Approved: March 8, 2011
Date

MINUTES OF THE SENATE ASSESSMENT & TAXATION COMMITTEE

The meeting was called to order by Vice Chairman Pat Apple at 10:30 a.m. on February 16, 2011, in Room 152-S of the Capitol.

All members were present except:
Chairman Les Donovan – excused
Sen. Bob Marshall – excused

Committee staff present:
Gordon Self, First Assistant Revisor of Statutes
Scott Wells, Office of the Revisor of Statutes
Chris Courtwright, Kansas Legislative Research Department
Michael Wales, Kansas Legislative Research Department
Mary Jane Brueck, Committee Assistant

Conferees appearing before the Committee:
Secretary Nick Jordan, Department of Revenue
Secretary Pat George, Department of Commerce
Richard Cram
Stan Aliech
Kent Eckles, Vice President of Public Affairs, Kansas Chamber of Commerce
Jennifer Bruning, Overland Park Chamber of Commerce
Christy Caldwell, Vice President Government Relations, Greater Topeka Chamber of Commerce
Blake Schreck, President, Lenexa Chamber of Commerce
Mark Murrey, National Federation In. (Independent?) Business (late testimony)
Art Hall
Angela Pitale, Director of Tax for NextEra Resoources, LLC
Bernie Koch, Kansas Economical Progress Council
Dennis Lauver, President & CEO, Salina Area Chamber of Commerce
Sheila Lenson, Associated Wholesale Grocers, Inc.
Betty Nelson -Ekey, Managing Director, Tax Incentives Group
Shawn Sullivan, Vice President of Tax Services, Allen Gibbs, & Houlik, L.C. Of Wichita KS
Ronald C. Seeber, Kansas Association of Ethanol Producers
Chris Vering, Knit-Rite, Inc.
Manolis Alatziniotakis, Karatzis USA LLC
Thomas Reed, Popstar Networks, Inc.
Tim Huttegegr, CEO Marathon Solutions, Inc.
Richard Mills III, CBIZ
Rick Katz, The Katz Law Firm
Eli Bowman, representing Codero

Others attending:
See attached list.

Vice-Chairman Pat Apple opened the meeting and explained he would start the ~~hearing~~ on today's bill with the an explanation of the bill by Gordon Self, First Assistant Revisor of Statutes, followed by hearing comments from Secretary Jordan, Secretary George, Richard Cram, and Stan Alrich., followed by brief questions. Then we will start moving through the list of conferees, giving them five minutes apiece to speak. We will try to give people who are here today and not able to be here tomorrow, even if they are opponents, time to speak.

He then opened the hearing on **SB 196 - Authorizing expensing of investment expenditures as a deduction in calculating Kansas income tax liability and IMPACT program changes**. by introducing Secretary Nick Jordan, Department of Revenue. He feels this bill will be beneficial to small businesses and the entire state of Kansas. This is a revenue neutral package. HPIP tax credits will be "granfathered in" this bill. (Attachment 1) Secretary Pat George, Department of Commerce told the committee this bill will not only be good for new businesses but also existing businesses by creating an environment favorable to business – from farming to manufacturing. (Attachment 2) Richard Cram discussed various aspects of this bill: expense deduction and other provisions. (Attachment 3) Richard introduced the committee to Stan Ahlerich, President, Kansas, Inc. He said Kansas Inc.'s montra is "every business matters". This bill will allow the state to build up moneys for the job creation fund, and it is revenue neutral. (no written testimony provided).

Vice-Chairman Apple introduced Kent Eckles, Vice President of Public Affairs, Kansas Chamber of Commerce. He spoke highly about aspects of this bill increasing economic growth. The Chamber recommends three provisions contained in HB 2051 included in SB 196: "allowing a corporation with multiple unitary groups to apply existing HPIP credits against the tax liability of any member or members of its unitary group in their combined tax report; extending from ten to twenty years the deadline for corporations to claim existing HPIP investment tax credits; eliminating the requirement that a company attains recertification before utilizing the tax credits." (Attachment 4)

Jennifer Bruning, Overland Park Chamber of Commerce said they feel there are many good aspects to this bill. She urged the committee to consider their suggestions to eliminate the HPIP sunset provision and the inclusion of contents of HB 2051. (Attachment 5) Christy Caldwell, Vice President Government Relations, Greater Topeka Chamber of Commerce, addressed four items: Expensing, making HPIP stronger by adding language from HB 2051; the job creation fund; and the machinery and equipment (M&E) property tax credit. (Attachment 6) Blake Schreck, President, Lenexa Chamber of Commerce; Art Hall, Executive Director, Center for Applied Economics, Kansas University School of Business submitted written testimony in favor of the bill. (Attachments 7 and 8)

Dennis Lauver, President & CEO, Salina Area Chamber of Commerce was recognized to speak as a neutral party. They feel the HPIP program is effective and is valued; making the state more neutral in decision making is a great idea; a cash based program will be a very effective tool that will stimulate jobs and capital investment; eliminating the sales tax exemption will stunt growth; there is a sense the deduction expensing concept will disproportionally help very large employers and may have limited impact. (Attachment 9)

Gary C. Allerheiligen, CPA and Immediate Past President of the Kansas Society of CPAs told the committee that after discussion with the leadership of KSCPA their position is neutral (Attachment 10) Bernie Koch, Kansas Economic Progress Council, submitted neutral written testimony on SB 196. (Attachment 11)

Sheila Lenson, representing Associated Wholesale Grocers, Inc. spoke in opposition to the bill.because in five years, it eliminates the High Performance Incentive Program (HPIP), which includes the sales tax exemption, while immediately increasing the investment credit threshold from $50,000.00 to $5,000,000.00 (Attachment 12) Betty Nelson -Ekey, Managing Director, Tax Incentives Group, representing CBIZ. She is in opposition to this bill because it would sunset the High Perfoorance Incentive Program (HPIP) in five years while raising the investment threshold to $5,000,000.00. (Attachment 13) Shawn Sullivan, Vice President of Tax Services, Allen Gibbs, & Houlik, L.C. Of Wichita KS told the committee this bill will have a crippling effect on the state's economic development efforts to recruit new businesses and retain our existing businesses in Kansas, resulting in the likely loss of capital, jobs and businesses in Kansas. (Attachment 14)

Written testimony in opposition was submitted by: Ron Seeber, Association of Ethanol Processors (Attachment 15); Chris Vering, Knit-Rite, Inc. (Attachment 16); Manolis Alatziniotakis, representing KARATZES USA LLC (Attachment 17); Thomas Reed representing Popstar Networks, Inc. (Attachment 18); Tim Hutteger, Marathon Solutions, Inc. (Attachment 19); Richard Mills, III representing CBIZ (Attachment 20); Rick Katz, Katz Law Firm (Attachment 21); and Eli Bowman, representing Codero (Attachment 22)

Vice-Chairman Apple asked if there were any other conferees who would not be able to attend tomorrow's continuation of this hearing. Seeing none, we will continue this hearing tomorrow, and we are adjourned.

The next meeting is scheduled for February 17, 2011.

The meeting was adjourned at 11:49 a.m.

SENATE
Assessment & Taxation Committee
GUEST LIST

DATE: 2-16-11

NAME	REPRESENTING
Sheila Lenson	Assoc. Wholesale Grocers
Betty Nelson-Ekey	CBIZ Accounting firm
DAN LARA	Commerce
Bud Burke	Cessna
Jane Wallace	KCEDC
Randall Hrabe	NW K P+D C
Cheryl Hayward	KS CPA Society
Mary MacBain	KS CPA Society
Bob North	Commerce
[illegible]	COMMERCE
[illegible]	Commerce
Jerry Capps	Allen Gibbs & Houlik LC
SHAUN SULLIVAN	ALLEN GIBBS & HOULIK, LC
Harry A. Watts	KFB
[illegible]	Commerce
John Frederick	The Boeing Co.
DENNIS W LAUVER	Salina Chamber of Commerce
Christy Caldwell	Topeka Chamber
George Stafford	Cerner

SENATE
Assessment & Taxation Committee
GUEST LIST

DATE: ____________

NAME	REPRESENTING
Michelle Butler	Cap. Strategies

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TESTIMONY
Senate Assessment and Taxation Committee
February 16, 2011
Senate Bill 196
by
Secretary of Revenue Nick Jordan

The Governor's Economic Growth Tax Policy

In his inaugural state of the state address a few weeks ago, Gov. Brownback named economic growth in Kansas as his top priority, and he urged us to work together to create the framework for more private sector jobs – and more earnings for Kansas families. In that spirit, a key component of the Governor's economic growth plan is the elimination of corporate tax subsidies enjoyed by only a few as we move toward a tax structure that will help all businesses in our state grow. That is what we are here to discuss today.

Taxation is a claim the government makes on the economic value created by the private sector. The more the government taxes an economic activity, the less that activity will take place.

To expand its economy, Kansas needs to minimize the taxation of activities related to risk-taking and the process of economic competition. We must sustain an environment in which entrepreneurs, businesses and innovation thrive. Our policy should encourage the growth of capital and investment.

From a public policy analysis, we should distinguish between the terms "economic growth" and "economic development" because people mistakenly use the terms interchangeably. Simply stated, economic development constitutes the many interrelated economic processes that culminate in economic growth – particularly the component of growth driven by improved labor productivity.

To maximize economic growth we must recognize that every business, every innovation and every entrepreneur matters. The initiatives described in this testimony strive to motivate all manner of people to commit their time and treasure to Kansas soil. The initiatives seek to increase the overall volume of new business starts and business expansions. Our policy challenge centers on establishing a business environment that induces the maximum amount of business birth and expansion without bias related to the size or type of business.

In a recent speech, Richard Fisher, president and CEO of the Federal Reserve of Dallas, said:

> "A look within the United States makes clear the overriding influence of fiscal and regulatory policy. Monetary policy is uniform across the 50 states; the base rate of interest paid on a business or consumer loan or a mortgage in Michigan, California, Ohio or here in New York is the same as that paid in Texas. Yet there is a reason that Michigan and California each lost more than 600,000 jobs over the past decade while Texas added more than 700,000 over the same period. There is a reason that the population of Ohio grew by only 183,000 residents over the past 10 years, while Texas grows by that number every five and a half months. There is a reason, as reported in this morning's *Wall Street Journal*, college graduates – the best and brightest of the successor generation – are leaving New York and Cleveland and Detroit and moving to Austin, Texas. There is a reason Texas now houses more Fortune 500 headquarters than any other state in the union.
>
> "That reason has nothing to do with monetary policy. It has everything to do with the taxation and fiscal and regulatory policy of the states. The cost of capital does not explain the different economic performances of the states; the cost of doing business has everything to do with those differences. However well-meaning tax and regulatory initiatives in the laggard states may have been when they were conceived and levied, they have had unintended consequences that have led to economic underperformance and job destruction.
>
> "Recent data make clear that the risks of a double-dip recession and deflation have ebbed and that economic growth and job creation are beginning to flow. Yet the ships of job-creating investment remain, for the most part, tied to the docks, or, worse, choose to sail for foreign ports where tax and regulatory conditions are more favorable."

Tax policy plays a central role in economic development policy. Over the decades, Kansas has enacted a variety of tax policies intended to advance economic development. Many of them provide a meaningful economic incentive to make new investments and create new jobs. And almost all of the policies provide meaningful incentive to a small number of worthy businesses to the exclusion of hundreds of thousands of other worthy businesses.

For example, in tax year 2008, 162 taxpayers claimed the High Performance Incentive Program credit; 635 claimed the business and job development credit; and 13,510 received business machinery and equipment credits. Compare these numbers with the 221,000 enterprises in Kansas that stand to benefit from tax policies that incentivize private investment more broadly.

The legislation before you would exponentially increase the number of potential businesses benefiting from smart changes to our tax code and encourage far more investment and growth in the private sector.

Our approach is designed to balance programs for attracting and expanding larger businesses with benefits for the thousands of small businesses in Kansas.

HIGH PERFORMANCE INCENTIVE PROGRAM (HPIP)

HPIP, with its 10 percent tax credit for investments and the sales tax exemption for HPIP related work, has proved attractive to many of our larger companies. There is a $50,000 investment threshold to qualify. In the Governor's proposal, we are changing only one aspect of HPIP, which would raise the threshold to $5 million. This figure was determined by reviewing the investment levels of larger companies in Kansas.

BUSINESS INVESTMENT EXPENSING

Expensing relates to the calculation of business income tax. Whenever a business makes a capital investment, it is allowed to take a deduction against income tax for the depreciation of the investment. Expensing is one form of depreciation deduction, and it allows for an immediate deduction of the full investment amount instead of requiring a prescribed schedule of smaller deductions over multiple years.

Expensing, properly implemented, is a tax policy that treats all businesses equally. By allowing business taxpayers to capture the time value of money related to an investment, expensing results in uniform income tax treatment for investments of all types and sizes.

Expensing shifts the time value of money from the state government to businesses undertaking investment. The shift explains the economic development "incentive." It improves the expected rate of return on every investment. This initiative seeks to make the investment-related tax incentive logically consistent and universally available rather than ad hoc.

The implementation of expensing in this plan is somewhat unique from a tax practitioner's perspective. It seeks to provide the full value of expensing to Kansas business investors, which is not provided by the depreciation procedures allowed by federal tax law. It is important to note here that, while the deduction generated by the Governor's expensing plan is not the equivalent of "full expensing" as practitioners would interpret it in a federal tax context, this would *not* decouple Kansas from the federal system.

The recent federal tax package included one year of full expensing. The Kansas expensing proposal would go into effect after the expiration of the federal program. At this time, we would be the only state known to have expensing. The proposal would result in approximately $47 million dollars available for investment in Kansas.

DEPARTMENT OF COMMERCE JOB CREATION FUND

The Kansas IMPACT program, along with savings from the elimination of certain tax credits, would be converted to a multi-million dollar fund that can be used to close economic development deals. This "job creation fund" is designed to strengthen state incentive program. and give the Secretary of Commerce and Governor flexibility to make prudent decisions to close a deal on a prime economic growth opportunity without adding additional debt to the state.

Considered together, the move away from certain limited tax credits combined with the implementation of expensing, HPIP adjustments, and the job creation fund forms a thoughtful ***economic growth package*** that balances the needs of larger businesses with the needs of tens of thousands of small- to mid-sized businesses in our state.

Thank you, Mr. Chairman and members of the committee.

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Pat George, Secretary

Department of Commerce

Sam Brownback, Governor

Testimony on Senate Bill 196
to
The Senate Assessment and Taxation Committee
by Secretary Pat George
Kansas Department of Commerce
February 16, 2011

Thank you for the opportunity to testify before you this morning on SB 196.

The Department of Commerce is focused on bringing jobs to the State of Kansas. Creating an environment that is inviting to businesses looking to relocate to Kansas is critical in moving forward. In order to become more attractive to these companies, the state must reduce the taxation of activities related to commerce, in order to encourage innovation and the development of new products and services. Encouraging and expanding investment is what this legislation is all about.

Historically, Kansas has had a tax policy that encouraged growth, but was not inclusive of all businesses that deserved to be supported through economic development incentives. The expensing legislation that we are discussing today will treat all businesses equally by allowing business taxpayers to capture the time value of money related to an investment. This is an incentive to business by transitioning the expected rate of return on the investment from state government to the organization that makes the investment.

Sn. Assmnt & Tax
2-16-11
Attachment # 2

The Department of Commerce is in favor of this proposal because we believe it makes Kansas a more attractive state to locate a business, as well provides the necessary incentive to make capital investment and expand a business. In addition, expensing will help Kansas stand out on the economic development landscape, with $47 million available for investment in Kansas, as well as the only state with an expensing option.

I would also like to discuss the High-Performance Incentive Program (HPIP) for a moment. This has been a great recruitment tool for large corporations in particular. In this legislation, we have raised the initial investment from $50,000 to $5,000,000.

Finally, the Department of Commerce Job Creation Fund, I believe will be another critical business development tool for the state. Essentially, the Kansas IMPACT program and other incentives that will be collapsed as a result of this legislation will be converted into the "job creation fund" that further enables us to secure an important deal for the state, which in turn does not add to our debt. The Governor and Secretaries of Commerce and Revenue would be able to evaluate each deal and utilize when it is deemed necessary. This flexibility is important, and crucial for our economic development team to keep Kansas competitive. Funds like this have been used successfully in other states, and businesses have come to expect.

Thank you for the opportunity to speak today, and I am happy to stand for questions.

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February 16, 2011

Senate Committee on Assessment and Taxation

Briefing on Expensing Provisions in Senate Bill 196

Presented by Richard Cram

Chairman Pat Apple and Members of the Committee:

Senate Bill 196 will provide a new expense deduction to all Kansas businesses for certain qualifying machinery and equipment, as well as canned computer software, placed into service (first made available for use in the business), starting in Tax Year 2012. It also calls for the repeal or limitation of certain tax credits, exemptions and programs now available only to a limited number of businesses in order to reserve sufficient revenue to cover the fiscal impact of this new deduction, as well as provide funding for the new job creation program fund.

Expense Deduction

Senate Bill 196 provides businesses that invest in machinery and equipment depreciable under the Modified Accelerated Cost Recovery System (MACRS) in section 168 of the Internal Revenue Code, or canned software as defined in section 197 of the Internal Revenue Code, an expense deduction against Kansas taxable income. The property must be located in Kansas to qualify for the expense deduction.

The Kansas expense deduction, when added to the present value of the depreciation deductions provided under federal income tax law, equals the full value of the cost of the machinery and equipment placed into service.

Present value is the current worth of a future sum of money or stream of cash flows given a specified rate of return. One dollar in your wallet now has a value of one dollar, and it is worth more to you than a dollar received a year from now. If you could earn 5% interest on an investment and you invested one dollar today, it would be worth $1.05 a year from now. Thus, the "present value" of $1.05 received a year from now is only $1.

The federal depreciation rules provide a stream of depreciation deductions, depending on the applicable recovery period for the type of property and the applicable depreciation method. For example, a computer is considered "five-year property," and is normally subject to the 200% declining balance method of depreciation under IRC Section 168. For a computer placed into service in the business in Tax Year 2012 with a cost of $10,000 and 5-year applicable recovery period, the Modified Accelerated Cost Recovery System (MACRS) IRC section 168 depreciation rules would provide federal income tax depreciation deductions as follows:

Tax Year 2012	$2,000
Tax Year 2013	$3,200
Tax Year 2014	$1,920
Tax Year 2015	$1,152
Tax Year 2016	$1,152
Tax Year 2017	$576
Total Cost Recovered	$10,000

If we assumed a discount rate (same as interest rate) of 5%, the present value of this stream of depreciation deductions would equal $8,840.

The expense deduction is computed by multiplying the depreciable cost of the item placed into service times the factor shown in the table in subparagraph (f) of Section 2, based on the recovery period (differs depending on the type of property) and method of depreciation (200% declining balance, 150% declining balance, straight-line) determined under IRC section 168, minus any IRC section 168(k) bonus depreciation claimed for the same item on the federal return. In determining the Kansas expense deduction, the business does not need to subtract from the depreciable cost any IRC section 179 expense deduction claimed on the federal return for the item.

The table in subparagraph(f) of Section 2 provides the factor, which when multiplied times the depreciable cost, determines the Kansas expense deduction (assuming no bonus depreciation is claimed at the federal level). This represents the difference between the present value of the stream of depreciation deductions permitted under the MACRS IRC section 168 rules and the depreciable cost of the property, using a discount rate of 5%. For businesses taking the IRC section 179 federal expense deduction, the Kansas expense deduction gives them the full value of the investment—plus the federal section 179 expense deduction: essentially "double-counting" the investment, for Kansas income tax purposes.

The expensing provisions in Senate Bill 196 do not "decouple" from the federal bonus depreciation or expensing provisions. Senate Bill 196 provides a Kansas expense deduction claimed on the Kansas income tax return, after any available federal depreciation deductions are already taken on the federal return. This means there is not requirement to "add-back" to the Kansas return any federal depreciation deductions taken in future tax years after the House Bill 2317 expense deduction is taken in the year the capital asset is placed into service.

Attached is an excerpt out of Table B-1 from IRS Publication 946, which identifies the class life, recovery period and depreciation method applicable to certain types of depreciable property. Asset class 00.12, Information Systems, includes computers, which are assigned a recovery period of 5 years under the General Depreciation System (GDS), which means the 200% declining balance depreciation method applies. The table in subparagraph (f) of Section 2 in Senate Bill 196 shows a factor of .116 (second column) for property with a recovery period of 5 years (first column), where the 200% declining balance method of depreciation (second column) applies. If the business is not taking any IRC section 168(k) bonus depreciation on the property, the Kansas expense deduction for a $10,000 computer placed into service in Tax Year 2012 would be .116 times $10,000 = $1,160.

If the business is claiming IRC Section 168(k) 50% bonus depreciation in Tax Year 2012, that amount must be subtracted from the depreciable cost of the computer before the Kansas expensing deduction is calculated: $10,000 -$5,000 = $5,000. The amount of the Kansas expense deduction in this situation is: $5,000 times .116 = $580.

If the business is claiming IRC Section 179 expensing for this computer, then no subtraction is made from the depreciable cost before multiplying that times the applicable factor to compute the Kansas expense deduction: $10,000 times .116 = $1,160 is the Kansas expense deduction.

The Kansas expense deduction is a post-apportionment deduction. For a multi-state business, this means the deduction is applied after the income has been apportioned to Kansas.

For example, if a corporation does business in both Missouri and Kansas and has property, payroll and sales in both states, the corporation's total multi-state business income (i.e., its federal taxable income after any applicable Kansas modifications) will be apportioned to Kansas for Kansas income tax purposes, based on the application of the 3-factor formula, which takes the average of 3 fractions: Kansas payroll divided by the corporation's payroll everywhere, Kansas property divided by property everywhere, and Kansas sales divided by sales everywhere. The average of those three fractions determines the corporation's Kansas apportionment factor, which is multiplied by the corporation's federal taxable income after Kansas modifications to compute the corporation's Kansas taxable income.

In our example, assume the multi-state corporation has Tax Year 2012 federal taxable income after Kansas modifications of $200,000 and has placed in service a computer with a cost of $10,000. In computing federal taxable income, the corporation would already have subtracted any applicable federal depreciation or expensing deductions. If the corporation were claiming IRC Section 179 expensing, it would have already taken a federal expensing deduction of $10,000. If the corporation were claiming 50% bonus depreciation, it would have already taken the normal MACRS deduction of $2,000 plus the 50% bonus depreciation deduction of $5,000.

Assume the corporation has a Kansas apportionment factor of .25. Now its Kansas taxable income can be computed: .25 times the federal taxable income with Kansas modifications = .25 times $200,000 = $50,000. If the corporation had claimed no federal bonus depreciation and had instead claimed an IRC Section 179 expense deduction of $10,000 on the federal return, the Kansas expense deduction would be $10,000 x .116 = $1,160 and claimed against Kansas taxable income of $50,000. By taking the Kansas expensing deduction after apportionment, the corporation receives the full benefit of the deduction: from Kansas taxable income of $50,000, the Kansas expense deduction of $1,160 is subtracted, and Kansas income tax liability is computed on $48,840 income: 4% tax on $48,840, for total of $1,954 in Kansas corporate income tax is due.

Any unused expense deduction may be carried forward until fully claimed in future tax years.

Part of the deduction is "recaptured" if the property is later sold or moved outside of Kansas during its applicable recovery period. For example, if a computer with a cost of $10,000 were placed in service in Tax Year 2012 and a Kansas expense deduction of $1,160 were claimed in Tax Year 2012, then if the computer were moved outside of Kansas during Tax Year 2013, part of the Kansas expense deduction of $1,160 claimed in Tax Year 2012 would need to be "recaptured" and claimed as Kansas apportioned income in Tax Year 2013. Since the computer has a recovery period of 5 years and it was moved out of state with 4 years still remaining in the recovery period, then 4/5 of the expense deduction would need to be recaptured and reported as Kansas income in Tax Year 2013: .8 x $1,160 = $928.

For a unitary business group, the deduction earned by one member may be claimed by another member that can use it. A spreadsheet is attached, illustrating how this would work in a hypothetical situation.

If the business claims the expense deduction, it will not be eligible for the following investment-related tax credits or other incentives: high performance incentive program credit, research and development credit, alternative fuel vehicle credit, swine facility improvement credit, historic preservation credit, refinery credit or accelerated depreciation; oil or gas pipeline or accelerated depreciation; integrated coal or coke gasification nitrogen fertilizer plant credit or accelerated depreciation; biomass-to-energy plant credit or accelerated depreciation; integrated coal gasification power plant credit; renewable electric cogeneration facility credit or accelerated depreciation; biofuel storage and blending equipment credit or accelerated depreciation; carbon dioxide capture equipment credit; or film production credit.

The fiscal impact of implementing the expense deduction using a 5% discount rate for the factors is estimated to be a negative $47.4 million/FY 2013.

Other Provisions

Senate Bill 196 proposes limitations on certain credits, exemptions, and other programs.

No further business and job development credits may be earned starting in Tax Year 2012.

For HPIP credits starting in Tax Year 2012, the current $50,000 minimum investment threshold is increased to $5 million, and the credit applies to qualifying investment in excess of $5 million. The Secretaries of Commerce and Revenue are authorized address transition situations during 2012. The HPIP credit will sunset in Tax Year 2017. For example, in Tax Year 2011, an HPIP-certified business places into service $10 million of qualified business facility investment and earns an HPIP credit equal to $10 million - $50,000 = $9,950,000 x 10% = $995,000. Were that same amount of investment to be placed into service in Tax Year 2012, the HPIP credit earned would be $10 million - $5 million = $5 million x 10% = $500,000.

Under Senate Bill 196, the HPIP credit would sunset in Tax Year 2017.

The refundable business machinery and equipment tax credit for property taxes paid would no longer apply starting in Tax Year 2012. Business machinery and equipment placed into service on or after July 1, 2006 is exempt from personal property tax. Equipment placed into service prior to that date would still be subject to personal property tax, and K.S.A. 79-32,206 currently provides a refundable tax credit for 25% of the personal property tax paid on business machinery and equipment/

The enterprise zone sales tax exemption (K.S.A. 79-3606(cc)) exempts from sales tax purchases of materials, machinery, equipment, and labor for the construction, reconstruction, enlargement or remodeling of a business facility when the requirements of the business & job development credit or the HPIP credit are met. Under Senate Bill 196, this sales tax exemption would end effective January 1, 2012 for projects qualifying for the business and job development credit, which will end after Tax Year 2011. The enterprise zone sales tax exemption for HPIP-qualified projects will end as of January 1, 2017, to coincide with the sunset of the HPIP credit.

The Kansas Economic Opportunity Initiative Fund (KEOIF) would be repealed effective January 1, 2012, and any moneys in that fund are to be transferred to the new job creation program fund.

Fiscal Estimate Breakout
The fiscal estimates for the various components of Senate Bill 196 are broken out as follows:

Implement Kansas expensing deduction @5% discount rate:

FY 2012	FY 2013
-$6 million	-$47.4 million

Repeal B&J credit effective TY 2012:

FY 2012	FY 2013
minimal	+$5 million

Raise minimum investment threshold for HPIP to $5 million and provide 10% credit only for amount of investment exceeding $5 million, effective TY 2012:

FY 2012	FY 2013
minimal	+$6.8 million

Repeal enterprise zone sales tax exemption for B&J starting Jan. 1, 2012

FY 2012	FY 2013
+$10 million	+$49.5 million

Repeal BM&E refundable credit effective TY 2012

FY 2012	FY 2013
0	+$37 million

Repeal KEOIF effective Jan. 1, 2012

FY 2012	FY 2013
+$1.3 million	+$1.3 million

Net Total Revenue (to be reserved for the new job creation program fund)

FY 2012	FY 2013
+5.3 million	+52.2 million

Job Creation Program Fund
The net positive revenues above are envisioned to be used for funding the new Job Creation Program Fund, along with changes proposed to the IMPACT fund, which will be explained by Department of Commerce staff.

Balloon Amendment
We have attached a balloon amendment, technical in nature, to replace the term "Kansas taxable income" with the term "Kansas net income before expensing or recapture" in Section 2(a) and (e).

Table B-1. **Table of Class Lives and Recovery Periods**

Asset class	Description of assets included	Class Life (in years)	Recovery Periods (in years) GDS (MACRS)	ADS
	SPECIFIC DEPRECIABLE ASSETS USED IN ALL BUSINESS ACTIVITIES, EXCEPT AS NOTED:			
00.11	**Office Furniture, Fixtures, and Equipment:** Includes furniture and fixtures that are not a structural component of a building. Includes such assets as desks, files, safes, and communications equipment. Does not include communications equipment that is included in other classes.	10	7	10
00.12	**Information Systems:** Includes computers and their peripheral equipment used in administering normal business transactions and the maintenance of business records, their retrieval and analysis. Information systems are defined as: 1) Computers: A computer is a programmable electronically activated device capable of accepting information, applying prescribed processes to the information, and supplying the results of these processes with or without human intervention. It usually consists of a central processing unit containing extensive storage, logic, arithmetic, and control capabilities. Excluded from this category are adding machines, electronic desk calculators, etc., and other equipment described in class 00.13. 2) Peripheral equipment consists of the auxiliary machines which are designed to be placed under control of the central processing unit. Nonlimiting examples are: Card readers, card punches, magnetic tape feeds, high speed printers, optical character readers, tape cassettes, mass storage units, paper tape equipment, keypunches, data entry devices, teleprinters, terminals, tape drives, disc drives, disc files, disc packs, visual image projector tubes, card sorters, plotters, and collators. Peripheral equipment may be used on-line or off-line. Does not incude equipment that is an integral part of other capital equipment that is included in other classes of economic activity, i.e., computers used primarily for process or production control, switching, channeling, and automating distributive trades and services such as point of sale (POS) computer systems. Also, does not include equipment of a kind used primarily for amusement or entertainment of the user.	6	5	5
00.13	**Data Handling Equipment; except Computers:** Includes only typewriters, calculators, adding and accounting machines, copiers, and duplicating equipment.	6	5	6
00.21	**Airplanes (airframes and engines), except those used in commercial or contract carrying of passengers or freight, and all helicopters (airframes and engines)**	6	5	6
00.22	**Automobiles, Taxis**	3	5	5
00.23	**Buses**	9	5	9
00.241	**Light General Purpose Trucks:** Includes trucks for use over the road (actual weight less than 13,000 pounds)	4	5	5
00.242	**Heavy General Purpose Trucks:** Includes heavy general purpose trucks, concrete ready mix-trucks, and ore trucks, for use over the road (actual unloaded weight 13,000 pounds or more)	6	5	6
00.25	**Railroad Cars and Locomotives, except those owned by railroad transportation companies**	15	7	15
00.26	**Tractor Units for Use Over-The-Road**	4	3	4
00.27	**Trailers and Trailer-Mounted Containers**	6	5	6
00.28	**Vessels, Barges, Tugs, and Similar Water Transportation Equipment, except those used in marine construction**	18	10	18
00.3	**Land Improvements:** Includes improvements directly to or added to land, whether such improvements are section 1245 property or section 1250 property, provided such improvements are depreciable. Examples of such assets might include sidewalks, roads, canals, waterways, drainage facilities, sewers (not including municipal sewers in Class 51), wharves and docks, bridges, fences, landscaping shrubbery, or radio and television transmitting towers. Does not include land improvements that are explicitly included in any other class, and buildings and structural components as defined in section 1.48-1(e) of the regulations. Excludes public utility initial clearing and grading land improvements as specified in Rev. Rul. 72-403, 1972-2 C.B. 102.	20	15	20
00.4	**Industrial Steam and Electric Generation and/or Distribution Systems:** Includes assets, whether such assets are section 1245 property or 1250 property, providing such assets are depreciable, used in the production and/or distribution of electricity with rated total capacity in excess of 500 Kilowatts and/or assets used in the production and/or distribution of steam with rated total capacity in excess of 12,500 pounds per hour for use by the taxpayer in its industrial manufacturing process or plant activity and not ordinarily available for sale to others. Does not include buildings and structural components as defined in section 1.48-1(e) of the regulations. Assets used to generate and/or distribute electricity or steam of the type described above, but of lesser rated capacity, are not included, but are included in the appropriate manufacturing equipment classes elsewhere specified. Also includes electric generating and steam distribution assets, which may utilize steam produced by a waste reduction and resource recovery plant, used by the taxpayer in its industrial manufacturing process or plant activity. Steam and chemical recovery boiler systems used for the recovery and regeneration of chemicals used in manufacturing, with rated capacity in excess of that described above, with specifically related distribution and return systems are not included but are included in appropriate manufacturing equipment classes elsewhere specified. An example of an excluded steam and chemical recovery boiler system is that used in the pulp and paper manufacturing equipment classes elsewhere specified. An example of an excluded steam and chemical recovery boiler system is that used in the pulp and paper manufacturing industry.	22	15	22

3-7

Three companies are members of a unitary group that file in Kansas. Co A is the parent company with some research activities located at its manufacturing facilities. Co B manufactures widgits and has one of its plants in Chapman, KS. Co B has placed into service in Tax Year 2012 fabricated metal manufacturing equipment at a cost of $5.5 million. This equipment has a 7 year applicable recovery period and is depreciated under GDS using the 200% declining balance method. The subparagraph (f) factor is .151. Co C sells the widgets around the world and has a sales office in Wichita, KS.

Unitary Group Usage of Kansas Expense Deduction

Expense deduction used against the combined group:

	Co A	Co B	Co C	Total
Combined Income	4,740,000	4,740,000	4,740,000	4,740,000
Average App't %	0.6091%	15.8560%	2.0953%	18.5604%
Kansas Taxable Income (KTI)	28,871	751,574	99,317	879,763
Expensing Deduction	0	751,574	78,926	830,500
(.151 x $5.5M=$830,500)				
KTI after Deduction	28,871	0	20,391	49,263
Tax @ 4%	1,155	0	816	1,971
Surtax @ 3.05% (>$50,000)	0	0	0	0
Total	1,155	0	816	1,971
Tax After Expensing Deduction	1,155	0	816	1,971

Unitary Group Tax Liability WITHOUT Kansas Expense Deduction

	Co A	Co B	Co C	Total
Combined Income	4,740,000	4,740,000	4,740,000	4,740,000
Average App't %	0.6091%	15.8560%	2.0953%	18.5604%
Kansas Taxable Income	28,871	751,574	99,317	879,763
Tax @ 4%	1,155	30,063	3,973	35,191
Surtax @ 3.05% (>$50,000)	0	21,398	1,504	25,308
Total Tax	1,155	51,461	5,477	60,498

Session of 2011

SENATE BILL No. 196

By Committee on Assessment and Taxation

2-11

AN ACT concerning taxation; relating to IMPACT program, withholding, requirements, limitations; income tax deductions, expensing of investment expenditures; income tax credits; sales tax exemptions; creating job creation program fund, administration, expenditures; amending K.S.A. 2010 Supp. 74-50,104, 74-50,106, 74-50,107, 74-50,109, 74-50,110, 74-50,111, 74-50,132, 79-32,160a, 79-32,206 and 79-3606 and repealing the existing sections; also repealing K.S.A. 2010 Supp. 74-50,151 and 74-50,152.

Be it enacted by the Legislature of the State of Kansas:

New Section 1.□(a) There is hereby created in the state treasury the job creation program fund. The secretary of commerce, in consultation with the secretary of revenue and the governor, shall administer the fund. All expenditures from the fund shall be for the purpose of promoting job creation and economic development by funding projects related to: (1) Major expansion of an existing Kansas commercial enterprise;

(2)□potential location in Kansas of the operations of major employer;

(3)□award of a significant federal or private sector grant which has a financial matching requirement;

(4)□potential departure from Kansas or the substantial reduction of the operations of a major Kansas employer;

(5)□training or retraining activities for employees in Kansas companies;

(6)□potential closure or substantial reduction of the operations of a major state or federal institution;

(7)□projects in counties with at least a 10% population decline during the period from 2000 to 2010; or

(8)□other unique economic development opportunities.

(b)□All expenditures from the fund shall be for the purposes described in subsection (a) and shall be made in accordance with appropriation acts upon warrants of the director of accounts and reports issued pursuant to vouchers approved by the secretary of commerce or the secretary's designee.

New Sec. 2.□(a) For taxable years beginning after December 31, 2011, a taxpayer may elect to take an expense deduction from Kansas ~~taxable~~ income allocated or apportioned to this state for the cost of the

net   before expensing or recapture

net income before expensing or recapture

years remaining in the applicable recovery period for such property as defined under section 168(c) or (g) of the internal revenue code, as amended, after such property is sold or removed from the state including the year of such disposition, and the denominator of which is the total number of years in such applicable recovery period.

(d) The situs of tangible property for purposes of claiming and recapture of the expense deduction shall be the physical location of such property. If such property is mobile, the situs shall be the physical location of the business operations from where such property is used or based. The situs of computer software shall be apportioned to Kansas based on the fraction, the numerator of which is the number of the taxpayer's users located in Kansas of licenses for such computer software used in the active conduct of the taxpayer's business operations, and the denominator of which is the total number of the taxpayer's users of the licenses for such computer software used in the active conduct of the taxpayer's business operations everywhere.

(e) Any member of a unitary group filing a combined report may elect to take an expense deduction pursuant to subsection (a) for an investment in property made by any member of the combined group, provided that the amount calculated pursuant to subsection (a) may only be deducted from the Kansas ~~taxable income~~ allocated to or apportioned to this state by such member making the election.

(f) The following table shall be used in determining the expense deduction calculated pursuant to subsection (a):

	Factors		
IRC§168 Recover Period (year)	**IRC§168(b)(1) Depreciation Method**	**IRC§168(b)(2) Depreciation Method**	**IRC§168(b)(3) or (g) Depreciation Method**
2.5	*	.077	.092
3	.075	.091	.106
3.5	*	.102	.116
4	*	.114	.129
5	.116	.135	.150
6	*	.154	.170
6.5	*	.163	.179
7	.151	.173	.190
7.5	*	.181	.199
8	*	.191	.208
8.5	*	.199	.217
9	*	.208	.226
9.5	*	.216	.235
10	.198	.224	.244
10.5	*	.232	.252
11	*	.240	.261
11.5	*	.248	.269
12	*	.256	.277
12.5	*	.263	.285
13	*	.271	.293

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Implementation of Expensing in Kansas:
A Technical Primer on Governor Brownback's Proposal

Art Hall, Executive Director
Center for Applied Economics, KU School of Business

Submitted to the Senate Committee on Assessment and Taxation
February 15, 2011

Statement of Policy:

Provide to business investors in Kansas the economic value of fully-accelerated depreciation that the federal government tax laws do not provide (but in addition to the economic value provided by federal tax laws for so-called Section 179 property).

The proposed expensing procedure is an option not a requirement. Some taxpayers may choose, for compelling business reasons, to follow federal depreciation procedures only.

Scope

- All business taxpayers shall have an automatic option to expense (immediately write-off for the year placed in service) any eligible investment. The expensing procedure amounts to an additional income tax deduction in Kansas over and above the deductions available for federal income tax purposes.

- The expensing provision applies to any non-real estate investment that can be depreciated for federal income tax purposes.

- There are no restrictions or caps, given the definitions and implementation procedures outlined in the bill.

- Unlimited carry-forward of unused deductions.

- For multi-divisional businesses, the "unitary group" can take the deduction on behalf of investments made by any member of the group.

What is "Expensing"?

- Expensing is a procedure related to the calculation of business income tax. Whenever a business makes a capital investment (whether equipment or structure), it is allowed to take a deduction against income tax for the depreciation of the investment. Expensing is one form of depreciation deduction.

- Expensing is a pro-investment tax policy that does not subsidize businesses. It simply allows them to capture an investment's full time value of money.

- Expensing, properly implemented, is a tax policy that treats *all* businesses equally.

Comparison of Expensing and Tax Credits
Hypothetical Business Operating Solely within Kansas

Assume a $100,000 Investment in 7-Year Property

Federal Depreciation (200% Declining Balance)								
Year	1	2	3	4	5	6	7	8
Dollars	14,290	24,490	17,490	12,490	8,930	8,920	8,930	4,460

Examples:

- Furniture and fixtures for a call center
- Agricultural machinery
- A new natural gas gathering pipeline
- Manufacturing equipment for many industries

		Year 1 Income Tax Calculation: Full Expensing	Brownback Expensing	HPIP Tax Credit
1	Gross Receipts	500,000	500,000	500,000
2	Less: Cost of Goods Sold	310,000	310,000	310,000
3	Less: Federal Depreciation (on above investment)	14,290	14,290	14,290
4	Equals: Net Profit (Federal Taxable Income)	175,710	175,710	175,710
5	Plus: Kansas Additions to Federal Taxable Income	0	0	0
6	Less: Kansas Deductions from Federal Taxable Income	0	0	0
7	Equals: Apportionable Business Income to Kansas	175,710	175,710	175,710
8	Less: Kansas Expensing Deduction	100,000	15,100 *	0
9	Equals: Kansas Taxable Income	75,710	160,610	175,710
10	Kansas Income Tax (at 4% + 3.05% Surtax over $50,000)	3,813	9,798	10,863
11	Less: HPIP Tax Credit (10%)	0	0	5,000
12	Equals: Kansas Tax Liability	3,813	9,798	5,863

* Uses Kansas Adjustment Factor as explained below.

- This example shows the accounting and tax difference related to expensing and the HPIP investment tax credit (which applies to qualifying investments above $50,000).
- For the example, so-called "full expensing" is the most valuable to a taxpayer; HPIP is next. That is because each delivers more than the time value of money—they, in whole or in part, double count the value of the federal depreciation benefits.
- The Brownback proposal achieves the stated policy goal: it shifts only the time value of money to the taxpayer based on the federal depreciation benefits. It improves the expected investment return, but it does not subsidize like "full expensing" or HPIP.

Expected Rate of Return on Identical Hypothetical Investments (7-Year Property, Full Value of Incentive Captured in Year 1)			
	$1 Million Investment	**$100,000 Investment**	**$50,000 Investment**
No Credit or Expensing	9.20%	9.20%	9.20%
Full Expensing (7.05% Tax Rate)	11.19%	11.19%	11.19%
Brownback Expensing (7.05% Tax Rate)	**9.63%**	**9.63%**	**9.63%**
HPIP Investment Tax Credit	11.92%	10.60%	9.20%

- The goal of an investment incentive is to increase the expected return on investment (ROI). The baseline in this example is a 9.20% after tax investment return assuming no credits or deductions.
- No doubt a 10% tax credit increases expected ROI the most, once the investment is large enough to trivialize the $50,000 HPIP threshold.
- Expensing can become more competitive with HPIP if Kansas decides to go to "full expensing." Of course, like HPIP, this subsidizes business rather than removing the tax penalty imposed by fixed depreciation schedules. The higher the discount rate (that is the larger the Kansas Adjustment Factor), the closer ROI will get to "full expensing."
- Expending treats every business equally—regardless of the size of the investment. A stated policy goal.
- HPIP applies to a few dozen companies a year; expensing to tens of thousands—with no permission required. Relative to HPIP, Brownback expensing will help increase the expected rate of return on an addition $6-7 billion of annual investment—in other words, every business, not the several hundred million dollars of investment made by select businesses.

Formulas for Calculating Taxpayer Value	
Full Expensing	Investment Amount x Tax Rate
Brownback Expensing	Investment Amount x Kansas Adjustment Factor x Tax Rate
HPIP Investment Tax Credit	(Qualifying Investment Expenditure - $50,000) x 10%

Additional Examples of Taxpayer Value
(HPIP subsidizes; Brownback Expensing removes tax penalty)

$50,000 Investment

		Taxpayer Value		
Property Class	Expensing Deduction 5% Factor	Corporate Rate 7.05%	Top Individual Rate 6.45%	HPIP
3-Year	3,731	263	241	0
5-Year	5,794	408	374	0
7-Year	7,547	532	487	0
10-Year	9,889	697	638	0

$100,000 Investment

		Taxpayer Value		
Property Class	Expensing Deduction 5% Factor	Corporate Rate 7.05%	Top Individual Rate 6.45%	HPIP
3-Year	7,463	526	481	5,000
5-Year	11,587	817	747	5,000
7-Year	15,095	1,064	974	5,000
10-Year	19,777	1,394	1,276	5,000

$1,000,000 Investment

		Taxpayer Value		
Property Class	Expensing Deduction 5% Factor	Corporate Rate 7.05%	Top Individual Rate 6.45%	HPIP
3-Year	74,629	5,261	4,814	95,000
5-Year	115,874	8,169	7,474	95,000
7-Year	150,946	10,642	9,736	95,000
10-Year	197,772	13,943	12,756	95,000

Implementation: Understanding the Kansas Adjustment Factor

The key—and novel—implementation feature of the proposal relates to the "Kansas Adjustment Factor," which is described in the example below. Kansas, like many states, piggybacks on the procedures in the federal income tax code. This fact makes the implementation of expensing in Kansas slightly more complicated than it would be at the federal level. In brief, it would require a Kansas business tax preparer to spend about 5-10 minutes to perform one additional calculation.

The purpose of the additional calculation is to keep undisturbed the Kansas procedure of using federal taxable income as the starting point for Kansas corporate income tax calculations (and federal adjusted gross income as the starting point for proprietorships, partnerships, and S-Corporations). These starting-point measures of income already have federal depreciation built in.

<u>An Example: Calculating the Kansas Adjustment Factor</u>

- Federal depreciation procedures rely on a set of prescribed rules.
- When a business taxpayer makes a capital investment, the tax preparer must make a decision about (1) how to classify the property for depreciation purposes and (2) what depreciation method to use. Once the tax preparer makes those decisions, all of the details about the depreciation schedule become known.
- The suggested implementation plan for expensing in Kansas relies on the decision that the tax preparer makes for federal depreciation purposes.

Acme Call Centers has a state-of-the-art facility in Hays, Kansas. Acme purchases $500,000 worth of new furniture to expand its call center. The CFO of Acme knows that furniture is classified as a 7-year form of property for federal depreciation purposes. She decides to use the 200% Declining Balance depreciation method (employing the half-year convention).

Acme Call Centers' Federal Depreciation Deduction Schedule								
Year	1	2	3	4	5	6	7	8
Dollars	71,450	122,450	87,450	62,450	44,650	44,600	44,650	22,300

- Kansas expensing amount if there were no federal depreciation rules: $500,000
- Kansas expensing amount under the proposal: <u>$500,000 x 0.151 = $75,500</u>.

The proposal would provide Acme an additional $75,500 income tax deduction—<u>in Year 1 only</u>. That amount captures the time value of money difference between the federal depreciation schedule and the full expensing amount of $500,000.

Where did the 0.151 number come from? Based on the implementation plan, it is a number that will be published as part of the law or published by the Kansas Department of Revenue. A Kansas Adjustment Factor will be published to correspond to each type of property classification and depreciation procedure (which will result in a table that easily fits on one page).

The actual number derives from taking the difference between the investment amount ($500,000, in this case) and the discounted present value of the federal depreciation schedule (years 2-8) using an interest rate of eight percent (5%). Mathematically, the adjustment factor of 0.151 remains invariant for any investment in 7-year property that a taxpayer depreciates using the 200% Declining Balance method under the half-year convention.

The same procedure used in the Acme Call Centers example would apply for any investment made in Kansas. Different adjustment factors would apply to the several different combinations of property classifications and depreciation methods available to taxpayers under the federal tax rules.

Derivation of the Kansas Adjustment Factor for the Acme Example

The property has a 7-year classification, but the schedule actually has 8 installments.

Present Value of Federal Depreciation Schedule (at 5% rate of interest, Year 1 not discounted):

$$424{,}500 = \frac{71{,}450}{(1.0)^1} + \frac{122{,}450}{(1.05)^2} + \frac{87{,}450}{(1.05)^3} + \frac{62{,}450}{(1.05)^4} + \frac{44{,}650}{(1.05)^5} + \frac{44{,}600}{(1.05)^6} + \frac{44{,}650}{(1.05)^7} + \frac{22{,}300}{(1.05)^8}$$

Difference between Full Investment Amount and Present Value:
$500,000 – $424,500 = $75,500

Calculation of Kansas Adjustment Factor (Invariant to Investment Size):
$75,500 ÷ $500,000 = 0.151

Adjustment Procedures Related to Federal Rules for Accelerated ("Bonus") Depreciation

- The implementation goal of the proposal is to allow Kansas expensing to "flex" with changes in federal law to maintain the Kansas policy goal stated above.
- Two categories of federal law interact with each other and the Kansas proposal: Section 179 of the IRS code and bonus depreciation.
- The following example uses the law as embodied in the Small Business and Jobs Act (Sept. 27, 2010)—and extrapolates to the federal expensing provision expected to be law for 2012:
    - Section 179 ("small business" expensing). In tax years 2010 and 2011, companies can expense up to $500,000 of qualifying property, as long as the purchase price does not exceed $2 million. For every dollar a price tag exceeds $2 million, the allowable expensing amount drops by one dollar. So, an investment of $2.5 million and over may not expense under Section 179. (These threshold amounts are likely to drop after 2011.)

- For 2010, qualifying investments can take so-called "bonus depreciation." The rules for 2010 allow for 50% bonus depreciation. The bonus depreciation rules can be combined with Section 179 rules. (New federal law for 2011 will likely allow 100% rather than 50% bonus depreciation.)

The table below shows the general formula for Kansas expensing proposal as it interacts with the two federal procedures (assuming the same property classification characteristics as the Acme example, but different investment outlays).

Investment Amount	Allowable Sec. 179 Expensing	Allowable Bonus 50% Depreciation	Brownback Expensing Expensing Formula with 50% Bonus Depreciation
500,000	500,000	-	500,000 x 0.151 = 75,500
2,000,000	500,000	750,000	(2,000,000 - 750,000) x 0.151 = 188,750
2,500,000	0	1,250,000	(2,500,000 - 1,250,000) x 0.151 = 188,750
5,000,000	0	2,500,000	(5,000,000 - 2,500,000) x 0.151 = 377,500

- The Kansas proposal makes no adjustment for Section 179, but does make an adjustment for bonus depreciation rules.
- With 50% bonus depreciation, Kansas would still offer value to the investor greater than what the federal rules allow: the stated policy goal of providing the economic value of 100% accelerated depreciation.
- With federal 100% bonus depreciation (as is expected for the tax year 2011 only), Kansas expensing would be eliminated for investments too large for Section 179 rules (per the policy intent) but would automatically renew when the federal rules expire or revert.

Testimony before the Senate Assessment & Taxation Committee
SB 196 – High Performance Incentive Program & Expensing
Presented by J. Kent Eckles, Vice President of Government Affairs

achieve more

Wednesday, February 16th, 2011

The Kansas Chamber of Commerce appreciates the opportunity to present testimony in favor of Senate Bill 196, which would make modifications to the High Performance Incentive Program (HPIP), allow for expensing of capital investments and establish an up-front "deal closing" cash incentives fund.

The Kansas Chamber and its members have spent many hours with the administration working to revise their original proposal and are appreciative they listened to our concerns to produce the workable compromise for which we are here today.

The Chamber has long been in favor of simplifying and adding flexibility to HPIP and has supported allowing expensing of capital investments as a way to spur investment and job creation in Kansas. It is important to note that our members have not advocated for an "either or" approach to both incentives, rather they would like to have both coexist, thus allowing companies to choose the option that best suits their business model and investment schedule.

With regard to HPIP, many of our members and economic development partners believe this is one of the State's most valuable incentives. The program represents a 10% investment tax credit to be claimed against a company's tax liability and until we can eliminate the corporate income tax in Kansas, maintaining this program is essential. It is precisely because our corporate tax rates are too high that we have to have such incentives in the first place. Finally, we believe the 5-year sunset for HPIP contained in SB 196 is a reasonable provision so this committee and the legislature can determine the program's return on investment in 2017.

Expensing of capital investments is a pro-growth policy that promotes capital spending and is a relatively inexpensive option for the State because the only cost to the government is the time value of money. Economists have rated expensing of capital investment as one of the most economically productive of economic stimulus initiatives. University of Connecticut Economics Professor Arthur Wright has recommended the Obama Administration allow firms to expense all investment outlays, saying there is "substantial empirical evidence that accelerated depreciation…..boost[s] corporate investment" in new business assets. During the past 60 years, the correlation between employment and capital-spending growth has averaged 0.86 (with 1.0 being perfect correlation). Since 1949 there have only been five quarters that experienced year-on-year private sector employment gains without growth in business investment.

While some of our members have expressed concerns with the bill's provision to eliminate the business machinery & property tax credit to make the expensing provisions revenue neutral, it's important to note that this bill does away with a program that provides a property tax credit for investment decisions made seven or more years ago in favor expensing, which rewards future investment and job creation on a permanent basis.

Another very important provision to this bill is the elimination of the Investments in Major Projects & Comprehensive Training (IMPACT) Fund and replacement of it with an up-front, cash-based "deal closing" fund. For many years, the legislature and this very committee have heard the Kansas Chamber talk about the need to move towards up-front cash incentives and away from the "credit card" approach to economic development. This measure does exactly that by ridding the state of a bond funded program (IMPACT) that in any given year has over half of its funds committed to debt service as opposed to actual projects. Moving away from IMPACT and to a deal closing fund will also enable the legislature to avoid doing company-specific legislation on an annual basis, which is obviously not good public policy.

Finally, there are three provisions contained in House Bill 2051, which we urge the committee to include in this bill when you work it in committee, specifically; allowing a corporation with multiple unitary groups to apply existing HPIP credits against the tax liability of any member or members of its unitary group in their combined tax report; extending from 10 to 20 years the deadline for corporations to claim existing HPIP investment tax credits; eliminating the requirement that a company attains recertification before utilizing the tax credits.

Allowing HPIP to be claimed against a company's unitary groups is consistent with the underlying bill since the measure proposes to allow expensing for a company's various unitary groups on their combined tax report apportioned to Kansas.

We urge the Committee to pass SB 196.

The Kansas Chamber, with headquarters in Topeka, Kansas, is the leading statewide pro-business advocacy group moving Kansas towards becoming the best state in America to live and work. The Chamber represents small, medium, and large employers all across Kansas. Please contact me directly if you have any questions regarding this testimony.

THE KANSAS CHAMBER

835 SW Topeka Blvd. Topeka, KS 66612 785.357.6321

Overland Park
Chamber of Commerce

Written Testimony in Support of Senate Bill 196

Submitted by Jennifer Bruning
On behalf of the Overland Park Chamber of Commerce

Senate Assessment & Taxation Committee
Wednesday, February 16, 2011

Chairman Donovan and Committee Members:

My name is Jennifer Bruning, and I am Vice President of Government Affairs with the Overland Park Chamber of Commerce. I am here today on behalf of our Board of Directors and our nearly 1,000 member companies. I appreciate the opportunity to testify as a proponent of Senate Bill 196, which contains several key components of Governor Brownback's strategic economic development plan.

HPIP

Historically the HPIP program has been an important part of Kansas' economic development toolbox, offering employers that pay above-average wages and demonstrate strong commitment to skills development for their workers a 10 percent income tax credit for eligible capital investment in their facility exceeding a certain threshold. We commend Governor Brownback and Secretaries Jordan and George for listening to the business community when we expressed our concern over the proposed immediate elimination of the HPIP program, and we further appreciate their willingness to modify their plan to allow companies with active HPIP certified projects to be grandfathered under the program's current rules and regulations.

While the HPIP program has been characterized as catering only to large businesses, a review of HPIP certifications over the last two years shows that approximately 64 percent of companies utilizing the credit have fewer than 100 employees. Interestingly, the proposed changes to raise the investment threshold from $50,000 to $5 million would likely make the program even more exclusive to large business, which would presumably conflict with the Governor's stated goal to provide incentives that assist a broad spectrum of businesses. An analysis of HPIP project applications received since January 1, 2009 shows that only 150 (18%) of the proposed projects out of 856 applications would have qualified for HPIP under the $5 million threshold.

We have reservation about the proposed five-year sunset provision. We hope the Legislature understands that companies seeking to relocate to a new state or make a large capital investment require certainty and longevity in the incentive proposals being offered to them, and any ambiguity in an offer will lead to Kansas losing out on job creation opportunities. This does not mean we do not think incentives such as HPIP should be consistently reviewed to ensure the programs are working effectively

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Attachment # 5

and projects are materializing as projected. We suggest inserting a five-year HPIP review process and potential renewal provision in lieu of the sunset stipulation.

Furthermore, we ask the Legislature to consider adding the provisions of House Bill 2051 to this bill, which would extend the carry-forward period of HPIP credits previously awarded to certified companies from ten years to twenty years and allow for unitary groups to claim the credits. Several Overland Park Chamber members and area businesses have been awarded HPIP tax credits in the last 10 years and have cited access to these credits as one of the key positive factors in their decision-making process to locate their facility in Kansas or expand their current facility. Because of our current economic climate, these companies have been unable to utilize the credit before the 10-year expiration date, meaning that under current law they will lose the benefits of the program. Should the carry-forward period be extended to 20 years and should unitary groups be allowed to use the credits, it would allow these Kansas companies to come out of this dark economic period with a stronger and more competitive fiscal outlook, thus encouraging these employers to hire more private sector employees and gradually lead to more capital investment in facilities, technology and employee training and education.

Expensing

The expensing proposal in SB 196, a form of depreciation deduction, allows Kansas businesses who make a capital investment to take a deduction against state income tax for the depreciation of the investment and allows for an immediate deduction of the full investment amount instead of requiring a prescribed schedule of smaller deductions over multiple years.

Because of the limited time period between receiving a copy of the full bill and today's hearing, we were unable to get substantive feedback from our member companies as to how this expensing proposal would affect their businesses. However, we deem additional tax options for businesses to be desirable, but whether these options are actually an incentive to create jobs is unclear.

Machinery & Equipment Property Tax Credit

In 2006, the Legislature exempted property taxes on all newly acquired machinery and equipment purchased after July 1, 2006. The 25 percent refundable machinery & equipment tax credit, which SB 196 proposes to eliminate, was instituted at that time to be used by those businesses with older equipment (purchased before 2006) still on the tax rolls. The companies utilizing this credit are the companies who with the current state of the economy cannot afford new business equipment, especially since the recession has limited their ability to acquire small business loans. If in fact the company does not have enough tax liability to utilize the credit, the State issues the company a check for the difference between the tax liability amount and the credit amount (refundability). Should this tax credit be eliminated, it will mean higher tax bills for many businesses at a time where they are already stretched to their limits.

Job Creation Fund

We have testified numerous times in the past about the need in our state for a "deal closer" fund which allows the Department of Commerce and the economic developers in communities across Kansas the flexibility to provide upfront cash to help close economic development deals. We do believe this contingency fund will strengthen our economic development arsenal, but subjecting a fund such as this to the yearly appropriations process – where targeted funds routinely get swept into the state general fund - is worrisome. We urge the Legislature to recognize the need for the certainty of the fund to create jobs.

SB 196 includes many good provisions that will enhance business-sector productivity and help grow the Kansas economy. We urge the Committee to consider some of our suggestions that we feel will even further boost the potential for economic prosperity in our state including the elimination of the HPIP sunset provision and the inclusion of the contents of HB 2051. Thank you for your consideration.

Greater Topeka
CHAMBER & GO TOPEKA

Testimony: SB 196 – Expensing, HPIP and other tax credits
Senate Assessment and Taxation Committee
February 16, 2011
By: Christy Caldwell, Vice President Government Relations
Greater Topeka Chamber of Commerce
ccaldwell@topekachamber.org

Mr. Chair and members of the committee:

The Topeka Chamber would like to take this opportunity to express our appreciation to Governor Brownback and Secretaries George and Jordan. Together they are working to place a high priority on economic recovery in our state. Our chamber continues to work to attract expansions of local companies and attract new investment and jobs in our community. We benefit from the partnership the administration and legislature provides.

SB 196 has a number of elements; I would like to address four of them:

- First, the Governor in his economic strategic plan has proposed the concept of **Expensing** capital investment by Kansas companies. This is an idea which has garnered favor from companies in the state who are considering purchases of new equipment. Such investments are good for our economy; they demonstrate a strengthening of business which sometimes will lead to growth in the number of jobs companies are able to create. This method of calculating taxes may be a tool that will encourage growth. Our chamber accepts this recommendation as one that companies can elect to participate in to improve their cash flow. The state will not lose tax dollars over time, allowing the immediate benefit expensing provides during the time the business places the investment in service.

- Originally the administration's proposed strategy included the elimination of the **High Performance Incentive Program (HPIP)**. There were numerous concerns raised by the removal of one of the state's premier incentives that has been quite effective in drawing investment and jobs to Kansas. In this bill, the administration altered its proposal to continue access to HPIP for five years, when at that time it will be re-evaluated. The Topeka Chamber appreciates the importance the Governor and both Secretaries have been in assuring Kansas remains vigilant in responding to the economic development front line. In Topeka/Shawnee County we have been very fortunate during this recession to have companies such as Frito Lay, Goodyear, Jostens, Hills, Payless Shoes, Del Monte, PTMW and the new Bimbo Bakeries plant, that is currently under construction, bring new capital investment and jobs here in our community through partnering with Kansas and the Topeka/Shawnee County community. HPIP has been a tool that has helped attract such investment; we do not want to jeopardize this effective state incentive. We would suggest making HPIP stronger by adding language from HB 2051 regarding the length of time credits, companies earned with prior investments, can be utilized and allowing credits to be used by a unitary group.

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Although we support the provisions regarding HPIP in this bill, we do want to share our concerns that the increase in the threshold may be problematic for small business who would also like to access HPIP when considering investing dollars and creating jobs in Kansas. Approximately 64% of HPIP users have been businesses with 100 employees or less. With the threshold changing in 2012 from $50,000 to $5 million it is unlikely most small businesses will be able to meet that level of investment. Currently, according to the Department of Commerce, about 80% of the investments are below the $5 million threshold.

- The proposal also includes adding a new **Job Creation Program Fund** which will eventually replace the IMPACT program now available. We like the idea of having a fund that can be utilized when there needs to be just a little more push to convince a company to expand or locate in Kansas. This is a tool that is used in many states with success. Here in Topeka/Shawnee County the citizens decided that was an effective tool as well; they voted a sales tax on themselves, several years ago, to provide funds to assist in drawing new investment and jobs to our community and it has been quite successful in our economic development efforts. We agree Kansas would benefit from such a fund.

- However we do have reservations with one of the tax credits that stands to be eliminated with the adoption of this bill, the refundable **Machinery and Equipment (M&E) Property Tax Credit**. Prior to action taken in 2006, the M&E property tax was excessive and resulted companies making little investment in upgrading their equipment. Governor Graves and the Legislature phased in the 25% M&E property tax credit to offset the high property taxes. That tax credit has remained in effect and given relief to all businesses for the amount of property tax they pay on M&E purchased prior to 2006.

  By eliminating this tax credit, businesses in Kansas will see a $37 million tax increase that will continue from year to year, although growing smaller each year as new equipment is placed in service. The impact of this tax will hit small businesses the hardest. We are very concerned for those businesses that cannot afford to buy new equipment and are still hanging on in a tough economy. These companies will lose out with the elimination of this tax credit. <u>We would suggest consideration be given to, allowing businesses an option of continuation of the M&E tax credit or the use of Expensing.</u> Thereby, allowing businesses to make decisions considering what will help them the most.

We can agree with the remainder of the bill as it deals with IMPACT and other tax credit programs.

Thank you for your time and focus on moving our state out of the recession by providing the tools necessary to encourage capital investments and jobs in Kansas.

Lenexa
Chamber of Commerce

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TO: Senator Les Donovan, Chair
Senator Pat Apple, Vice-Chair
Members, Senate Taxation Committee

FROM: Blake Schreck, President
Lenexa Chamber of Commerce

DATE: February 16, 2011

RE: **Testimony on Behalf of SB 196**

The Lenexa Chamber of Commerce appreciates the opportunity to express its views on Senate Bill 196, which is intended to promote statewide economic growth and provide economic development tools that are more efficient, flexible, and competitive.

Incentives and tax policy that allow Kansas to compete across the country and around the world are crucial to our ability to grow the state's economy. The advantages the state has provided have attracted and retained significant jobs, capital investment, and tax base in Kansas. Economic development is dynamic, however, and competition for projects is increasingly aggressive. Unless a state continues to evolve its efforts, it will rapidly lose ground in its ability to attract and retain projects.

For that reason, we are pleased the state is continuing to explore how it can improve its tax policy and economic development framework, and we support a number of the goals represented in SB 196 including seeding a more competitive "deal-closing" fund and looking for additional means to assist and encourage all of our existing companies. While the bill's specific proposals must be carefully and comprehensively considered to ensure they will achieve their intended purpose, we believe at its heart this legislation opens a critical discussion into new and creative ways the state may better foster a healthy and growing statewide economy.

Thank you very much for your time and consideration of these important business issues.

Implementation of Expensing in Kansas:
A Technical Primer on Governor Brownback's Proposal

Art Hall, Executive Director
Center for Applied Economics, KU School of Business

Submitted to the Senate Committee on Assessment and Taxation
February 15, 2011

Statement of Policy:

Provide to business investors in Kansas the economic value of fully-accelerated depreciation that the federal government tax laws do not provide (but in addition to the economic value provided by federal tax laws for so-called Section 179 property).

The proposed expensing procedure is an option not a requirement. Some taxpayers may choose, for compelling business reasons, to follow federal depreciation procedures only.

Scope

- All business taxpayers shall have an automatic option to expense (immediately write-off for the year placed in service) any eligible investment. The expensing procedure amounts to an additional income tax deduction in Kansas over and above the deductions available for federal income tax purposes.
- The expensing provision applies to any non-real estate investment that can be depreciated for federal income tax purposes.
- There are no restrictions or caps, given the definitions and implementation procedures outlined in the bill.
- Unlimited carry-forward of unused deductions.
- For multi-divisional businesses, the "unitary group" can take the deduction on behalf of investments made by any member of the group.

What is "Expensing"?

- Expensing is a procedure related to the calculation of business income tax. Whenever a business makes a capital investment (whether equipment or structure), it is allowed to take a deduction against income tax for the depreciation of the investment. Expensing is one form of depreciation deduction.
- Expensing is a pro-investment tax policy that does not subsidize businesses. It simply allows them to capture an investment's full time value of money.
- Expensing, properly implemented, is a tax policy that treats *all* businesses equally.

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Comparison of Expensing and Tax Credits
Hypothetical Business Operating Solely within Kansas

Assume a $100,000 Investment in 7-Year Property

Federal Depreciation (200% Declining Balance)								
Year	1	2	3	4	5	6	7	8
Dollars	14,290	24,490	17,490	12,490	8,930	8,920	8,930	4,460

Examples:

- Furniture and fixtures for a call center
- Agricultural machinery
- A new natural gas gathering pipeline
- Manufacturing equipment for many industries

		Year 1 Income Tax Calculation		
		Full Expensing	**Brownback Expensing**	**HPIP Tax Credit**
1	Gross Receipts	500,000	500,000	500,000
2	Less: Cost of Goods Sold	310,000	310,000	310,000
3	Less: Federal Depreciation (on above investment)	14,290	14,290	14,290
4	Equals: Net Profit (Federal Taxable Income)	175,710	175,710	175,710
5	Plus: Kansas Additions to Federal Taxable Income	0	0	0
6	Less: Kansas Deductions from Federal Taxable Income	0	0	0
7	Equals: Apportionable Business Income to Kansas	175,710	175,710	175,710
8	Less: Kansas Expensing Deduction	100,000	15,100 *	0
9	Equals: Kansas Taxable Income	75,710	160,610	175,710
10	Kansas Income Tax (at 4% + 3.05% Surtax over $50,000)	3,813	9,798	10,863
11	Less: HPIP Tax Credit (10%)	0	0	5,000
12	Equals: Kansas Tax Liability	3,813	9,798	5,863

* Uses Kansas Adjustment Factor as explained below.

- This example shows the accounting and tax difference related to expensing and the HPIP investment tax credit (which applies to qualifying investments above $50,000).
- For the example, so-called "full expensing" is the most valuable to a taxpayer; HPIP is next. That is because each delivers more than the time value of money—they, in whole or in part, double count the value of the federal depreciation benefits.
- The Brownback proposal achieves the stated policy goal: it shifts only the time value of money to the taxpayer based on the federal depreciation benefits. It improves the expected investment return, but it does not subsidize like "full expensing" or HPIP.

Expected Rate of Return on Identical Hypothetical Investments (7-Year Property, Full Value of Incentive Captured in Year 1)			
	$1 Million Investment	**$100,000 Investment**	**$50,000 Investment**
No Credit or Expensing	9.20%	9.20%	9.20%
Full Expensing (7.05% Tax Rate)	11.19%	11.19%	11.19%
Brownback Expensing (7.05% Tax Rate)	**9.63%**	**9.63%**	**9.63%**
HPIP Investment Tax Credit	11.92%	10.60%	9.20%

- The goal of an investment incentive is to increase the expected return on investment (ROI). The baseline in this example is a 9.20% after tax investment return assuming no credits or deductions.
- No doubt a 10% tax credit increases expected ROI the most, once the investment is large enough to trivialize the $50,000 HPIP threshold.
- Expensing can become more competitive with HPIP if Kansas decides to go to "full expensing." Of course, like HPIP, this subsidizes business rather than removing the tax penalty imposed by fixed depreciation schedules. The higher the discount rate (that is the larger the Kansas Adjustment Factor), the closer ROI will get to "full expensing."
- Expending treats every business equally—regardless of the size of the investment. A stated policy goal.
- HPIP applies to a few dozen companies a year; expensing to tens of thousands—with no permission required. Relative to HPIP, Brownback expensing will help increase the expected rate of return on an addition $6-7 billion of annual investment—in other words, every business, not the several hundred million dollars of investment made by select businesses.

Formulas for Calculating Taxpayer Value	
Full Expensing	Investment Amount x Tax Rate
Brownback Expensing	Investment Amount x Kansas Adjustment Factor x Tax Rate
HPIP Investment Tax Credit	(Qualifying Investment Expenditure - $50,000) x 10%

Additional Examples of Taxpayer Value
(HPIP subsidizes; Brownback Expensing removes tax penalty)

$50,000 Investment

Property Class	Expensing Deduction 5% Factor	Taxpayer Value: Corporate Rate 7.05%	Top Individual Rate 6.45%	HPIP
3-Year	3,731	263	241	0
5-Year	5,794	408	374	0
7-Year	7,547	532	487	0
10-Year	9,889	697	638	0

$100,000 Investment

Property Class	Expensing Deduction 5% Factor	Taxpayer Value: Corporate Rate 7.05%	Top Individual Rate 6.45%	HPIP
3-Year	7,463	526	481	5,000
5-Year	11,587	817	747	5,000
7-Year	15,095	1,064	974	5,000
10-Year	19,777	1,394	1,276	5,000

$1,000,000 Investment

Property Class	Expensing Deduction 5% Factor	Taxpayer Value: Corporate Rate 7.05%	Top Individual Rate 6.45%	HPIP
3-Year	74,629	5,261	4,814	95,000
5-Year	115,874	8,169	7,474	95,000
7-Year	150,946	10,642	9,736	95,000
10-Year	197,772	13,943	12,756	95,000

Implementation: Understanding the Kansas Adjustment Factor

The key—and novel—implementation feature of the proposal relates to the "Kansas Adjustment Factor," which is described in the example below. Kansas, like many states, piggybacks on the procedures in the federal income tax code. This fact makes the implementation of expensing in Kansas slightly more complicated than it would be at the federal level. In brief, it would require a Kansas business tax preparer to spend about 5-10 minutes to perform one additional calculation.

The purpose of the additional calculation is to keep undisturbed the Kansas procedure of using federal taxable income as the starting point for Kansas corporate income tax calculations (and federal adjusted gross income as the starting point for proprietorships, partnerships, and S-Corporations). These starting-point measures of income already have federal depreciation built in.

An Example: Calculating the Kansas Adjustment Factor

- Federal depreciation procedures rely on a set of prescribed rules.
- When a business taxpayer makes a capital investment, the tax preparer must make a decision about (1) how to classify the property for depreciation purposes and (2) what depreciation method to use. Once the tax preparer makes those decisions, all of the details about the depreciation schedule become known.
- The suggested implementation plan for expensing in Kansas relies on the decision that the tax preparer makes for federal depreciation purposes.

Acme Call Centers has a state-of-the-art facility in Hays, Kansas. Acme purchases $500,000 worth of new furniture to expand its call center. The CFO of Acme knows that furniture is classified as a 7-year form of property for federal depreciation purposes. She decides to use the 200% Declining Balance depreciation method (employing the half-year convention).

Acme Call Centers' Federal Depreciation Deduction Schedule								
Year	1	2	3	4	5	6	7	8
Dollars	71,450	122,450	87,450	62,450	44,650	44,600	44,650	22,300

- Kansas expensing amount if there were no federal depreciation rules: $500,000
- Kansas expensing amount under the proposal: $500,000 x 0.151 = $75,500.

The proposal would provide Acme an additional $75,500 income tax deduction—in Year 1 only. That amount captures the time value of money difference between the federal depreciation schedule and the full expensing amount of $500,000.

Where did the 0.151 number come from? Based on the implementation plan, it is a number that will be published as part of the law or published by the Kansas Department of Revenue. A Kansas Adjustment Factor will be published to correspond to each type of property classification and depreciation procedure (which will result in a table that easily fits on one page).

The actual number derives from taking the difference between the investment amount ($500,000, in this case) and the discounted present value of the federal depreciation schedule (years 2-8) using an interest rate of eight percent (5%). Mathematically, the adjustment factor of 0.151 remains invariant for any investment in 7-year property that a taxpayer depreciates using the 200% Declining Balance method under the half-year convention.

The same procedure used in the Acme Call Centers example would apply for any investment made in Kansas. Different adjustment factors would apply to the several different combinations of property classifications and depreciation methods available to taxpayers under the federal tax rules.

Derivation of the Kansas Adjustment Factor for the Acme Example

The property has a 7-year classification, but the schedule actually has 8 installments.

Present Value of Federal Depreciation Schedule (at 5% rate of interest, Year 1 not discounted):

$$424{,}500 = \frac{71{,}450}{(1.0)^1} + \frac{122{,}450}{(1.05)^2} + \frac{87{,}450}{(1.05)^3} + \frac{62{,}450}{(1.05)^4} + \frac{44{,}650}{(1.05)^5} + \frac{44{,}600}{(1.05)^6} + \frac{44{,}650}{(1.05)^7} + \frac{22{,}300}{(1.05)^8}$$

Difference between Full Investment Amount and Present Value:
$500,000 – $424,500 = $75,500

Calculation of Kansas Adjustment Factor (Invariant to Investment Size):
$75,500 ÷ $500,000 = 0.151

Adjustment Procedures Related to Federal Rules for Accelerated ("Bonus") Depreciation

- The implementation goal of the proposal is to allow Kansas expensing to "flex" with changes in federal law to maintain the Kansas policy goal stated above.
- Two categories of federal law interact with each other and the Kansas proposal: Section 179 of the IRS code and bonus depreciation.
- The following example uses the law as embodied in the Small Business and Jobs Act (Sept. 27, 2010)—and extrapolates to the federal expensing provision expected to be law for 2012:
    - Section 179 ("small business" expensing). In tax years 2010 and 2011, companies can expense up to $500,000 of qualifying property, as long as the purchase price does not exceed $2 million. For every dollar a price tag exceeds $2 million, the allowable expensing amount drops by one dollar. So, an investment of $2.5 million and over may not expense under Section 179. (These threshold amounts are likely to drop after 2011.)

- For 2010, qualifying investments can take so-called "bonus depreciation." The rules for 2010 allow for 50% bonus depreciation. The bonus depreciation rules can be combined with Section 179 rules. (New federal law for 2011 will likely allow 100% rather than 50% bonus depreciation.)

The table below shows the general formula for Kansas expensing proposal as it interacts with the two federal procedures (assuming the same property classification characteristics as the Acme example, but different investment outlays).

Investment Amount	Allowable Sec. 179 Expensing	Allowable Bonus 50% Depreciation	Brownback Expensing Expensing Formula with 50% Bonus Depreciation
500,000	500,000	-	500,000 x 0.151 = 75,500
2,000,000	500,000	750,000	(2,000,000 - 750,000) x 0.151 = 188,750
2,500,000	0	1,250,000	(2,500,000 - 1,250,000) x 0.151 = 188,750
5,000,000	0	2,500,000	(5,000,000 - 2,500,000) x 0.151 = 377,500

- The Kansas proposal makes no adjustment for Section 179, but does make an adjustment for bonus depreciation rules.
- With 50% bonus depreciation, Kansas would still offer value to the investor greater than what the federal rules allow: the stated policy goal of providing the economic value of 100% accelerated depreciation.
- With federal 100% bonus depreciation (as is expected for the tax year 2011 only), Kansas expensing would be eliminated for investments too large for Section 179 rules (per the policy intent) but would automatically renew when the federal rules expire or revert.

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Senate Taxation Committee Testimony re: SB 196 - February 16, 2011

Chairman Donovan and other committee members; I am Dennis Lauver, President & CEO of the Salina Area Chamber of Commerce.

I provided detailed information about the SB 196 and its provisions to a number of Salina area employers.

Here is a summary of the five general responses I received:

1. **The HPIP program is effective and is valued.** *A move to simplify the program is welcome. However, the other proposed changes will reduce its utility.*

- A 1,000 employee manufacturer headquartered in Salina with a global customer based observed they have used the HPIP credit for many years to allow them to continue to invest in their multiple Kansas manufacturing facilities. If they do not make their products more efficiently each year, they run the risk of losing out to an increasing overseas competition. Raising the threshold from $50,000 to $5,000,000 will effectively eliminate this tool for them and many Kansas businesses. They told me "If you truly believe that our best growth is going to be from existing business then the threshold needs to allow existing Kansas medium and small business a chance to participate in the credit. We cannot imagine that many Salina employers will be able to use HPIP at the new proposed investment level. We understand that money must come from somewhere, but perhaps there is a more moderate middle ground that still recognizes the need to encourage growth." Instead of increasing the threshold 100 times, perhaps a more 10 times increase is appropriate.

- A Salina firm has used HPIP to expand and help increase employment from 30 to 140 people. The new HPIP proposal advocates a five million dollar expansion minimum. Only one of recent expansions would have qualified at that level because they expanded in several smaller additions and machinery acquisitions. 100 percent of the $1,700,000 dollars of Kansas Income tax saved by the firm thru HPIP was put on their shop floor. The owner said "I cannot stress enough how important this program is to us and my sincere appreciation to the State of Kansas for implementing this program *in its current condition*. We have expanded from one industrial laser to twelve, the cost of each ranging from $500,000 to $1,200,000, we have added 210,000 sq foot of warehouse and manufacturing space from approximately 40,000 sq foot."

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Another business owner predicted that: "A five million dollar threshold will eliminate many from utilizing the program. HPIP negates some of the risk we take as business owners with these expansions and helps us pay our investment off quicker resulting in competitive advantage against our regional competitors in nearby states. We are an S Corp and there is a huge difference between a tax credit and a deduction. Furthermore, when income is 70% off, a deduction is not really that valuable. A tax credit, that helps offset Kansas tax, frees up limited cash to help pay my capital expansion loan makes a big difference to me."

2. **Making the state more neutral in decision making is a great idea**

- A formula driven approach provides more predictability to programs and helps decision makers better evaluate the advantages of operating in Kansas.

3. **A cash based program will be a very effective tool that will stimulate jobs and capital investment**.

- More and more, cash is the most attractive option at the end of the process of recruiting growth.

4. **Eliminating the sales tax exemption will stunt growth**

- A 500 employee manufacturer responded: "We would hate to lose the sales tax exemption on major capital projects as proposed by the change because this would influence investment decisions."

5. **There is a sense the deduction expensing concept will disproportionally help very large employers and may have limited impact**

- A capital intensive 80 employee manufacturer with corporate headquarters in Salina. This firm ships internationally, primarily to Africa, South America and China. They said: "An accelerated depreciation at the state level would not be a significant influence on our investment decisions."
- A 500 employee multinational firm that has recently consolidated operations from multiple states and three nations to their Salina operations notes the expensing concept: "would have a significant impact on the company (a large multinational firm) but won't impact the plant at all.

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- One business owner (135 employees) observed that "if this change encourages existing business to re-invest in itself and/or new businesses to look at Kansas as a 'friendly' then I would support it. However if it can result in larger companies that tend to reinvest at much higher levels to leverage it into an advantage over smaller competitors I would not support it. Suffice to say, this change would need to assure a level playing field for all companies it would serve. I don't think it will influence small businesses in their decision to come to Kansas. It may affect the large corporations

Overall, I think there is a positive intent to the bill. However, I'm concerned enough about unintended consequences, that I encourage some additional changes. Therefore, at this point, we are neutral on the bill…*and I'm really anxious to be in a position where we can aggressively support SB 196.*

General observations about tax policy and economic development

I lifted the following directly from a Fox News story earlier this week. I think it is relevant to this discussion.

> It's recently become an article of faith for many governors as they try to attract jobs: raising taxes during a recession is a nonstarter, choking off growth and damaging a state's fragile economic
>
> But there's a catch to the anti-tax, pro-business rhetoric: Businesses consider a range of factors when deciding where to locate, including the quality of schools, roads and programs that rely on a certain level of public spending and regulation. And evidence suggests there is little correlation between a state's tax rate and its overall economic health.
>
> "Concerns about taxes are overstated," said Matt Murray, a professor of economics at the University of Tennessee who studies state finance. "Labor costs, K-12 education and infrastructure availability are all part of a good business climate. And you can't have those without some degree of taxation."
>
> States' tax rates also do not predict their resilience during an economic downturn. While high-tax states such as New York, New Jersey and California have been clobbered by the current recession, so too have states that pride themselves on low tax rates, including Nevada, Texas and Arizona.

February 16, 2011

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SB 196
Testimony Before the Senate Committee on Taxation
Gary C. Allerheiligen, CPA, Immediate Past President

Chairman Carlson and Members of the Committee:

I am Gary Allerheiligen, Immediate Past President of the Kansas Society of CPA's (KSCPA). We have 2,600 members in the state of Kansas in public accounting, business, industry, government, and education.

We are here today to offer our expertise in answering questions of the committee about how SB 196 might impact the businesses CPAs serve. Our leadership reviewed the proposed legislation and met by conference call. After much discussion, the position of the KSCPA leadership on this bill is currently neutral.

Our concerns with the proposed legislation includes:

1. The potential complexity of implementing the expensing provision.
2. The combination of the change in the HPIP credit and the expensing provision in the same legislation.
3. The substantial jump from $50,000 to $5 million investment to receive the HPIP credit, even with a 2-year "pipeline."
4. The discontinuation of the Business & Jobs Development Credit will negatively impact small businesses.

Our recommendations are:

1. Reduce the HPIP threshold and use a tiered approach to phasing in this change.
2. Classify any unused expense not taken in the current year as a Net Operating Loss carry forward rather than as a deduction, which would reduce some of the complexity.
3. New Section 2 should clarify how schedule f tables will be applied in the event the section 179 election has been made.

Thank you for your time and I will be happy to answer any questions.

Sn. Assmnt & Tax
2-16-11
Attachment # 10

Kansas Economic Progress Council
Suite 200
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Topeka, Kansas 66603

Testimony on SB 196
Senate Assessment and Taxation Committee
Testimony on HB 2317
House Taxation Committee
February 16, 2011

Mr. Chairman and members of the committee, thank you for the opportunity to appear on this legislation. I'm Bernie Koch with the Kansas Economic Progress Council, a statewide not for profit organization of businesses, trade associations, and chambers of commerce. We support pro-growth policies for communities and the state.

We decided to testify as neutral because there are things we like in this bill, and things that concern us. It is a very wide-ranging bill. Normally, with so many adjustments in major economic development programs, we would urge you to move slowly and carefully, so that we get any changes right. However, we recognize that we need to do whatever we can as soon as we can to get Kansas back to work.

The Governor has proposed allowing businesses to deduct their full investment in equipment or structure in one year instead of a prescribed schedule of smaller deductions over several years. We believe this is a positive because it gives business some options.

We are pleased that the administration has modified its position about the High Performance Incentive Program. This is clearly an important program for many businesses who want to expand. Like other conferees, we are concerned that limiting who qualifies for this program cuts out small businesses from its use. We urge you to continue to explore this area.

We strongly support a "deal closer" fund. I understand the amount currently available for this in Kansas is about $1.4 million. The State of Texas has a $295 million deal closing fund, the largest in the country. Governor Mary Fallin in Oklahoma has said she wants to create an Oklahoma fund similar to what Texas has. We need this tool.

The machinery and equipment property tax credit is a program I am very familiar with. In my 21 years lobbying the Kansas Legislature, I have spent more time testifying about the importance of machinery and equipment that any other topic. Please understand that eliminating this tax credit will affect businesses with equipment that was acquired before July 1 of 2006.

Business personal property purchased after that date is exempt from all property tax in Kansas.

But those with the older equipment still pay property tax on that business personal property, and get 25% of that property tax back in a fully refundable tax credit.

Technically, you can't say that eliminating this credit increases their tax liability. It certainly increases their expenses.

These would tend to be small businesses and businesses that cannot afford to purchase new equipment, particularly with the tight credit brought on by the recession. My feeling is that many companies are unaware of this proposal and will be very upset if it passes.

The HPIP program and the machinery and equipment property tax credit were put together with considerable thought. Please give considerable thought to what you do to them in this legislation.

Thank you again for the opportunity to testify.

The Kansas Economic Progress Council is a not for profit designed to draw together organizations and businesses interested in advancing sound public policy in Kansas to enhance our state's quality of life.

Kansas Economic Progress Council
www.ksepc.org
212 SW 8th Avenue, Suite 200
Topeka KS 66612

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February 14, 2011

Governor Sam Brownback
Attn: Dave Kensinger, Chief of Staff
Office of the Governor
301 W. 10th Avenue, #241S
Topeka, KS 66612

Dear Governor Brownback:

It appears that the few large Kansas-based businesses were able to get your attention regarding the importance of the HPIP and other tax credits currently available from the State of Kansas. We want to make sure you also hear the voice of those who make up the majority of businesses in Kansas...small businesses, or as we like to think of ourselves, "community businesses."

Data Center, Inc. (DCI) was founded in 1963 in Hutchinson, Kansas, where its national headquarter still resides today. DCI is a technology, software and service provider to the "community banking industry." DCI employs 265 people throughout the country with approximately 210 of those residing in Kansas. We provide an annual payroll of $12M, of which $9.5M stays right here in Kansas.

DCI pays wages well above the state averages and invests approximately $1.5M to $3.0M each year in our equipment, software, and facilities. Obviously, some of the investment is required to operate a sound business; however, we go above and beyond because of the current incentives in place. The current proposal with a minimum investment at $5M (and to exclude the minimum from the credit calculation) would completely eliminate DCI, as well as most Kansas companies.

Existing businesses like DCI don't have many options for economic development benefits. The HPIP tax credit, Business and Job Development tax credit, and the Machinery and Equipment refundable tax credits are the only incentives available to us. The proposed "expensing incentive" is nothing more than the savings on the time value of money since it is only advancing the deductions we would be taking anyway under current depreciation laws.

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Additionally, our industry is continually evolving as the financial system's transaction volume moves more and more to an electronic form. This continually lessons the "physical" presence that was once necessary in our industry. Other states realize this and continually work to "incent" us to move our operations. While we have no intentions to move, we don't want Kansas' lack of business-friendly incentives to give us reason to consider it.

We love our state, our community and the communities across the state that we do business in. Please don't underestimate the impact that small businesses…"community businesses" have on the economy of Kansas. We urge you to retain the incentives currently in place in support of Kansas' small businesses.

Sincerely,

Dennis A Queal

Dennis A. Queal
Chief Financial Officer

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TESTIMONY OF ASSOCIATED WHOLESALE GROCERS, INC
SENATE COMMITTEE ON ASSESSMENT AND TAXATION
OPPOSITION TO SB #196
FEBRUARY 16, 2011

Mr. Chairman and members of the Committee. My name is Sheila Lenson representing Associated Wholesale Grocers, Inc (AWG). AWG is the second-largest retailer-owned grocery wholesaler in the United States. AWG and its subsidiaries provide over 1,900 retail member stores in 24 states with a complete assortment of grocery products and general merchandise items and produces the *Best Choice* and *Always Save* brands of grocery products. We submit this written testimony to you in opposition to Senate Bill #196 because in 5 years, it eliminates the High Performance Incentive Program (HPIP), which includes the sales tax exemption, while immediately increasing the investment credit threshold from $50,000 to $5,000,000.

AWG has been HPIP certified since 2002 and greatly relies on the benefits the HPIP program offers our company. Through the HPIP program, our company earns a sales tax exemption and we utilize these tax savings to invest in the continuous education and training of our workforce. We also invest the savings in efficiencies to improve our cooperative's operations in order to better serve our retailers. AWG supplies approximately 180 family-owned grocery stores throughout Kansas while employing nearly 1,100 employees. Even given the size of our company, we rarely make investments in excess of $5,000,000. In 2009, our investment was approximately $4.4 million. Therefore our company, along with 90% of the other currently HPIP certified companies, will be excluded from earning a tax credit during the sunset period of the HPIP Program.

We propose that the current programs be retained, specifically HPIP with its sales tax exemptions. If expensing is a fair equivalent to the current programs as the Governor suggests that it is, then high performing companies should be allowed to choose between the current programs or expensing. Our company will choose to continue with the HPIP program. The expensing program is based solely on capital investments and offers **no sales tax savings**. Furthermore, I would appeal to you that companies currently HPIP certified be allowed to retain the $50,000 investment threshold.

We would strongly urge you to defeat this legislation.

Sn. Assmnt & Tax
2-16-11
Attachment # 12

TESTIMONY OF CBIZ
SENATE COMMITTEE ON ASSESSMENT AND TAXATION
OPPOSITION TO SB #196
FEBRUARY 16, 2011

Mr. Chairman and members of the Committee on Assessment and Taxation. My name is Betty Nelson-Ekey representing CBIZ and the numerous Kansas businesses our firm supports. CBIZ is a professional services company, providing a comprehensive range of business services to our clients. I am the Managing Director of the Tax Incentives Group in CBIZ's State and Local Tax Practice. I stand before you today in opposition to Senate Bill #196 because it would sunset the High Performance Incentive Program (HPIP), which includes the 10% investment credit and sales tax exemption, in 5-years while raising the investment threshold to $5,000,000. Currently 322 companies in 54 counties, which is over half of the Kansas counties, participate in the HPIP program and with the proposed legislation, only 10% of these companies will continue to qualify for the investment tax credit. By raising the investment threshold to 100 times its current level, the Governor is preventing small to mid-sized companies from qualifying for the program's investment credit.

CBIZ participates in several Kansas tax incentive programs that we view as essential to our business. In July 2003, CBIZ moved approximately 540 employees to Kansas from out of state. The sole and decisive factor in relocating to Kansas was the tax incentives that the state offered, which included HPIP, the Business and Job Credit, sales tax exemption, and the IMPACT program. Without the presence of these tax incentives, our relocation to Kansas from out of state **would not have happened**. As a service-oriented company with highly-paid employees, the proposed expensing plan and subsequent repeal of HPIP and other tax programs will have a markedly unfavorable impact on our business. I submit the attached exhibit as evidence of the adverse effect of the proposed expensing plan.

My opposition to this bill extends beyond the interests of my own company. As a consultant in the field of Tax Incentives, I am truly concerned about the disadvantage the proposed elimination of these beneficial programs will have on the economic growth and development of the state of Kansas. The elimination of HPIP as well as the other credit programs will place Kansas at a substantial disadvantage when attempting to recruit and retain businesses. Economic Developers and representatives from the surrounding states have already communicated to me their view of Kansas' proposed legislation as a windfall to their own states' economic prosperity. Without the persuasive influence of HPIP and sales tax exemptions, states such as Missouri and Oklahoma can offer comparably far more lucrative incentives to businesses.

As a recruitment tool, the proposed expensing plan lacks viability. The expensing program merely accelerates the timing of an existing deduction. There is no parallel in replacing the elimination of a tax liability with a deduction. Any potential financial benefit of the expensing plan will be difficult to quantify on a proposal to a prospective business. The regard for the plan as a true incentive is further diminished by offering the program to all business sectors, including retail. For instance, I pose the question: why should a small manufacturer or software developer that (1) pays higher than average wages; (2) generates greater than 50% of revenue from out of state; and (3) extensively trains their workforce, not receive a greater incentive than the Kentucky Fried Chicken or liquor store that is purchasing equipment?

I would suggest that if HPIP must be eliminated, then existing companies who have previously been HPIP certified as well as those companies that have been offered HPIP as part of their formal incentive proposal from the state be allowed to retain the current $50,000 investment threshold throughout the duration of the sunset period.

I would strongly urge you to defeat this legislation.

Exhibit as part of the Testimony of Betty Nelson-Ekey

Kansas Proposed Legislation
Current Incentives vs Expensing Comparison

	Machinery & Equipment			Building	
Investment in:					
Machinery & Equipment	1,000,000			-	
Building	-			3,000,000	
Current Incentives:					
HPIP Tax Credit	95,000			295,000	
Sales Tax Exemption	83,000			-	
Total Current Incentives	178,000			295,000	
Benefit of Expensing:					
Assumptions:					
Interest Rate	5.0%			8.0%	
Depreciable Life - M&E	7	MACRS + 50% Bonus			
Depreciable life - Building				39.5	Years Straight Line
	Corporate	Individual		Corporate	Individual
Kansas Tax Rate	7.00%	6.45%		7.00%	6.45%
Machinery & Equipment:					
Current Deduction Tax Benefit	70,000	64,500		-	-
Present Value of Depreciation Tax Benefit with MACRS / 50% Bonus	(65,953)	(60,771)		-	-
Value of Expensing M&E	4,047	3,729		-	-
As a % of Investment	0.40%	0.37%		0.0%	0.0%
Building:					
Current Deduction Tax Benefit	-	-		-	-
Present Value of Depreciation Tax Benefit	-	-		-	-
Value of Expensing Building	-	-		-	-
As a % of Investment	0.0%	0.0%		0.0%	0.0%
Value of Expensing	6,041	5,566			
Cost of Proposed Legislation	(173,953)	(174,271)		(295,000)	(295,000)

Note: Assumes taxpayer can currently utilize credits and deductions.
Federal legislation passed 12/17/10 provides for 100% expensing for 2011.

Allen, Gibbs & Houlik, L.C.
CPAs & Advisors

Testimony of D. Shawn Sullivan, CPA, on Senate Bill 196
Before the Kansas Senate Assessment and Taxation Committee, February 16, 2011

My name is Shawn Sullivan. I am a certified public accountant and vice president of tax services for Allen, Gibbs & Houlik, L.C., (AGH) in Wichita, Kansas. AGH is one of the largest CPA and advisory firms in the Midwest, employing more than 115 people. I am here today on behalf of my firm and a number of my firm's corporate clients to express our opposition to several provisions of SB 196. These clients, identified on Attachment 1, collectively represent more than $1.5 billion of the state's economy and almost 5,000 Kansas employees. They are primarily home-grown Kansas companies who regard themselves as "community businesses."

AGH and our identified clients believe that these bills' intended purpose – to stimulate economic development by creating a tax break on state income for a larger group of businesses – will instead create the opposite effect. We believe that if legislators and businesses understood the real impact of this legislation behind all the technical details -- as we hope to share with you today – that they would recognize the problems associated with the bill's consequences:

- A de facto tax INCREASE for almost all but the smallest and largest of Kansas businesses
- A crippling effect on the state's economic development efforts to recruit new businesses and retain our existing businesses in Kansas...resulting in the likely loss of capital, jobs and businesses in Kansas

Here's why. SB 196 proposes to give all businesses an "extra" income-tax expense deduction for business machinery and equipment investments – meaning that you would be allowed to deduct an additional small portion of the cost of machinery and equipment from your taxable income the same year you spend the money. By itself, that's positive. However, because the deduction is a small percentage of the actual investment, it alone is not sufficient to stimulate investment.

But SB 196 also proposes to eliminate a number of tax credits and exemptions currently available to businesses which have been critical to helping Kansas attract and retain capital, jobs and companies in our state. The bill proposes eliminating or radically changing FIVE important tax incentives which companies rely on to help them offset the capital investment required for new facilities and equipment – these are the Business & Jobs Development income tax credit, Business Machinery & Equipment property tax income tax credit, sales tax exemption on new projects under $5,000,000, and the Kansas Economic Opportunity Initiatives Fund. The bill also proposes raising the minimum investment to benefit from the Kansas High Performance Incentive Program or HPIP, from $50,000 to $5,000,000 before tax benefits are realized – limiting likely potential beneficiaries to less than a handful of Kansas companies.

HPIP, in particular, is a powerful economic development tool that often serves as the tipping point to convince a company to invest in Kansas versus other potential sites. As an example, within our firm alone, we are currently working three client engagements in which companies are making decisions whether to invest in facilities and equipment in Kansas, or in other states or even other

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countries. For one client, the HPIP tax advantage alone was the key to their decision to invest in Kansas instead of expanding elsewhere. By comparison, surrounding and competitor states can offer the following tax credits.

- Oklahoma (Quality Jobs Program, Investment Tax Credit)
- Colorado (Investment Tax Credit, Job Training Tax Credit, Wage Subsidy Program)
- Nebraska (Nebraska Advantage Program)
- Missouri (Enhanced Enterprise Zone Act, Quality Jobs Program)
- Texas (Investment Tax Credit, Job Creation Credit)
- California (New Jobs Credit, Investment Tax Credit)

By eliminating or radically changing some of these tax incentives, we eliminate many of the tools economic development agencies and organizations such as the Kansas Department of Commerce and the Greater Wichita Economic Development Commission use to help create new jobs and bring new businesses to Kansas.

As a CPA firm which has a deep understanding of all of these tax issues, we have created sample illustrations showing the projected tax liability of a company investing in a capital project of $3,000,000 in today's tax environment versus the company's tax liability if the proposed bill becomes law. This sample Kansas company has taxable income of $6.5 million, and invests $2 million in a new facility, and $1 million in machinery and equipment.

In the current environment, the company would benefit from tax incentives for both the facility and equipment investment through HPIP tax credits. The bill would limit tax benefits to just the expensing benefits attributable to the $1 million in machinery purchased, and eliminate the HPIP benefit altogether because the total project cost is less than $5,000,000.

The current Kansas tax liability for this hypothetical company would be $160,000 versus $442,890 under SB 196. That's a tax increase of $282,890 -- enough to potentially cause a company to relocate the capital investment or forget it altogether. By way of comparison, the reduction in Kansas income taxes the company would see from the proposed expensing provision is a total of $12,000 on a $1,000,000 investment – a decent benefit if a company has already invested, but not enough to cause new spending on machinery and equipment. In addition, the $12,000 is a tax benefit in timing of the taxes only, not a tax credit like that available through programs such as HPIP.

To be clear about our concerns, AGH and our identified clients are not opposing tax benefits for large companies who are capable of investing $5,000,000 or more at a time – that's good news for Kansas. But we believe that these tax benefits should be extended to small and medium-sized businesses as well – those businesses which make up the majority of our state's economic growth and which are the businesses currently adding jobs and considering expansion.

We believe that adopting SB 196/HB 2317, especially when our state's economy is finally starting to show signs of recovering, could effectively redirect the flow of capital, jobs and business from our own state into other states or countries with a more business-friendly tax environment.

Company	City	County
Kan Pak, LLC	Arkansas City	Cowley
Harper Industries, Inc.	Harper	Harper
Cereal Ingredients, Inc.	Leavenworth	Leavenworth
Bradbury Company, Inc.	Moundridge	McPherson
Moridge Manufacturing, Inc.	Moundridge	McPherson
Shield Industries, Inc.	South Hutchinson	Reno
Aero Mach Labs, Inc.	Wichita	Sedgwick
Buckley Industries, Inc.	Wichita	Sedgwick
IMA Financial Group, Inc.	Wichita	Sedgwick
Lubrication Engineers, Inc.	Wichita	Sedgwick
McCormick Armstrong Co., Inc.	Wichita	Sedgwick
Rand Graphics Inc.	Wichita	Sedgwick
Rose America Corporation	Wichita	Sedgwick
Westland Corporation, U.S.A.	Wichita	Sedgwick
Youngers & Sons Manufacturing Co., Inc.	Viola	Sedgwick
Cobalt Boats, LLC	Neodesha	Wilson

14-2

SB 196 HB 2317
TAX INCREASE

Current Scenario	
Kansas Capital Investment	$3,000,000
Kansas HPIP Credit Rate	10.00%
Kansas HPIP Credit Rate	$295,000
Kansas Taxable Income	$6,500,000
Estimate Tax Rate	7.00%
Tax Liability before HPIP	$455,000
Less Kansas HPIP Credit	($295,000)
Kansas Tax Liability	$160,000
Tax Increase	**$282,890**

Proposal	
Kansas Capital Investment**	$1,000,000
Expensing Factor 7 yr property	17.30%
Expensing Deduction	$173,000
Kansas Taxable Income	$6,500,000
Less Kansas Expensing Deduction	($173,000)
Kansas Taxable Income	$6,327,000
Estimated Tax Rate	7.00%
Kansas Tax Liability	$442,890
Expensing Benefit	$12,110

**Equipment only--real estate excluded

ATTACHMENT 2

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February 14, 2011

Governor Sam Brownback
Attn: Dave Kensinger, Chief of Staff
Office of the Governor
301 W. 10th Avenue, #241S
Topeka, KS 66612

Dear Governor Brownback:

It appears that the few large Kansas-based businesses were able to get your attention regarding the importance of the HPIP and other tax credits currently available from the State of Kansas. We want to make sure you also hear the voice of those who make up the majority of businesses in Kansas...small businesses, or as we like to think of ourselves, "community businesses."

Data Center, Inc. (DCI) was founded in 1963 in Hutchinson, Kansas, where its national headquarter still resides today. DCI is a technology, software and service provider to the "community banking industry." DCI employs 265 people throughout the country with approximately 210 of those residing in Kansas. We provide an annual payroll of $12M, of which $9.5M stays right here in Kansas.

DCI pays wages well above the state averages and invests approximately $1.5M to $3.0M each year in our equipment, software, and facilities. Obviously, some of the investment is required to operate a sound business; however, we go above and beyond because of the current incentives in place. The current proposal with a minimum investment at $5M (and to exclude the minimum from the credit calculation) would completely eliminate DCI, as well as most Kansas companies.

Existing businesses like DCI don't have many options for economic development benefits. The HPIP tax credit, Business and Job Development tax credit, and the Machinery and Equipment refundable tax credits are the only incentives available to us. The proposed "expensing incentive" is nothing more than the savings on the time value of money since it is only advancing the deductions we would be taking anyway under current depreciation laws.

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Additionally, our industry is continually evolving as the financial system's transaction volume moves more and more to an electronic form. This continually lessons the "physical" presence that was once necessary in our industry. Other states realize this and continually work to "incent" us to move our operations. While we have no intentions to move, we don't want Kansas' lack of business-friendly incentives to give us reason to consider it.

We love our state, our community and the communities across the state that we do business in. Please don't underestimate the impact that small businesses..."community businesses" have on the economy of Kansas. We urge you to retain the incentives currently in place in support of Kansas' small businesses.

Sincerely,

Dennis A Queal

Dennis A. Queal
Chief Financial Officer

Kansas AEP

Association Of Ethanol Processors

Ethanol - *Made In Kansas*

Senate Taxation Committee
Written Testimony in Opposition to SB 196
HPIP Threshold Changes
Submitted by Ron Seeber
on behalf of the
Kansas Association of Ethanol Processors
February 16, 2011

Good morning Chairman and members of the Senate Tax Committee. I am Ron Seeber and I am the Vice President of Government Affairs for the Kansas Association of Ethanol Processors (KAEP), which represents the ethanol industry in Kansas. We represent the 11 ethanol plants in Kansas that produce fuel grade ethanol. These plants produce an estimated 500 million gallons of ethanol annually.

KAEP opposes certain provisions in SB 196. Specifically, the proposed changes to the High Performance Incentives Program. By changing the investment threshold from \$50,000 to \$5,000,000, our ethanol plants would find it very difficult to invest the adequate amount in land, buildings and equipment during a year – as would be required by the legislation. The proposed change in HPIP would dramatically reduce the ability of small to mid-sized Kansas companies to benefit from the program. The small to mid-sized companies, such as ethanol processors, are the backbone of employers in Kansas and they need the same incentives available to them as larger companies.

We urge that you allow keep the current threshold so that small to mid-size companies are eligible to apply for HPIP. This will greatly assist the ethanol industry in Kansas to continue to grow and prosper.

Thank you for your consideration.

Sn. Assmnt & Tax
2-16-11
Attachment # 15

816 SW Tyler, Ste. 100 Topeka, KS 66612 (785) 234-0461 Fax (785) 234-2930 www.KAEP.o

KNIT-RITE INCORPORATED

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TESTIMONY OF KNIT RITE, INC.
SENATE COMMITTEE ON ASSESSMENT AND TAXATION
OPPOSITION TO SB#196
FEBRUARY 16, 2011

February 15, 2011

Mr. and Ms. Chairman, member of the Committee on Assessment and Taxation. My name is Chris Vering, representing Knit-Rite, Inc. We are a growing medical textile manufacturer in Kansas City, KS, who has been serving the prosthetic, orthotic, diabetic, compression and several other medical markets for over 88 years. We submit this written testimony to you in opposition to Senate Bill #196 because it would phase out the High Performance Incentive Program (HPIP), which includes the 10% investment credit and sales tax exemption, over 5-years while raising the investment threshold to $5,000,000. By raising the investment threshold to 100 times its current level, the Governor is fundamentally preventing small to mid-sized companies, such as ours, from participating in the phase out period of the HPIP program. Currently 322 companies in 54 counties, which is over half of Kansas counties, participate in the HPIP program and with the proposed legislation, only 10% of these companies will be able to qualify for the investment tax credit during the 5-year phase out period.

Our company sincerely believes in the value and importance of HPIP and considers the decision to phase out this program over 5-years while imposing a $5,000,000 investment threshold to be detrimental to our business. We are a mid-sized company with over 50% of our revenues generated outside of the state of Kansas. We employ 77 employees who earn above-average wages and each year we make a significant investment in the training of these employees. We have been HPIP certified since moving to Kansas in the late 1990's from Missouri. The programs offered by Kansas were the reason we moved here to begin with. However with the Governor's decision to require investments in excess of $5,000,000, we will be precluded from earning an investment credit during the 5-year phase out since annually we typically only make $300,000 to $500,000 in eligible capital investments. I would suggest that if HPIP must be phased out, allow existing companies to retain the $50,000 threshold during the phase out period.

In addition to our operations in the state of Kansas, we currently own and operate a factory in Ellerbe, NC. where we employ approximately 65 employees. Through programs offered by the state of North Carolina, we have invested more funds in that facility the last 2 years. We currently receive tax incentives and/or direct funds for training, job growth and capital investments that exceed the programs offered by the state of Kansas. The proposals being offered to reduce the benefits in Kansas will only make Kansas even less competitive with North Carolina and

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Sn. Assmnt & Tax
2-16-11
Attachment # 16

KNIT-RITE INCORPORATED

core spun THERAFIRM SmartKnit

other states. For example, I continuously receive calls from Iowa Economic Development officials. I am sure the state would not want to lose companies to other states, including Iowa and North Carolina.

As a Kansas business committed to economic growth and development within the state, we believe the proposed plan will have an adverse impact on our ability to continue to contribute to that effort. We propose that the current programs be retained, specifically HPIP with sales tax exemptions. If expensing is a fair equivalent to the current programs as the Governor suggests that it is, then allow high performing companies to choose between the current programs or expensing. Our company will choose the current program. The expensing program merely accelerates the timing of an existing deduction. There is no parallel in replacing a tax credit with a tax deduction. What would you choose?

We would strongly urge you to defeat this legislation.

Best Regards,

Christopher H. Vering
Exec. V.P., CFO, COO
Knit-Rite, Inc.

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TESTIMONY OF KARATZIS USA LLC
SENATE COMMITTEE ON ASSESSMENT AND TAXATION
OPPOSITION TO SB#196
FEBRUARY 16, 2011

Mr. Chairman and members of the Committee on Assessment and Taxation:

My name is Manolis Alatziniotakis, representing Karatzis USA LLC. KARATZIS USA LLC is an affiliated company of Karatzis SA Group, a Greek public listed company dedicated to the manufacture of premium quality netting materials. Our USA products are widely used in the agricultural sector and our annual revenue is $10,000,000. The decision to move production from overseas to Kingman KS was based partly on the current incentives and any alterations in these will have a negative impact on our financials and competitiveness in the market. To offset this difference, we will have to lay off employees or cut benefits to reduce our operational cost.

We submit this written testimony to you in opposition to Senate Bill #196 because it would phase out the High Performance Incentive Program (HPIP), which includes the 10% investment credit and sales tax exemption, over 5-years while raising the investment threshold to $5,000,000. By raising the investment threshold to 100 times its current level, the Governor is fundamentally preventing small to mid-sized companies, such as ours, from participating in the phase out period of the HPIP program. Currently 322 companies in 54 counties, which is over half of Kansas counties, participate in the HPIP program and with the proposed legislation, only 10% of these companies will be able to qualify for the investment tax credit during the 5-year phase out period.

Our company sincerely believes in the value and importance of HPIP and considers the decision to phase out this program over 5-years while imposing a $5,000,000 investment threshold to be detrimental to our business. We are a small to mid-sized company with over 50% of our revenues generated outside of the state of Kansas. We employ 36 employees who earn above-average wages and each year we make a significant investment in the training of these employees. We have been HPIP certified since 2008. However with the Governor's decision to require investments in excess of $5,000,000, we will be precluded from earning an investment credit during the 5-year phase out since annually we typically only make $2,000,000 in eligible capital investments. I would suggest that if HPIP must be phased out, allow existing companies to retain the $50,000 threshold during the phase out period.

As a Kansas business committed to economic growth and development within the state, we believe the proposed plan will have an adverse impact on our ability to continue to contribute to that effort. We propose that the current programs be retained, specifically HPIP with sales tax exemptions. If expensing is a fair equivalent to the current programs as the Governor suggests that it is, then allow high performing companies to choose between the current programs or expensing. Our company will choose the current program. The expensing program merely accelerates the timing of an existing deduction. There is no parallel in replacing a tax credit with a tax deduction. What would you choose?

We would strongly urge you to defeat this legislation.

TESTIMONY OF POPSTAR NETWORKS, INC.
SENATE COMMITTEE ON ASSESSMENT AND TAXATION
OPPOSITION TO SB #196
FEBRUARY 16, 2011

Mr. Chairman and members of the Committee. My name is Thomas Reed representing Popstar Networks, Inc. Popstar is a software development, licensing and managed services company. We submit this written testimony to you in opposition to Senate Bill #196 because it would eliminate the High Performance Incentive Program (HPIP); Sales Tax Exemption under HPIP and Business & Job Development Programs; Machinery & Equipment Property Tax Credits; Business & Job Development Tax Credits; Kansas Economic Opportunity Initiative Funds (KEOIF); and convert the IMPACT program to a "deal closer" fund with a $10 million cap on the available resources.

Our company sincerely believes in the value and importance of the current tax credit programs, and considers the decision to replace these programs with an expensing plan to be detrimental to our business. Unlike the current tax credit programs, the proposed expensing plan does not offer a means by which the actual tax liability will be removed, but merely accelerates the timing of an existing deduction. The expensing plan is based solely on capital investments and offers **no sales tax savings**. The plan also does not include an alternative to the current benefit tax credit programs provide on the **lease or purchase of a building**.

The critical need to provide continuing training for existing and **new** employees is mandatory for any company, let alone a technology company, to stay competitive and to grow. The need for assistance with this paradigm shift in the skills and skill levels of the American employee is one of the most important areas that the state government can assist a growing company. Without this assistance a company will likely have to go out of state to find qualified workers. Without a plan to train and "up-skill" new employees the ability to find and employ quality employees becomes a negative with recruiting and retention. A change in the current program will only encourage employers to relocate or force them to downsize their business.

We would strongly urge you to defeat this legislation if the state is truly dedicated to providing the best business environment possible to promote a robust and innovative environment for its small and medium sized business constituents. A change at this time will only tend to exacerbate an already challenging economy and send the wrong message

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2-16-11
Attachment # 18

to employers. It will also open the door to other states that can point to the "anti-business" environment Kansas is moving towards.

With the state's assistance in this important area, companies will be encouraged to move more aggressively in re-training their employee's and make them a more productive and valued resource. This will help provide a more competitive resource and a differentiation that Kansas can point to compared to a lot of other states. This is **NOT** the area that should be cut or redefined.

Respectfully submitted,

Thomas L. Reed

President & CEO

Popstar Networks, Inc.

TESTIMONY OF MARTHON SOLUTION, INC.
SENATE COMMITTEE ON ASSESSMENT AND TAXATION
OPPOSITION TO SB#196
FEBRUARY 16, 2011

Mr. Chairman and members of the Committee on Assessment and Taxation. My name is Tim Hutteger, representing Marathon Solutions, Inc. Marathon Solutions, Inc. is a premier credit card processor located in Mission, KS. We submit this written testimony to you in opposition to Senate Bill #196 because it would phase out the High Performance Incentive Program (HPIP), which includes the 10% investment credit and sales tax exemption, over 5-years while raising the investment threshold to $5,000,000. By raising the investment threshold to 100 times its current level, the Governor is fundamentally preventing small to mid-sized companies, such as ours, from participating in the phase out period of the HPIP program. Currently 322 companies in 54 counties, which is over half of Kansas counties, participate in the HPIP program and with the proposed legislation, only 10% of these companies will be able to qualify for the investment tax credit during the 5-year phase out period.

Our company sincerely believes in the value and importance of HPIP and considers the decision to phase out this program over 5-years while imposing a $5,000,000 investment threshold to be detrimental to our business. We are a small to mid-sized company with over 50% of our revenues generated outside of the state of Kansas. We employ 12 employees who earn above-average wages and each year we make a significant investment in the training of these employees. We are in the process of becoming HPIP certified. However with the Governor's decision to require investments in excess of $5,000,000, we will be precluded from earning an investment credit during the 5-year phase out since annually we typically only make $100,000 in eligible capital investments. I would suggest that if HPIP must be phased out, allow existing companies to retain the $50,000 threshold during the phase out period.

As a Kansas business committed to economic growth and development within the state, we believe the proposed plan will have an adverse impact on our ability to continue to contribute to that effort. We propose that the current programs be retained, specifically HPIP with sales tax exemptions. If expensing is a fair equivalent to the current programs as the Governor suggests that it is, then allow high performing companies to choose between the current programs or expensing. Our company will choose the current program. The expensing program merely accelerates the timing of an existing deduction. There is no parallel in replacing a tax credit with a tax deduction.

We would strongly urge you to defeat this legislation.

Sincerely,

Tim Hutteger
Chief Executive Officer
Marathon Solutions, Inc.

Sn. Assmnt & Tax
2-16-11

Attachment # 19

TESTIMONY OF CBIZ
SENATE COMMITTEE ON ASSESSMENT AND TAXATION
OPPOSITION TO SB #196
FEBRUARY 16, 2011

Mr. Chairman and members of the Committee. My name is Richard Mills, III representing CBIZ. CBIZ is a professional services company, providing a comprehensive range of business services, products, and solutions that help our clients succeed by better managing their finances and employees. We are one of the nation's leading Accounting Providers; Employee Benefits Specialists; Property & Casualty Agencies; Valuation firms; Medical Management practice firms; and Retirement Plan service providers. We submit this written testimony to you in opposition to Senate Bill #196 because it would phase out the High Performance Incentive Program (HPIP), which includes the 10% investment credit and sales tax exemption, over 5-years while raising the investment threshold to $5,000,000. By raising the investment threshold from $50,000 to $5,000,000, the Governor is preventing 90% of the companies currently HPIP certified from qualifying for the investment tax credit during the phase out period.

In July 2003, CBIZ made the pragmatic economic decision to move one of our largest regional operations and approximately 540 employees to Kansas from out of state. The sole and decisive factor in relocating to Kansas was the tax incentives that the state offered, which included HPIP, the Business and Job Credit, sales tax exemption, and the IMPACT program. Since 2003, CBIZ which includes the entities of CBIZ MHM, CBIZ Benefits & Insurance, and M&S Consulting, has been HPIP certified.

As a service-oriented company with highly-paid employees, we analyzed the impact the expensing plan will have on our business and the consequences are unfavorable. The proposed expensing program merely accelerates the timing of an existing deduction and is structured solely around capital investments while offering **no sales tax savings** on these purchases. Also, the expensing plan **does not provide an alternative to the benefit the current tax credit programs provide on the lease or purchase of a building**.

We propose that the current programs be retained, specifically HPIP with sales tax exemptions. However if there is no alternative to phasing out HPIP, then I would suggest that currently participating companies be allowed to retain the $50,000 threshold during the phase out period and be allowed to choose between participating in the current programs or the proposed expensing program.

We would strongly urge you to defeat this legislation.

Sn. Assmnt & Tax
2-16-11

Attachment # 20

TESTIMONY OF THE KATZ LAW FIRM
SENATE COMMITTEE ON ASSESSMENT AND TAXATION
OPPOSITION TO SB#196
FEBRUARY 16, 2011

Mr. Chairman and members of the Committee. My name is Rick Katz, representing The Katz Law Firm. We are a real estate law firm specializing in real estate development and leasing. We submit this written testimony to you in opposition to Senate Bill #196 because it would phase out the High Performance Incentive Program (HPIP), which includes the 10% investment credit and sales tax exemption, over 5-years while raising the investment threshold to $5,000,000. By raising the investment threshold, the Governor is fundamentally preventing small to mid-sized companies, such as ours, from participating in the phase out period of the HPIP program. Currently 322 companies in 54 counties, which is over half of Kansas counties, participate in the HPIP program and with the proposed legislation, only 10% of these companies will be able to qualify for the investment tax credit during the 5-year phase out period.

Our company sincerely believes in the value and importance of HPIP and considers the decision to phase out this program over 5-years while imposing a $5,000,000 investment threshold to be detrimental to our business. We are a small to mid-sized company with over 50% of our revenues generated outside of the state of Kansas. We employ 10 employees who earn above-average wages and each year we make a significant investment in the training of these employees. We have been HPIP certified since 2008. However with the Governor's decision to require investments in excess of $5,000,000, we will be precluded from earning an investment credit during the 5-year phase out since annually we typically only make approximately 3 million dollars in eligible capital investments. I would suggest that if HPIP must be phased out, then existing HPIP companies should be allowed to retain the current $50,000 threshold during the phase out period.

As a Kansas business committed to economic growth and development within the state, we believe the proposed plan will have an adverse impact on our ability to continue to contribute to that effort. We propose that the current programs be retained, specifically HPIP with sales tax exemptions. If expensing is a fair equivalent to the current programs as the Governor suggests that it is, then allow high performing companies to choose between the current programs or expensing. Our company will choose the current program. The expensing program merely accelerates the timing of an existing deduction. There is no parallel in replacing a tax credit with a tax deduction.

We would strongly urge you to defeat this legislation.

TESTIMONY OF CORDERO
SENATE COMMITTEE ON ASSESSMENT AND TAXATION
OPPOSITION TO SB#196
FEBRUARY 16, 2011

Mr. Chairman and members of the Committee on Assessment and Taxation. My name is Eli Bowman, representing Codero. Codero is a dedicated server web hosting service provider. We submit this written testimony to you in opposition to Senate Bill #196 because it would phase out the High Performance Incentive Program (HPIP), which includes the 10% investment credit and sales tax exemption, over 5-years while raising the investment threshold to $5,000,000. By raising the investment threshold to 100 times its current level, the Governor is fundamentally preventing small to mid-sized companies, such as ours, from participating in the phase out period of the HPIP program. Currently 322 companies in 54 counties, which is over half of Kansas counties, participate in the HPIP program and with the proposed legislation, only 10% of these companies will be able to qualify for the investment tax credit during the 5-year phase out period.

Our company sincerely believes in the value and importance of HPIP and considers the decision to phase out this program over 5-years while imposing a $5,000,000 investment threshold to be detrimental to our business. We are a small to mid-sized company with over 50% of our revenues generated outside of the state of Kansas. We employ 57 employees who earn above-average wages and each year we make a significant investment in the training of these employees. We have been HPIP certified since December 30, 2008. However with the Governor's decision to require investments in excess of $5,000,000, we will be precluded from earning an investment credit during the 5-year phase out since annually we typically only make $15,000 in eligible capital investments. I would suggest that if HPIP must be phased out, allow existing companies to retain the $50,000 threshold during the phase out period.

As a Kansas business committed to economic growth and development within the state, we believe the proposed plan will have an adverse impact on our ability to continue to contribute to that effort. We propose that the current programs be retained, specifically HPIP with sales tax exemptions. If expensing is a fair equivalent to the current programs as the Governor suggests that it is, then allow high performing companies to choose between the current programs or expensing. Our company will choose the current program. The expensing program merely accelerates the timing of an existing deduction. There is no parallel in replacing a tax credit with a tax deduction.

We would strongly urge you to defeat this legislation.

Sn. Assmnt & Tax
2-16-11

Attachment # 22