only about \$1.5 million was collected during through December 1992, several assumptions were explored. It was recognized that many contracts were exempted because they were executed prior to the effective date, and that a rush of contract execution took place. The participants also noted that several factors have mitigated against greater collections, including: confusion over the application of the tax, difficulty on the part of contractors, especially smaller businesses, in administering the tax, ability of out-of-state contractors to avoid the tax, and direct evasion of the tax. The participants also noted that the Department of Revenue apparently has only six persons to enforce sales tax collections, all of whom were engaged fully prior to the enactment of this tax.

If the potential amount subject to the 2.5 percent sales tax

is \$500 million, then given the above cited difficulties in collection and enforcement, it is assumed that a "slippage" rate of 28 percent would not be unreasonable, and this would produce a total taxable value of \$360 million. It should be noted that one participant felt the "slippage" rate should be significantly higher and at least be estimated at 40 percent. A 28 percent slippage would yield taxable value of \$360 million and that, in turn, would produce estimated annual revenues of \$9 million. This amount was agreed upon by the participants as a reasonable approximation of expected revenues in FY 1994 for the sales tax on services on original construction.

Other Group Conclusions

The participants noted that there are extremely serious problems in the administration and collection of the sales tax on original construction. The Department of Revenue lacks adequate staff to enforce and administer this tax, and the costs to fully staff for its collection would be prohibitive. They also note that the construction industry and its subcontractors are extremely resentful of this new tax and can resort to very creative methods of avoidance. It was also noted that the sales tax is harmful to jobs and activity in the construction industry which will reduce the potential yield of the tax. It is estimated that approximately 1,800 jobs will be lost because of the tax and that employment loss will in turn result in additional losses to the state general fund from reduced sales and personal income tax collections. (An estimate of that loss in income tax alone is: 200 jobs X annual wages of \$22,500 = \$40.5 million payroll loss; and, an income tax loss of \$1.6 million annually.)

It was also noted that the tax on utilities consumed will have a negative impact on economic development in Kansas causing further reductions in state general fund revenues.

If the participants' estimates on the 2.5% sales tax are approximately correct, these two taxes would yield \$22 million. An increase in the general state sales tax rate from 4.9 percent to 5.0 percent would yield \$24 million, or \$2 million more with none of the attendant negative implications for economic development, difficulties in collection or enforcement, and related losses in state sales or income taxes due to reduced employment and economic activity.

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MEMORANDUM

OF COUNSEL

DANIEL B. BAILEY

TO: MEMBERS OF HOUSE TAXATION COMMITTEE

FROM: ALAN F. ALDERSON, ATTORNEY, HOME BUILDERS
ASSOCIATION OF GREATER KANSAS CITY

RE: SALES TAX ON ORIGINAL CONSTRUCTION; HOUSE BILL
NO. 2148

DATE: FEBRUARY 17, 1993

I appear today on behalf of the Home Builders Association of Greater Kansas City to urge you to restore the sales tax exemption of original construction labor services that existed prior to the 1992 legislative session.

I have been working with the Home Builders Association of Greater Kansas City since immediately after the passage of 1992 House Bill No. 2892 and have participated in a number of meetings in which contractors and representatives of the Kansas Department of Revenue have been present. My involvement with the original construction exemption, however, dates back to 1978 when I first went to work for the Kansas Department of Revenue as a sales tax attorney -- shortly after the legislature had restored the provisions of the labor services subsection of the Kansas sales tax law after it had been stricken down by the Supreme Court as unconstitutionally vague. In addition, I have discussed this topic in seminars I have presented two or three times a year for the last 5 or 6 years for the National Business Institute.

I am of the opinion that the imposition of sales tax on original construction labor services has created more difficulties for contractors than the amount of revenue being collected could ever possibly justify. I have been attempting to obtain a series of private letter rulings from the Director of Taxation which would clarify the Department of Revenue's position on a number of the troublesome issues and, while the Department's position has become clearer in a number of these areas, the interpretation of the newly-enacted subsection continues to create uncertainty and unequal treatment for Kansas contractors and subcontractors. A number of the difficulties created or exacerbated by the imposition of the 2 1/2% tax on original construction labor services are as follows:

1. By interpretation of the Department of Revenue, professional services, such as real estate commissions, so-

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called professional fees and land costs are not considered to be included within the taxable service base. However, upon inquiry, it has been determined that builder's fees are not considered to be within the ambit of "professional fees".

Neither profit nor overhead are excluded from the sales tax base and, while I do not quibble with this interpretation, the Director of Taxation has ruled that items such as building permits and sewer hook-up fees are includable in the sales tax base. I find it very hard to distinguish between other non-service items, such as real estate commissions and professional fees and those items that the Director of Taxation considers to be part of the base.

Also troubling is the attempted distinction between excludable and includable professional fees. The Director contends that architecture, engineering or surveying performed by a contractor who also performs taxable services are not excludable from the tax base. Would these services be excludable if performed through a separate corporation?

2. Although I would not argue with the Director's interpretation of the law in this regard, the contractor also must be aware that travel expenses, per diem expenses, the purchase, lease or rental of machinery and equipment, consumable supplies such as form lumber, sandpaper, tools and other equipment are considered to be a part of the tax base. All in all, trying to make sense out of the elements that are required by the Department of Revenue to be included in the base for sales tax purposes is unbelievably confusing for contractors.

3. To further compound the problem, there are certain of the elements of a sales tax base that can be excluded by contractor who segregates the payment of certain fees and expenses and makes those acquisitions or pays those expenses through a separate corporation in which there are no employees performing actual labor services. Obviously, only the larger construction companies can afford to create these separate corporations for the purpose of shielding non-labor items from the tax base. The savings that can be obtained through the creation and operation of these separate corporations makes it worthwhile for the larger contractors, however. This works a discrimination against the small contractors subcontractors who cannot afford to operate under multiple corporate shells. The Department of Revenue has ruled that sewer hook-up fees, building permits and the like can be acquired through these corporations without sales tax. Professional services, whatever those include, could also probably be dropped into a separate corporation for exclusion purposes.

4. The larger contractors are also in a position to build spec homes they own themselves to shield original construction from sales tax. Sales tax would only apply to services performed for sale at retail and, just as if you set out to build your own home, a contractor can do the same thing if he structures his financing properly. Obviously, not all contractors are in a position to take advantage of this type of arrangement.

5. The Department of Revenue has agreed that the Bernie's Excavation case applies to allow bifurcation of certain types of contracts. In Bernie's, the Kansas Court of Appeals upheld a Board of Tax Appeals decision in which an excavation was allowed to segregate his billings between taxable and non-taxable services. The Court -- correctly, I believe -- held that an excavation contractor is actually performing two services, under certain circumstances: (1) The non-taxable service of digging a ditch, for example, and (2) the taxable "installation" of pipe. The Court said that, as long as the Contractor properly segregates his billing for the two services, the performing of the non-taxable service does not have to be included in the taxable portion of the service base.

While the enactment of the tax on original construction labor services does not affect the Court's decision in Bernie's, the Department of Revenue is unwilling to extend the ruling in Bernie's beyond its' application to excavation contractors. There are other situations in which it is clear that a contractor may be performing services which could be segregated into taxable and non-taxable components. One example is the clean-up and detail work done at the completion of a construction project. A crew may be sent to the building to do clean-up, which would normally be considered to be a non-taxable service, but this crew may also be required to install switch plates, light fixtures, and other detailing items.

The Department has ruled that the performance of any of these minor taxable installation services renders the entire clean-up and detailing job taxable. The Department has not, as yet, extended the logic of Bernie's to the bifurcation of these types of contracts. I see no reason why those contractors who can afford to have multiple corporations couldn't have the nontaxable clean-up work performed by a corporation other than the one that is performing taxable labor services in order to avoid the Department of Revenue's refusal to extend the application of Bernie's to services other than excavation.

6. The situation that has occurred in Johnson County is of particular concern to subcontractors because, under the new law, a Kansas contractor can hire a Missouri subcontractor at

a savings. This is true because there is no local use tax in Kansas. Therefore, a Missouri subcontractor can undercut the bid of a Kansas subcontractor under identical job specifications because the Kansas subcontractor would have to bid the job with local sales tax.

While Attorney General Stephan has rendered an opinion to the effect that local units can charter out of the original construction labor services tax base, the Kansas Department of Revenue has now indicated that it will not honor the action taken by a number of cities in Johnson County and will collect local sales tax from contractors who perform labor services in those cities.

I attended a meeting last May or June in Overland Park in which I overheard a contractor indicating to another that he would definitely begin hiring Missouri subcontractors because the savings of 2% off the top on a job of any magnitude would make it worth his while. This has created a discriminatory situation under which our own subcontractors will be the losers.

7. Although this last situation I will describe was not created by the enactment of the original construction labor services tax, I mention it because it has recently become apparent that the application of this interpretation causes greater confusion now that there is a taxable portion of original construction labor services. This situation is that a development contractor cannot collect and remit tax at the lower rate on any of the service items which cannot be specifically attributable to a specific "building or facility". Therefore, street lighting, paving, laying sewer mains and water mains and other similar service items are considered taxable at the full 4.9% state rate because they are not considered to be "in connection with" the construction of a specific building or facility.

This is a rather stringent interpretation by the Department of Revenue and one which, like all of the other problems created by the imposition of the new tax on the previously exempt services creates substantial confusion and uncertainty for contractors. Where is the line between sewer pipe and water line that is to benefit the development in general and that which is to benefit a particular dwelling? Can any street lighting be tied to a particular residence?

These are only some of the problems that are now being encountered by contractors. It is my understanding that the tax collection under this newly imposed tax has been very minimal. On behalf of the Home Builders of Kansas, I would urge you to support the passage of House Bill No. 2148.

THE KANSAS CONTRACTORS ASSOCIATION, INC.



1923 - 1993

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TESTIMONY

BY THE KANSAS CONTRACTORS ASSOCIATION
BEFORE THE HOUSE ASSESSMENT AND TAXATION COMMITTEE
REGARDING
SALES TAX ON ORIGINAL CONSTRUCTION

Mr. Chairman and members of the House Assessment and Taxation Committee, I want to thank you for allowing me the opportunity to appear before you this morning to discuss the sales tax on original construction.

My name is Don Popejoy. I am President of Popejoy Construction Company in Ulysses. We are an asphalt paving contractor in southwest Kansas. I am also President of the Kansas Contractors Association. Our association represents more than 330 heavy, highway, and municipal utility contractor and supplier member firms in the Kansas construction industry.

I am here today to ask that you remove the 2 and a half percent sales tax on the labor involved in the construction of roads and highways around the state. This tax was imposed last year as part of the School Finance Bill and raises approximately 2 and a half million dollars in revenue for Kansas. 2/17/93

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Attachment 9*

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Our association believes this tax was inadvertently added to the school finance measure and we do not believe the intent of the Legislature was to have it affect the highway industry. It has caused a tremendous inconvenience to our highway contractors due to its interpretation.

For one thing, when the tax was implemented, the revenue department had a difficult time in explaining which items were taxable and which were not. It was not until sometime in August that our contractors got the right information for their operations.

Secondly, besides the additional paperwork for our contractors, it has also caused a lot of additional work for the revenue department which has also had to determine what tax has to be collected, on what projects, what materials, and whether it should be collected at all. As you may realize, sales tax on materials is at 4.9%, there is no tax on excavating dirt, and this tax is at 2.5%....unless the project is tax exempt.

In addition, this tax basically only affects the sub-contractors of our industry. Prime contractors, who work for the state are not charged the tax since they are doing work for the state .. and the state cannot impose a tax on itself. As a result, sub-contractors on projects do charge a sales tax for the work they do for the prime contractor. What that means to you and me is our highway projects cost the state a little more money because of this tax.

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For example, when a prime bids on a job, he includes the costs incurred by his sub-contractors. Sub-contractors now must submit bids including the sales tax on labor. As you can see, when the state pays for a highway job, instead of just paying for the project it is also now paying for the sales tax on labor. That means money that was designated to build roads is now being diverted to pay taxes which then goes into the school finance funding process.

As I mentioned, we believe it was not the intent of the Legislature last year to include the highway industry in the taxing process. When the matter was discussed both in conference committee and on the Senate floor, the question was asked whether the highway program would be affected, and in both cases, it was said it would not be affected. But after the measure was passed, it was determined the highway industry would be taxed.

For those reasons, I ask that you remove the sales tax on labor regarding the construction of roads and highways.

I appreciate your time today and I will be glad to try and answer any of your questions.

1/27/93

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THE KANSAS CONTRACTORS ASSOCIATION, INC.



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SALES TAX ON ORIGINAL CONSTRUCTION OF HIGHWAYS

The Kansas Contractors Association is opposed to the 2.5% sales tax on labor used in the construction of the state's roads, bridges and highways. The 2.5% sales tax, which creates about two and a half million dollars in tax revenues, is a tax on the state itself. In addition, it creates a bifurcated system when compared to the 4.9% tax levied on materials used in highway construction.

The KCA believes it adds more work to our contractor's accountants and the state's auditors. Moreover, it only affects the subcontractors involved in highway construction and not the prime contractors who contract with the state. It creates a defacto discriminatory environment against subcontractors by giving an advantage to prime contractors by not levying the tax on their projects.

The KCA recommends the sales tax be eliminated on new construction when it comes to the construction of highways and bridges. Further, we suggest that other forms of taxation be substituted to make up any difference this measure's elimination would cause.

By eliminating the tax, the KCA believes it would also eliminate the need for additional state employees to administer this program. It also would eliminate the public's view that money actually allocated for highway construction was being diverted to support the financing of our public schools.

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**TESTIMONY BEFORE THE HOUSE
TAXATION COMMITTEE**

**ARGUMENTS FOR THE REPEAL OF THE
SALES TAX ON CONSTRUCTION SERVICES**

**BY GUS RAU MEYER
RAU CONSTRUCTION COMPANY
FEBRUARY 17, 1993**

My name is Gus Rau Meyer and I am Vice President of Rau Construction Company. Rau Construction Company is a middle to large volume construction company, founded in 1870, and doing business in the Kansas City Metropolitan area since the early 1900's. Our headquarters for over 35 years has been in Overland Park, being a pioneer during the growth in this area. Our main focus is in the construction of new commercial and industrial projects on a negotiated or design/build bases. This work is done almost without exception in the private sector.

Over the past 5 years, our average annual billings have been approximately \$18,500,000. During that period of time, our work volume was historically 1/3 in Kansas and 2/3 in Missouri. The majority of this work was new construction. Since the implementation of the Sales Tax On Construction Services last May, we have not contracted for any new construction in Kansas, but have been awarded or have contracted for over \$10,000,000 in new construction in Missouri. The projects which we are negotiating and anticipate Contracting for in the first half of 1993 total an additional \$15,000,000 in Missouri and only \$750,000 in Kansas. These actual and anticipated awards mentioned above amount to over \$25,000,000 worth of new construction in Missouri and only one project worth \$750,000 of new construction in Kansas. This projects our Kansas contracts for the 12 month period after the implementation of the Tax on Construction Services to be less than 4% of our total Contracts, verses our historical average for Kansas of 32% over the last 5 years. The Sales Tax on Construction Services has not necessarily effected our total volume of work, but I feel that it has had an effect on what State our work is located in. Kansas has been the loser.

I am submitting with this testimony a projection of what the effect of the Sales Tax on Construction Services has on a hypothetical \$2,000,000, 30,000 square foot, new construction project. Examples of a project of this size would be a medium size "strip" shopping center or a small to average size 2 story office building. This project would be about 1/2 the size of the typical area grocery store or 1/6 the size of the latest K-Mart or Wal-Mart Super Stores. This "hypothetical" project could be found in any area of the State. The labor provided by all Contractors on this job amounts to 39.31% of the "hard" construction cost or \$786,227. The Subcontractor and General Contractor Overhead and Profit amount to \$414,918 of the hypothetical project. The additional amount of costs (costs in addition to those previously under the Tax on Materials) subject to the new Sales Tax on Construction Services is \$1,201,145, or over 60% of this \$2,000,000 project. The 4.1% Tax generates additional tax receipts of \$49,247 or

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*House Taxation Cmte
Attachment 10*

TESTIMONY BEFORE THE HOUSE TAXATION COMMITTEE
ARGUMENTS FOR THE REPEAL OF THE SALES TAX ON CONSTRUCTION SERVICES
BY GUS RAU MEYER
FEBRUARY 17, 1993
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2.46% of the cost of the project over the previously enacted Sales Tax. Based on 30,000 gross square feet, this equates to an additional \$1.64 per square foot of construction cost. Using a factor of; 90% rentable square footage, 10% financing and 20 year amortization, this would cause a \$0.21 per square foot per year increase in rents to cover this cost. This is a tremendous burden in any real estate market, let alone a depressed real estate market, be it a commercial, retail, or industrial application.

This Tax not only effects developers which have to contend with the costs of this Tax on rental rates, but it also affects the decisions of owner/users. We have been working with a repeat client for over 2 years on a 300,000 square foot office structure for his own use in Overland Park. The client has spent considerable monies to bring his construction plans to a 98% complete condition. The project was put on hold about 1 year ago. Although the client continues to expand his workforce in the Kansas City Metropolitan area, this project appears to be canceled with one of the stated reasons being this Sales Tax on Construction Services.

Although I am not an economist or an actuary, my own analysis of the shift we have seen in the location of where the projects we are constructing (from historically 32% in Kansas to now only 4% in Kansas), combined with the analysis of the impact of this Tax on a hypothetical \$2,000,000 project, makes me believe that the Taxes (Sales Tax on Materials, Property, Income, etc) and other revenues being lost by the shifting of projects to outside of Kansas far outweigh the gains realized by the Sales Tax on Construction Services.

In conclusion, from a strictly "volume of work" and profit standpoint, the Sales Tax on Construction Services does not effect my company. The volume of work we have lost in Kansas, we have made up in Missouri. As a life long resident of Kansas, and a backer of it's high quality of life and standard of living, I feel this Tax is a disaster to economic development in the State. It is hurting the people who do not have a choice as to where to build their business by significantly increasing their cost. It is also, and more importantly, driving the people who do have a choice away from Kansas. This is a near sighted Tax that demands a dollar up front today in lieu of many dollars in Sales Tax, Property Tax, Income Tax, and other revenues in the future. The repeal of this Tax may not bring back the businesses that have left Kansas, but will help retain the ones we have and attract more to come.

I thank you Mister Chairman and members of this committee for allowing me to appear before you today. I appreciate your consideration and ask for your support in repealing this Tax. If you have any questions, I would be glad to address them.

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FEBRUARY 17, 1993
 TESTIMONY BEFORE THE HOUSE TAXATION COMMITTEE
 BY GUS RAU MEYER

TYPICAL CONSTRUCTION COST
 \$2,000,000.00 BUILDING

	ESTIMATED SHELL CONST.	ESTIMATED INTERIOR CONST.	TOTAL COST	% LABOR	ESTIMATED LABOR PORTION
GENERAL CONDITIONS	23,952	15,000	38,952	85.00%	33,109
EXCAVATION	15,216		15,216	30.00%	4,565
ASPHALT	181,100		181,100	25.00%	45,275
REINFORCING STEEL	25,177		25,177	42.00%	10,574
FOUNDATIONS	44,585		44,585	65.00%	28,980
FLAT CONCRETE	158,740		158,740	42.00%	66,671
MASONRY	176,447		176,447	55.00%	97,046
STRUCTURAL STEEL	155,267		155,267	44.00%	68,317
CARPENTRY	25,845	65,212	91,057	50.00%	45,529
MILLWORK	4,406	15,915	20,321	7.00%	1,422
FLAT ROOFING	78,690		78,690	27.00%	21,246
SHEETMETAL	33,509		33,509	30.00%	10,053
CAULKING	3,420		3,420	60.00%	2,052
HOLLOWMETAL	7,010	11,645	18,655	50.00%	9,328
GLASS & GLAZEING	32,981		32,981	33.33%	10,993
HARDWARE	4,418	7,763	12,181	10.00%	1,218
DRYWALL	128,588	85,397	213,985	35.00%	74,895
ACOUSTICAL CEILING	18,173	17,856	36,029	50.00%	18,015
FLOORING	2,397	58,226	60,623	25.00%	15,156
CERAMIC TILE	2,532		2,532	33.00%	836
PAINT & WALL COVERINGS	4,874	59,747	64,621	75.00%	48,466
TOILET ROOM ACC.	4,389		4,389	20.00%	878
PLUMBING	45,548	7,763	53,311	45.00%	23,990
FIRE SPRINKLERS	17,188	6,599	23,787	62.50%	14,867
H.V.A.C.	85,627	15,527	101,154	45.00%	45,519
ELECTRICAL	167,611	50,462	218,073	40.00%	87,229

Sub Total	1,447,690	417,112	1,864,802	39.31%	\$786,227
G/C OH&P (7.25%)	104,958	30,241	135,198		=====

BUILDING TOTAL	\$1,552,648	\$447,353	\$2,000,000		=====
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NEWLY TAXABLE AMOUNTS

LABOR	\$786,227	
SUB OH&P	\$279,720	15% X \$1,864,802
G/C OH&P	\$135,198	

TOTAL	\$1,201,145	=====
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LBR SRVCS TAX (4.1%)	\$49,247	
% OF PROJECT	2.46%	
COST/SF (30,000 SF)	\$1.45	
AMORTIZED COST/SF/YR	\$0.19	90% RENTABLE, 10% INTEREST 20 YEAR AMORTIZATION

10-3



Executive Offices:
3644 S. W. Burlingame Road
Topeka, Kansas 66611
Telephone 913/267-3610

TO: THE HOUSE TAXATION COMMITTEE
FROM: KAREN FRANCE, DIRECTOR, GOVERNMENTAL AFFAIRS
DATE: FEBRUARY 17, 1993
SUBJECT: HB 2148 SALES TAX ON NEW CONSTRUCTION

Thank you for the opportunity to testify. On the behalf of the Kansas Association of REALTORS® I appear today to support HB 2148 and renew our opposition to the collection of sales tax on the labor involved in new construction.

As we testified last year before this committee, we believe that placing a sales tax on new construction is a self-defeating effort on the part of the state of Kansas.

During the past recessionary cycle which the country has been experiencing, one of the "signs of recovery" which the economists were all looking for was whether the number of new building permits was increasing. New home construction is considered to be one of the "Leading Economic Indicators", an index which economists use to predict upturns and downturns in our economy.

If new home construction is an industry that historically leads the economy out of a recession, why would the state of Kansas want to do anything which will hamper that industry? How can it be justified that increasing the up-front costs of a new home will somehow be good for our economy? How can the State justify running jobs out of the state at a time when we are losing a critical number of jobs in other industries?

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While the number of building permits issued in 1992 increased over the previous year, we must look to the state line counties which must compete with neighboring states. I believe other conferees have been able to demonstrate for you the great impact our sales tax has had on assisting the building industry in neighboring counties by sending business across the state line.

The annual fiscal note projection for this exemption last year was approximately \$43 million. Yet, the state has been able to collect only a small portion of the projected "gold mine" and has greatly reduced the revenue estimate. We predicted last year that such a tax would not collect those projected amounts, only to be proven correct.

We question, once again, the public policy for placing the sales tax on new construction. It certainly cannot be an economic development argument, because sending new construction across the state line can hardly be interpreted as having positive economic impacts. This sales tax exemption was just as important for economic development as the other sales tax exemptions which were not touched last year, such as the exemptions for machinery and equipment and for farm machinery.

We have recently seen how cyclical our economy can be, thus demonstrating the need for diversity in order to ride the cyclical storms. Government should not be in the business of creating or exacerbating the tough economic cycles. The sales tax on new construction does just that by pushing business and jobs across state lines and by the outright reduction of business within the state.

We know the prospect of raising \$43 million by the removal of this exemption looked appealing because it was so large, at a time when the Legislature was looking for money. However, we are asking you to re-examine the decision made last year in light of the actual dollar amounts collected over the past six

months, in light of the "flight" of business to other states, in light of the dramatically reduced revenue projections and most important, in light of the pressing need for job creation in the state. We ask you to re-instate the sales tax exemption for the labor involved in new construction by recommending HB 2148 favorable for passage.

Thank you again for the opportunity to testify.

Testimony

by
Tom Riederer, President
Lenexa Chamber of Commerce

February 17, 1993

Good Morning. My name is Tom Riederer and I am President of the Lenexa Chamber of Commerce. I am here today in support of HB2148, the repeal of the sales tax on new construction.

Lenexa has been fortunate to have had significant growth, both commercially and residentially. That growth has resulted in increased jobs and tax revenue for Lenexa and the State of Kansas. The growth of Lenexa and of Johnson County has led the State and kept the economy moving forward.

The competition for new business and residential development has become fierce and issues like this tax put us in a difficult position. We compete with Missouri and the cost of this tax may, for example, make a similar home there more attractive, causing us to lose a taxpaying resident, not just a sale. Businesses make decisions based on many criteria, but this tax shows as a negative on their checklist when they consider Kansas. We spend money and time to stimulate the creation of jobs and then put up a roadblock. It doesn't make sense. The Enterprise Zone Program will help many businesses if they are eligible for sales tax exemption, but it will not help the residential developments.

The loss of development or even slowing that development down will not serve the best interest of the State. I believe this will cause greater loss of revenue than it will ever produce. I urge you to repeal this tax.

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February 17, 1993

House Committee on Taxation

Chairman Roe and Members of the Committee

Good morning, my name is Chris Beal and I represent the Greater Kansas City Chamber of Commerce.

The Greater Kansas City Chamber represents over 3,000 businesses in the Kansas City area including a number of home builders and contractors located on both sides of the state line.

One of the legislative priorities for 1993 was the removal of the tax on original construction services.

The construction industry is a major source of jobs in the Kansas City metropolitan area. This tax is ill-conceived for two reasons. First, the tax has brought in only a small portion of the revenue projected when it was adopted last year without the full benefit of public hearings. In addition, some companies are avoiding the tax by moving across the state line into Missouri. Second, the tax has contributed to Kansas' reputation as having an unstable tax environment.

On behalf of the Greater Kansas City Chamber of Commerce, I urge your support for the repeal of the sales tax on original construction as proposed in House Bill 2148.

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TESTIMONY ON THE SALES TAX ON ORIGINAL CONSTRUCTION

By Mark McGrory, President
McGrory Construction, Inc.

My name is Mark McGrory. I am President of McGrory Construction, Inc. I am a small builder in Topeka, Kansas. I build about 15 single-family homes a year, all priced under \$90,000.

Since I build homes at the lower end of the new home price scale, the tax on original construction labor services has been very damaging to my business. My goal as a builder has always been to give people the most home for their money and the general public is very good at buying the best value. Since I build affordable homes instead of large custom homes, used homes become my biggest competition. In order to sell my homes, I must offer a better value than the used home or I lose my customers. The labor services tax has caused me to raise my prices about 2% without adding any value to my homes. This has caused me to lose several customers to the used home market because when people compare value, even a small percentage of increased cost can multiply into a much larger percentage of lost business.

When I lose a customer to the used home market, I am not the only loser. The State of Kansas and the people of Kansas also lose. The state loses because of all the new revenue generated by the construction of a new home is lost. Construction of a new home generates income taxes from all of the people who work on the home, sales taxes from the large quantity of materials used to build the home, plus new property taxes that a new home generates year after year to support our schools and local governments. These are new growth revenues that will not be produced if a home buyer decides to purchase a used home.

The people of Kansas also lose because of the jobs that were not created by the new home. These jobs are not just the people who work on the home, the reach is much greater than that. Many of the jobs created by new construction are never seen at the jobsite. Take a lumber company for example. The truck driver may be the only person at the jobsite but in order to get that lumber to the job, they must employ yardmen, estimators, buyers, draftsmen, salespeople and dispatchers. The same can be said for concrete producers, cabinet suppliers and the multitude of other companies that supply new home products and services. Then add to that the products and services that purchasers of new homes buy after they purchase that new home, such as furniture, draperies and landscaping. There are also many jobs provided by the sales and service of the equipment used by the new construction industry like bulldozers, pickups, compressors, saws, nail guns, and the list goes on and on.

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To get to the point, the State of Kansas should do everything in its power to provide a tax structure favorable to the new construction industry for our mutual benefit. New construction provides growth, growth produces new revenue and new revenue reduces the need to raise taxes. This premise is why the exemption for new construction labor services was enacted in the first place and why it should be reinstated as soon as possible.

CPAK

Commercial Property
Association of Kansas

Gordon T. Garrett
Vice President -
Legal Counsel

Board of Directors

Randy Austin
Fairlawn Plaza
Topeka

Tim Earnest
Melvin Simon Co.
Mgr.-West Ridge Mall
Topeka

Greg Erbert
Godfather's Pizza of Ks
Wichita

Mike Loveland
Commercial Real Estate
J. P. Weigand & Sons
Wichita

Mike McPherson
McPherson Development
Topeka

Cal Roberts
Mortgage Banker
Overland Park

Clarence Roeder
J. C. Nichols Co. (Ret.)
Overland Park

Colby Sandlian
Developer
Wichita

Cindy Sherwood
Dentist
Independence

Bob Shmalberg
Scotch Industries
Lawrence

Ross Stiner
Realtor & Developer
Olathe

Steve Struebing
Attorney - Developer
Junction City

Patty Stull
Realtor
Hays

Eldon Thorman
Motels
Clay Center

Dan Tucker
Banker-Businessman
Kansas City, KS

Larry Winn
Attorney
Overland Park

February 17, 1993

COMMERCIAL PROPERTY ASSOCIATION OF KANSAS

TESTIMONY BEFORE THE

HOUSE COMMITTEE ON ASSESSMENT AND TAXATION

BY

Gordon T. Garrett, V.P. and Legal Counsel

Madame Chair and members of the Committee -

My name is Gordon T. Garrett, and I represent CPAK. The membership of this association includes commercial developers, both large and small, and owner and occupants of commercial buildings.

We wish to speak in support of the repeal of the tax upon original construction services.

As you have already heard excellent testimony and many valid reasons to repeal this tax from others, I will confine my statement to the impact of this tax on commercial development.

As other conferees, we cannot provide accurate statistical data on how this tax may have inhibited commercial development - but logic tells you that its true. If its not true now - it certainly will be in the future.

Aside from the fact that this tax puts Kansas at a competitive disadvantage with other states, and the fact that it is an administrative nightmare, we think this tax inhibits commercial development and new commercial buildings primarily in two ways.

For construction jobs to be created, and construction is a very important part of our economy, a developer or owner must actually make the decision to build something and then get the financing to do it. This tax is just one more negative factor in a

commercial feasibility decision. (This tax simply is inflationary regarding construction costs.)

1. To obtain financing on any commercial project in this climate is extremely difficult. To the extent that this tax raises the cost of the project, it simply makes financing all the more difficult. Federally Insured Lenders now have regulations that they can loan no more than 75% of the cost of a commercial real estate project.

2. Most commercial developments in Kansas in the next few years will almost certainly be small developments. Single users, restaurants, small office buildings, etc. There probably will not be big speculative projects like we witnessed in the 1980's. This tax will undoubtedly inhibit small commercial projects as their bottom line feasibility is narrower than a large project. In effect, this tax may help discourage small developments which are probably the only ones we will see in Kansas for awhile.

Commercial construction is down significantly in Kansas since reappraisal and classification took effect. This tax on original construction exacerbates an already unhealthy tax burden on commercial real estate.

New commercial construction is very important to our states economy in a number of ways. It not only creates and provides jobs, but new commercial construction greatly increases the value of our tax base. With new spending pressures coming from every direction our tax base must be continually expanded if we are to hold in check dramatic mill levy increases.

If this tax stops just one small office building, industrial building, or strip shopping center all of Kansas is a loser. This sales tax is collected just once, but a building that is constructed pays property tax every year, not counting the sales and income taxes the occupants would pay.

We think this tax should be repealed.

Thank you for the opportunity to speak and I will be happy to answer any questions.

TESTIMONY
of the
HOME BUILDERS ASSOCIATION OF KANSAS

My name is Roger Schultz, owner of Schultz Construction, Inc., of Manhattan, Kansas, and Legislative Chairman for the Home Builders Association of Kansas. I am appearing today to voice the strong opposition to the 2.5% gross receipts tax places on new construction by the 1992 Kansas Legislature. I would like to stress that this is a gross receipts tax instead of a tax on labor only which many of the legislators thought they were voting on.

The Home Builders Association of Kansas has contracted with Kansas University professor Dr. Darwin Daicoff, to provide statistics on a statewide basis on the effects of this tax on home ownership and economic impact to the state as a whole. However, that study will not be available until February 4, and we will provide you those results at that time.

The effects of the removal of the sales tax exemption on the economy of Kansas is difficult to predict for several reasons. First, the law contained a provision which exempted any contract signed prior to June 15 from the sales tax. Many contracts were signed which were not fulfilled for weeks or months.

Secondly, interest rates have remained the lowest in years. If the interest rates had been at 12% and 14% level as they were 3 years ago, the affect on the industry would have been greater.

The Kansas Governor and Legislature established a Department of Housing and expanded the name of the Department of Commerce to the Department of Housing and Commerce because of their expressed concern for "Affordable Housing for all Kansas citizens". Yet that same Governor and Legislature enacted legislation which increases the cost of all housing which is not constructed by a non-profit organization.

There is a great deal of confusion regarding the "guidelines" issued by the Department of Revenue. Subcontractors in particular are not sure what they should charge because of the many variables in the system, such as city tax, county tax, remodeling % vs. new construction, etc. This creates a quagmire of expensive bookkeeping and many of the accountants are even unsure of the specific guidelines. This all has a ripple effect of increasing costs not by 2.5% but as much as 5 to 10%.

On top of all this we have created unfair competition with manufactured housing being tax exempt on their inventory and site built being taxed at the existing rates. Also, out of state contractors building site homes have the added advantage of not paying this sales tax.

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Each \$1 spent on new construction in Kansas generates a total of \$2.2450 in economic activity in both industries and services in the state. Each additional \$1 million spent on a new construction in Kansas creates 34.7 jobs. NAHB economists advise that for every \$1,000 increase in the cost of a residence, 1% of the public is priced out of the market.

Increase	Less Homes	Jobs Lost	Wages Lost	Personal Tax
\$1,000	200	335	\$ 7,370,000	\$270,000
\$1,500	300	502	\$11,055,000	\$405,000
\$2,000	400	670	\$14,740,000	\$540,000

Further statistical considerations are not provided for the "ripple effect" on the economy nor the amount of state expenditures for unemployment and assistance due to these loss of jobs. Current construction code revisions and construction material increases combined add significant numbers, 15% to 20% to the cost on construction. These items alone are expected to add as much as \$5,000 to the cost of a moderate house this year. Data from the Federation of Tax Administrators indicates that only 12 states tax new construction labor. 10 states tax excavating and grading on new construction sites. 14 states, including Kansas, tax remodeling labor. 3 other states join Kansas in taxing remodeling and exempting new construction labor and 2 states exempt remodeling and tax new construction labor.

JAMES E.
DUNNING SR.

JAMES E.
DUNNING JR.

CERTIFIED PUBLIC ACCOUNTANTS

RE: Sales Tax on Labor - New Construction

Our clients engaged in residential construction have been severely and negatively impacted by this legislation. The result has been an increased cost of \$1,000 to \$1,200 on a \$100,000 house.

This levy has been applied against overhead and profits in addition to the labor costs. This increased cost has further restricted the number of potential buyers. The related losses of revenue, both local and state wide would seem to outweigh the benefits of this tax on labor - new construction. The losses include, but are not limited to, reduced income tax both by the builder and the potential buyer employed by an industry locating in a neighboring state due to these costs, a loss of sales tax on materials due to the reduction in number of new residences being built, and the loss of Property Taxes for the same reason.

One client currently building 15 new homes per year would realize a direct increase in cost of \$15,000 to \$18,000. If he builds one less house per year, he would pay approximately \$2,200 less sales tax for materials, \$1,100 less personal income tax and \$1,600 less in property tax would be realized each year. This additional \$1,000 to \$1,200 sales tax is potentially costing the state and local governments \$4,900.

I urge you to consider the negative impact of this tax.

Sincerely,

James E. Dunning
James E. Dunning

JED:gf

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TO: HOUSE TAX COMMITTEE

RE: LEGISLATIVE PROPOSAL TO RESTORE THE SALES TAX EXEMPTION
ON ORIGINAL NEW CONSTRUCTION

FROM: WESS GALYON, PRESIDENT/CEO, WICHITA AREA BUILDERS
ASSN.

Dear Committee Member,

I regret that I am out of the state on business and unable to appear before the committee to request your support of the proposal to restore the sales tax exemption on original new construction.

This is an issue that the member companies of the Wichita Area Builders Association feel very strongly about and I did not want to let the opportunity pass to express to you our concerns.

We believe that the construction industry was somewhat singled out in an effort to begin eliminating certain exemptions which would enable the state to collect more tax revenue than would otherwise be the case. It is unfortunate that the zeal to collect more tax dollars overshadowed the real and lasting benefits that a healthy vibrant housing industry contributes to the states economy.

It is further unfortunate that housing affordability has been further threatened at all levels because of the imposition of this additional tax. It is significant to note that the impact of the tax, along with labor cost increases due to work comp, and material cost increases have driven, upward, the cost of housing to the 15% range in the past 24 months. The impact of these increases have not yet been fully realized by the housing industry. When that occurs, it is very likely that we will see a depressed housing industry throughout our state. But for the fact that interest rates have been at their lowest level in 20 years, this condition might very well exist today.

We further feel that the figures which were used to project the benefits in terms of the increased tax revenues to the state were extremely overstated. An analysis of the value of the labor services performed on original new construction in relation to the total value of new construction would not suggest that the tax revenue will be anything near what was estimated. Thus, I would submit that a healthy housing

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industry contributes more benefits to the state in terms of the positive economic impact due to the jobs which are created, the tax base which is expanded, and stability in terms of the maintenance of affordability in housing at all levels for the people of Kansas who desire to own their own home.

Your consideration in regard to restoring the sales tax exemption on original construction services would be sincerely appreciated in an effort to keep the construction industry in Kansas one of the states most viable industries.

Thank you.

WATER DISTRICT NO. 1 OF JOHNSON COUNTY



5930 Beverly — Mission, Kansas 66202
Mailing Address: P.O. Box 2921, Mission, Kansas 66201

Tel. (913) 722-3000
FAX (913) 262-0375

**TESTIMONY PRESENTED TO HOUSE TAXATION COMMITTEE
Rep. Keith Roe, Chairperson
Room 170-W State Capitol**

by

**WATER DISTRICT NO. 1 OF JOHNSON COUNTY
HOUSE BILL 2148**

Mr. Chairman and Members of the Committee:

Water District No. 1 of Johnson County urges passage of House Bill 2148 because it would significantly lessen the financial impact on more than 100,000 customers in Johnson County.

Restoring the exemption of the sales taxes on labor for original construction would be particularly beneficial in 1994 and succeeding years because the District is preparing another expansion of facilities to accommodate the growth in Johnson County.

A glance at the attached chart reveals nearly \$300,000 in each of the years 1994 through 1997 would be added to costs of the District should the exemption not be restored.

This would force the Board to consider an increase in water rates of .7% to .8% simply because of the sales tax effect.

We urge a favorable recommendation on HB 2148 to ease the added impending financial burden on the more than 100,000 families in our area.

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February 17, 1993

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WATER DISTRICT NO.1 OF JOHNSON COUNTY, KS

IMPACT OF SALES TAXES ON NEW CONSTRUCTION LABOR and UTILITIES USED IN MANUFACTURING

2.5% State; 0.5% County; 1.0% Cities

	Amount of Sales Taxes					Total 1993-97
	June-Dec 1993	1994	1995	1996	1997	
TAX ON NEW CONSTRUCTION LABOR:						
Annual Water System Improvements	\$50,300	\$83,800	\$83,800	\$83,800	\$83,800	\$385,500
Master Plan Improvements	46,300	205,500	169,600	225,000	179,800	826,200
TOTAL IMPACT- TAX ON LABOR	\$96,600	\$289,300	\$253,400	\$308,800	\$263,600	\$1,211,700
Water Rate Increase Impact	0.2%	0.7%	0.7%	0.8%	0.7%	
TAX ON UTILITIES USED FOR MANUFACTURING:						
POWER Used In Producing Water	\$114,000	\$122,000	\$130,000	\$139,000	\$148,000	\$653,000
Water Rate Increase Impact	0.3%	0.3%	0.3%	0.3%	0.4%	
GRAND TOTAL BOTH TYPES OF TAXES	\$210,600	\$411,300	\$383,400	\$447,800	\$411,600	\$1,864,700
Water Rate Increase Impact	0.5%	1.0%	1.0%	1.1%	1.1%	

SALTXIMP
02/12/93

19-2