

2016 KANSAS LEGISLATIVE E-REPORT #14

Paul Johnson – April 22, 2016

REVENUE ROULETTE

The state tax revenue picture continues to darken for Kansas. The slow drift into bankruptcy continues. The quality of Kansas life in regards to education and state services continues to deteriorate. The 'free lunch' of lower income tax rates and no income tax on business income for the wealthiest Kansans has been delivered. Working and hungry Kansans are covering that lost income tax revenue with higher grocery bills. The Governor's answer to this revenue mess is prayer and a hope for that economic growth miracle just over the rainbow. Kansas legislators were in shock over the lower revenue estimates. Will there be any political leadership to fix this revenue crisis when the veto session begins on April 27 or will this mess be bandaged over and left for the newly elected 2017 Kansas Legislature? Will the Kansas electorate demand an answer?

The Consensus Revenue Estimating Group (CREG) – consisting of three university economists, the Governor's budget/revenue staff and legislative research staff – delivered the bad news last Wednesday evening. The new estimate lowered revenues by \$228 million for this fiscal year and the 2017 fiscal year that ends June 30, 2017. When these lower revenue estimates are plugged into the budgets for 2016 and 2017, there is now a deficit of \$140 million to end 2016 and a \$151.3 million deficit for 2017. CREG has lowered estimates the last three years because of the uncertainty over the full impact of the lower income tax laws. Even the higher sales tax rate has not generated the estimated increases. From the revised estimate from November 2015 to this new estimate in April, individual income taxes down \$125 million, corporate income taxes down \$20 million, sales tax down \$30 million and severance taxes down \$15 million for 2016. For 2017, individual income taxes down \$108 million, corporate income taxes down \$24 million, sales tax down \$30 million and severance taxes down \$24.3 million. Kansas personal income and the state's domestic product growth lowered.

The Governor's office quickly offered three options to try and balance the 2016 and 2017 budget. There was no proposal to increase revenues or tamper with the exemption of not taxing 'small business' income for 333,000 LLC's. (It should be noted that there is no definition in the tax code for 'small business' and 17,000 (5%) of these LLC's - with incomes starting at \$100,000 on into the millions – account for 84% of the lost \$250 million in income tax collections.) All three of the options include moving \$70 million in sales tax revenue from the Highway Fund in 2016 and \$115 million in 2017. The Kansas Department of Transportation (KDOT) reported that already-programmed modernization and expansion projects will be shelved for at least two years but that

most maintenance and repairs will continue as will already under-construction projects. 10 new projects slated for 2016 costing \$273 million and 15 slated for 2017 costing \$279 million will be delayed. Delays also planned for 2018 and 2019.

In option one – beyond the KDOT reductions – the Governor requests the authority to securitize a portion of the tobacco settlements that many other states have done. These tobacco settlements have been used for early childhood programs. The total spent on these programs yearly is now \$42 million. This year's tobacco settlement was \$58 million. The plan here would be to securitize and sell off the future tobacco settlements that are above \$42 million thus freezing that amount for at least ten years. The estimate is that this scheme would bring Kansas a one-time payment of \$158 million for 2017. The additional \$16 million between the \$42 baseline and the actual receipt of \$58 million has also been used for a range of children's programs and would not be available if this bonding scheme is allowed. The Governor's office assured the legislators that additional State General Funds (SGF) could be used for worthy children's programs but no analysis or prediction on the availability of new SGF funds.

In option two – beyond the KDOT reductions – the Governor proposes to reduce Regent Institutions budgets by \$18 million for 2017 as was done in 2016. The Governor would also utilize special allotment authority to reduce \$25 million in state expenditures through targeted efficiency savings. This was a hypothetical number thrown on the table without any specific details on 'efficiency savings'. The largest savings would come through delaying the repayment of \$100 million in employer contributions into the Kansas Public Employee Retirement Systems (KPERs) from 2017 to sometime in 2018. When this \$100 million repayment is made there would be an 8% interest payment made. This maneuver will take special legislation in the veto session.

In option three – beyond the KDOT reductions – the Governor would request legislative approval to make cuts of 3% or 5% in agency budgets worth \$140 million in the upcoming fiscal year. A 5% cut would be made to the health division of the Kansas Department of Health and Environment netting \$35 million and ultimately reducing payments to medical providers providing medical assistance to the poor. A 3% reduction to the Kansas Department of Education for general state aid to K-12 will net \$57.2 million in savings to the state. After the promises of a 'stable' block grant for years 2016 and 2017 and with most school districts having finalized next year's school budget, this reduction will start July 1, 2016 and cause reductions to staff and probably shorten school years to balance budgets. (For greater detail on these school cuts – go to the Kansas Association of School Boards website www.kasb.org, click on advocacy at the top bar, click on webinars in the drop down tab, and click on the April 22, 2016 webinar. Mark Tallman will provide an hour long update on these funding cuts.) Most

state agencies and the smaller colleges are cut 3% while KU, KSU and Wichita State take a 5% cut.

The scramble is now on to fix this mess with as little political damage done to those legislators running for re-election. Most legislators would prefer that a 'lame duck' Governor - who has sufficient allotment authority already – make these difficult political decisions without forcing reluctant legislators to take very tough votes. Fixing the mess at Osawatomie and Larned State Hospitals has become a high priority given the problematic press reports on staffing and the loss of federal dollars. The Governor is requesting over \$17 million in state funds for both institutions. The Department of Children and Families is having recruitment and retention problems for social workers. After six years of no state employee salary increases, the Governor is offering a fateful bargain of a 5% pay increase if the employee switches from Classified Service to Unclassified Service. With no administrative protection for these state employees from abuse by managers, the state workforce turns into a patronage game for the elected bosses. All 125 Kansas House seats and 40 Senate seats are up for election in November. The filing deadline is June 1. The future of Kansas will be on this ballot.

REHABILITATION OF ABANDONED REAL PROPERTY BY CITIES

Senate Bill 338 revises provisions of law pertaining to the authority of cities and nonprofit organizations to petition the district court to possess abandoned property temporarily for rehabilitation purposes. Various interest groups from realtors to cities worked on this bill for several years to find a consensus. Cities like Kansas City or Wichita have thousands of abandoned homes that threaten the safety and economic value of neighborhoods. This bill gave abandoned property owners ample opportunity to find a way into compliance. Just finding many of the abandoned property owners has become a real challenge for limited city staffs. The Governor decided to veto SB 338. The Senate passed SB 338 on a vote of 32 to 8. The House voted 79 to 44. A veto override would require 27 votes in the Senate and 84 votes in the House.

VETO SESSION

The veto session starts next Wednesday – April 27. It is most difficult to predict how long this veto session will last. Initial plans made public by the leadership indicated the session would be over by Friday – May 6. The legislature was not going to wait around for a May 10th Kansas Supreme Court hearing on the school funding bill on equity that passed both chambers and signed by the Governor. If the Court rules against this school funding bill and threatens to close schools starting July 1, the Legislature and the Governor will decide if a special session is needed or let the Court take the political damage. (5 of the 7 Supreme Court justices are up for retention elections this fall.)

If the Legislature has the courage to test the Governor's resolve against raising taxes, the veto session could last much longer. Some compromise would have to be developed that melds sensible budget cuts with new revenues. This compromise would not come easy and it would take several iterations to find a plan that garners 63 House votes, 21 Senate votes and does not garner a veto by the Governor. As the days drag on, what other legislation will be worked? **House Bill 2088** - that puts a property tax lid on cities and counties - is in a conference committee where supposedly a workable compromise has been found. The Senate has passed a water bill that opens up the raiding of surplus Missouri River water for western Kansas. The House has had no debate on this controversy. The noxious weed bill – **House Bill 2479** – has been fundamentally changed by the Senate so its future is uncertain. The American Legislative Exchange Council bill to control local food policy by the legislature – **House Bill 2595** – has passed the House and now sits in the Senate Commerce committee. The Governor needs legislative approval to sell off the assets of the Kansas Bioscience Authority since the Governor has \$25 million in asset sales built into the 2017 budget. The Governor wants a 'step therapy' bill that directs using generic drugs first to save the State \$10 million in medical costs. The horse trading will be endless as legislative leadership tries to find those budget compromises to finally finish this session.