

March 23, 2011

The Honorable Les Donovan, Chairperson  
Senate Committee on Assessment and Taxation  
Statehouse, Room 123-E  
Topeka, Kansas 66612

Dear Senator Donovan:

**SUBJECT:** Fiscal Note for SB 197 by Senate Committee on Assessment and Taxation

In accordance with KSA 75-3715a, the following fiscal note concerning SB 197 is respectfully submitted to your committee.

SB 197 would phase out the retail sales tax imposed by the state on food and food ingredients over a five-year period. The bill would expand on the current definition of food and food ingredient to exclude candy, dietary supplements, food sold through vending machines, prepared food, and soft drinks. The bill also provides specific definitions for candy, food sold through vending machines, prepared food, and soft drinks. The bill would adjust the state retail sales tax rates on food and food ingredients as follows:

<u>Date of Rate Change</u>	<u>Tax Rate</u>
Current law	6.30 %
July 1, 2011	5.04
July 1, 2012	4.78
July 1, 2013	3.52
July 1, 2014	1.26
July 1, 2015	--

The bill would also modify the food sales tax refund amounts to coincide with the tax rate changes on food and food ingredients. The food sales tax refund program would be eliminated in calendar year 2015 to coincide with the elimination of sales tax on food and food ingredients. The bill would adjust the food sales tax refund amounts as follows:

<u>Calendar Year</u>	<u>Income \$17,500 or less</u>	<u>Income \$17,500 to \$35,000</u>
2011(Current law)	\$90	\$45
2011	\$72	\$36
2012	\$54	\$27
2013	\$36	\$18
2014	\$18	\$9
2015	--	--

Estimated State Fiscal Effect				
	FY 2011 SGF	FY 2011 All Funds	FY 2012 SGF	FY 2012 All Funds
Revenue	--	--	(\$56,510,000)	(\$65,290,000)
Expenditure	--	--	\$86,262	\$86,262
FTE Pos.	--	--	--	--

The Department of Revenue estimates that SB 197 would decrease state revenues by \$65,290,000 in FY 2012. Of those totals, the State General Fund is estimated to decrease by \$56,510,000 in FY 2012, while the State Highway Fund is estimated to decrease by \$8,780,000 in FY 2012. The decrease in revenues and how the November 2, 2010 consensus revenue estimate for FY 2012 would be affected are shown in the following table:

Effect on FY 2012 Consensus Revenue Estimates  
(Dollars in Thousands)

Receipt Description	Consensus Revenue Estimates (Nov. 2, 2010)	Change in Revenue FY 2012	Proposed Adjusted CRE FY 2012
Motor Carrier	\$ 27,000	\$ --	\$ 27,000
Income Taxes:			
Individual	2,705,000	10,500	2,715,500
Corporate	275,000	--	275,000
Financial Institutions	21,000	--	21,000
Excise Taxes:			
Retail Sales	2,090,000	(67,010)	2,022,990
Compensating Use	295,000	--	295,000
Cigarette	97,000	--	97,000
Corporate Franchise	8,000	--	8,000
Severance	94,300	--	94,300
All Other Excise Taxes	96,400	--	96,400
Other Taxes	<u>127,000</u>	<u>--</u>	<u>127,000</u>
Total Taxes	\$5,835,700	(\$ 56,510)	\$5,779,190
Other Revenues:			
Interest	\$ 11,800	\$ --	\$ 11,800
Transfers	(93,700)	--	(93,700)
Agency Earnings	<u>56,800</u>	<u>--</u>	<u>56,800</u>
Total Other Revenues	(\$ 25,100)	\$ --	(\$ 25,100)
Total Receipts	\$5,810,600	(\$ 56,510)	\$5,754,090

The fiscal effect to state revenues during subsequent years would be as follows:

	<u>FY 2013</u>	<u>FY 2014</u>	<u>FY 2015</u>	<u>FY 2016</u>
State General Fund	(\$110,520,000)	(\$180,010,000)	(\$245,380,000)	(\$255,440,000)
State Highway Fund	<u>(17,310,000)</u>	<u>(49,720,000)</u>	<u>(66,720,000)</u>	<u>(69,060,000)</u>
	(\$127,830,000)	(\$229,730,000)	(\$312,100,000)	(\$324,500,000)

To formulate these estimates, the Department of Revenue reviewed data on the food sales tax refund program, consumer expenditure reports, state sales tax reports, and from historical data that shows the average household spends 15.0 percent of its taxable income on food and food ingredients. The Department of Revenue estimates that under current law, sales tax revenue from food and food ingredients will be \$353.0 million in FY 2012 and the food sales tax refund program is estimated to issue \$42.0 million in refunds in FY 2012. Applying food and food ingredient sales to the lower sales tax rate in SB 197 is estimated to reduce overall sales tax revenue by \$75,790,000 in FY 2012, including \$67,010,000 from the State General Fund and \$8,780,000 from the State Highway Fund. Lowering the food sales tax refund amount is estimated to increase State General Fund revenue by \$10.5 million. The bill is estimated to reduce the State General Fund by a net of \$56,510,000 in FY 2012 (+\$10.5 million - \$67,010,000).

The Department of Revenue indicates the bill would require \$86,262 from the State General Fund in FY 2012 for administrative costs to modify the automated tax system. The Department estimates that the bill would require in-house programming and testing which would be performed by existing staff of the Department of Revenue. However, 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, expenditures for outside contract programmer services beyond the Department's current budget may be required. The Department indicates that the bill would require similar administrative costs to adjust food sales tax rates and food sales tax refund amounts in FY 2013, FY 2014, FY 2015, and FY 2016.

The Division of the Budget notes that the changes in tax receipts estimated by the Department of Revenue do not account for the potential cumulative effect on other taxes at the state and local level. This fiscal effect does not account for possible increases in revenue from other tax sources as a result of increases to disposable income, economic growth, net migration, or other factors that have the potential to partially or fully offset the reduction in revenue reported by the Department of Revenue. Calculating the cumulative fiscal effect of this legislation would require dynamic scoring analysis, which is not currently used by the Department of Revenue or the Division of the Budget in the preparation of fiscal notes.

The Kansas Department of Transportation (KDOT) indicates the bill would reduce sales tax revenue dedicated to the State Highway Fund by \$8,780,000 in FY 2012 and by \$17,310,000 in FY 2013. It is estimated that sales tax revenue dedicated to the State Highway Fund would be reduced by a total of \$211.6 million between FY 2012 and FY 2016, requiring expenditure reductions of the same amount over this time period. KDOT indicates the bill would not allow it to fully fund the new ten-year comprehensive transportation plan, known as T-WORKS, which

The Honorable Les Donovan, Chairperson

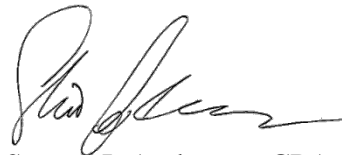
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was passed by the 2010 Legislature. Any fiscal effect associated with SB 197 is not reflected in *The FY 2012 Governor's Budget Report*.

Retailers that sell food and food ingredients would be required to break out the amount of food and non-food sales tax collections to ensure that amounts are reported correctly. Retailers would also be required to reprogram cash registers to accommodate the lower sales tax rate for food and food ingredients.

Sincerely,

A handwritten signature in black ink, appearing to read "Steven J. Anderson", with a long horizontal flourish extending to the right.

Steven J. Anderson, CPA, MBA  
Director of the Budget

cc: Steve Neske, Revenue  
Ben Cleeves, Transportation  
Larry Baer, League of Municipalities  
Melissa Wangemann, Kansas Association of Counties