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Adam C. Proffitt, Director

Laura Kelly, Governor

February 26, 2025

The Honorable Adam Smith, Chairperson
House Committee on Taxation
300 SW 10th Avenue, Room 346-S
Topeka, Kansas 66612

Dear Representative Smith:

SUBJECT: Fiscal Note for HB 2336 by House Committee on Taxation

In accordance with KSA 75-3715a, the following fiscal note concerning HB 2336 is respectfully submitted to your committee.

HB 2336 would create a procedure to allow corporate income tax rates to decrease in tax year 2028. In FY 2026, the Director of the Budget would certify to the Secretary of Revenue at the end of the fiscal year the amount of actual corporate income tax receipts to the State General Fund that is in excess of the prior fiscal year's corporate income tax receipts. The Secretary of Revenue would be required to compute the rate reductions to the normal tax on corporations that would decrease receipts by the certified amount, rounded down to the nearest 0.1 percent. The rate change would be required to be published by the Secretary of Revenue by October 1, 2027, and would go into effect in tax year 2028. The rate reduction would remain in effect unless further reduced. Lower tax receipts would not trigger an automatic rate increase.

The bill would allow financial institutions to elect to apportion business income by the taxpayer's receipts factor for tax years 2025, 2026, and 2027. The election would be effective and irrevocable for the taxable year of the election and would be binding on all members of a unitary group of corporations. All business income would be apportioned by multiplying the business income by the receipts factor beginning on January 1, 2028. The bill would also create a deduction for qualified, publicly traded companies that see an increase in tax liability from the single sales factor. Taxpayers would be able to spread out the total deduction amount in equal amounts over ten tax years beginning in tax year 2035.

The bill would allow a taxpayer to elect to apportion business income by multiplying the taxpayer's business income by the sales factor for tax years 2025, 2026, and 2027. The election would be effective and irrevocable for the taxable year of the election. All business income would be apportioned by multiplying the business income by the sales factor beginning on January 1, 2028. The bill would allow any taxpayer that previously made an election to make a new election to apportion business income by multiplying the taxpayer's business income by the sales factor. The bill would also create a deduction for qualified, publicly traded companies that see an increase in tax liability from the single sales factor. Taxpayers would be able to spread out the total deduction amount in equal amounts over ten tax years beginning in tax year 2035.

The bill would allow trucking companies and railroads to use the same apportionment methods as most other companies instead of using mileage-based apportionment. The bill would also make changes to the definition of sales for income tax purposes.

The Department of Revenue estimates that HB 2336 would decrease State General Fund Revenues by at least $115.7 million in FY 2026, $89.9 million in FY 2027, and $73.1 million in FY 2028.

To formulate these estimates, the Department of Revenue reviewed corporate income tax returns from tax years 2021 and 2022. Companies that operate solely in Kansas would see no change from the apportionment method changes in this bill. For tax years 2025, 2026, and 2027, companies would have the option to choose between using the current three factor apportionment method or a single sales factor when they file their return. It is assumed companies will choose the method that results in a lower tax liability. Based on tax year 2022 data, an optional single sales factor would decrease corporate tax liability by approximately $41.6 million per tax year. For tax year 2028, the single sales factor would become mandatory, which is expected to increase tax liability by $10.4 million.

For financial institutions, data on the three-factor formula is not available. The impact on privilege tax was estimated using the impacts for corporate tax, and tax years 2021 and 2022 collection data. This would be expected to decrease privilege tax liability by $2.9 million in tax years 2025, 2026 and 2027 and increase tax liability by $800,000 in tax year 2028.

For interstate motor carriers and railroads, three factor data is not available due to the current use of mileage-based apportionment. Companies operating in multiple states were identified based on NAICS codes and the current apportionment factor used. These companies having the option to use single sales factor apportionment and basing sales on cost of performance would be expected to decrease tax collections by at least $35.2 million per tax year.

The deductions provided in the bill would take effect in tax year 2035 with the first impact being seen in late FY 2035. Limited information is available to determine this impact. Based on population size and a similar deduction in Massachusetts, this would be expected to decrease State General Fund revenues by a total of $223.7 million, which would likely be spread out with $22.4 million claimed per tax year over the next ten tax years that the deduction is in effect.

It is unknown if the corporate income tax rate reduction mechanism for tax year 2028 would be triggered. Factoring in the fiscal note of this bill with the November Consensus Revenue

Estimates for FY 2025 and FY 2026, the total corporate income tax receipts to occur in FY 2026 are estimated to be lower than the corporate income tax receipts estimated to occur in FY 2025, which would not trigger the rate reduction. However, corporate income tax receipts estimates could change based on corporate profits, economic outlook, and state and federal tax policy changes, which could allow for corporate income tax receipts to be higher in FY 2026 than FY 2025 and trigger the rate reduction. This fiscal note does not take into effect any reduction in corporate income tax receipts due to the rate reduction mechanism because actual receipts from FY 2025 and FY 2026 are unknown.

The estimate for FY 2026 includes 100.0 percent of tax year 2025 tax liability and 30.0 percent of tax year 2026 tax liability. The estimate for FY 2027 includes 70.0 percent of tax year 2026 tax liability and 30.0 percent of tax year 2027 tax liability.

The Department indicates that the bill would require $61,740 from the State General Fund in FY 2026 to implement the bill and to modify the automated tax system. The required programming for this bill by itself would be performed by existing staff of the Department of Revenue. In addition, if the combined effect of implementing this bill and other enacted legislation exceeds the Department's programming resources, or if the time for implementing the changes is too short, additional expenditures for outside contract programmer services beyond the Department's current budget may be required. Any fiscal effect associated with HB 2336 is not reflected in *The FY 2026 Governor's Budget Report*.

Sincerely,

Adam C. Proffitt
Director of the Budget

cc: Lynn Robinson, Department of Revenue