This Week in Topeka

Overland Park Chamber

Business, Economic Development & Local Government News
from the Veto Session Weeks of May 30-June 10, 2017 (and beyond)

The Veto Session finally came to a close on Saturday, June 10, the 113th day of the 2017 session. Assuming all that remains of the session is the return on June 26 for *Sine Die,* the formal adjournment, the 2017 session will tie the all-time record of 114 days set in 2015. These final two weeks saw a flurry of activity, with multiple conference committee meetings and a number of votes, many addressing the "big" issues that remained; i.e., budget, taxes, school finance and guns. At this point, of the bills dealing with those issues, only the tax bill is final; school finance, guns and budget are all waiting for the Governor's disposition.

Before providing the regular brief summary of the activity at the Capitol, there are two things to be mentioned. First is our acknowledgment of the sad and unexpected passing of freshman Rep. Patsy Terrell (D-Hutchinson) during the final week of the session. We want to share our sincere regrets and express our condolences to her family and friends; she will be missed. Our thoughts and prayers are with all during this difficult time.

And, second, the Chamber wants to thank all members of the legislature, particularly our Johnson County Delegation, who devoted so much time and energy to represent Kansans all across the state. We recognize the sacrifices each of you makes on our behalf. We also want to recognize the many staff members who make it possible for the legislators to do their work, the administrative assistants as well as members of the Legislative Research Department and the Revisor's Office, all of whom put in countless hours in support of the legislative process. Thank you for the hard work and a job well done!

Taxes and K-12 School Finance; Tax Veto Override and Governor Signs School Finance Bill. At times over the last couple of weeks it was difficult to separate discussion of tax reform from school finance, so I will try to give you a chronological update taking on major aspects of both issues more or less as they appeared in various conference committee reports (CCR).

On the first day back after the Memorial Day weekend, the Tax Conference Committee agreed on a report using HB2067 as its vehicle. That CCR included the repeal of the non-wage pass through business income exemption effective as of January 1, 2017, repeal of the march to zero income tax and reinstatement of a 3-bracket income tax schedule. That 3-bracket schedule would have resulted in rates of 3.1% for taxable income up to $30,000, 5.25% for income from $30,001 to $60,000, and 5.7% on income over $60,000 (each based on married taxpayers filing jointly). This plan would have generated estimated additional revenue of $591 million in FY2018 and $626 million in FY2019. The Senate adopted the CCR, interrupting its school finance debate in a bit of an unusual move to accommodate the House's midnight rule, and sent it on to the House where it was rejected with almost no debate.

With the failure of that tax plan, and the desire to get something moving on the K-12 funding issue, the Tax Conference Committee tried a new and different approach. Using SB19 as the shell this time, the Committee added an income tax piece to the school finance bill, dedicating all of the income tax receipts to K-12 funding in order to avoid a conflict with the "one subject rule" (i.e., the constitutional requirement that the contents of bills being considered by the legislature be limited to a single subject, in this case K-12 education funding). They also put some of the other tax-related provisions (e.g., reinstatement of some itemized deductions and the child care tax credit, repeal of several sales tax exemptions for certain non-professional services, establishment of the Ad Astra Rural Jobs Act, providing tax credits to employers regarding certain aviation and aerospace employees, and STAR bond renewal), making the effectiveness of each bill contingent upon the passage of the other. First up was the House's consideration of the CCR on SB19, which included the following key income tax provisions:

- Repeal of the income tax exemption for non-wage pass through business income effective January 1, 2017;
- Repeal of the march to zero individual income tax;
- Increase individual income tax rates effective on January 1, 2017 utilizing a 3-bracket schedule of 2.9%, 4.9% and 5.2%, increasing on January 1, 2018 to 3.1%, 5.25% and 5.6%, on taxable income brackets of 0-$30,000, $30,001-$100,000, and $100,001 and above, respectively;
- Reduce the low income exclusion threshold from $12,500 to $5,000 (married filing jointly) and from $5,000 to $2,500 (single filers) beginning January 1, 2018; and
- Repeal of the sales tax exemption for several non-professional services.

This bill would have raised an additional estimated $531.6 million ($505 million income tax and $17.6 million sales tax) in FY2018 and $575 million ($539.7 million income tax and $26.6 million sales tax) in FY2019. The CCR on SB19 was considered first in the House where it failed on a vote of 32-91, thereby killing that version of SB19 and making its companion bill, SB30, moot, and it was back to the drawing board for the Tax Conference Committee.

Next up, the Committee negotiated a different version of the tax plan, gutted SB30 and inserted the new plan in that shell, a plan that would raise an estimated additional $591 million in FY2018 and $633 million in FY2019. Key provisions in the CCR for SB30 included:

- Repeal of the income tax exemption for non-wage pass through business income effective January 1, 2017;
- Allow taxpayers to claim certain non-wage business income losses as allowed under federal tax law beginning in 2017;
- Repeal of the march to zero individual income tax;
- Increase individual income tax rates effective on January 1, 2017 utilizing a 3-bracket schedule of 2.9%, 4.9% and 5.2%, increasing on January 1, 2018 to 3.1%, 5.25% and 5.7%, on taxable income brackets of 0-$30,000, $30,001-$60,000, and $60,001 and above, respectively (it's also worth noting that while these rates are higher than the current 2-bracket schedule, they are still lower than what was in place in 2012 before the massive, and ill-advised tax cuts – 3.5%, 6.25%, and 6.45%);
- Reduce the low income exclusion threshold from $12,500 to $5,000 (married filing jointly) and from $5,000 to $2,500 (single filers) beginning January 1, 2018;
- Itemized deductions for medical expenses, mortgage interest and property taxes paid would be allowed at 50% of the federal allowable amount in 2018, increasing to 75% in 2019 and 100% in 2020 and thereafter;
- Reinstate the child care and dependent care tax credit at 12.50% of the federal allowable amount in 2018, increasing to 18.75% in 2019 and 25% in 2020 and thereafter; and
- Extend the sunset for the STAR bonds program from July 1, 2017 to July 1, 2020, imposing a moratorium; however, on creation of any new STAR bond districts in the first year of the 3-year extension (all STAR bond districts created prior to the one year moratorium could continue to use STAR bonds to develop projects in those districts).

One interesting aspect of this new CCR was the Committee's decision to eliminate the Ad Astra Rural Jobs Act, the aviation/aerospace tax credit program and the repeal of sales tax exemptions on several non-professional services, all as had been included in the CCR on SB19 previously considered and rejected by the House.

Again, the House was the first to run the new tax plan in the CCR on SB30 and passed it 69-52 on Monday, June 5. Later the same evening (much later, actually about 12:30 on Tuesday morning) the Senate also adopted the CCR by a vote of 26-14. About 30 minutes later, the Governor's office sent out a press release confirming what most believed, that he would veto the tax bill, doing so later on Tuesday morning, June 5th, setting up the anticipated confrontation as the legislature prepared to consider an override of the Governor's veto later the same day. **First to take up the override was the Senate. Needing 27 votes, the final tally**

was 27-13, right on the number. The House followed the Senate's lead, voting 88-31 to override, four votes more than the minimum needed; the new tax plan would become law notwithstanding the Governor's veto.

Nineteen of twenty-five House members and five of nine Senators in the Johnson County Delegation voted to override the Governor's veto; in the opinion of the Chamber, a much needed step in getting the state back on sound financial footing. It appears that Moody's Investor Service agreed, quickly revising its Kansas bond rating outlook from negative to stable, stating, in part, that the upgrade "is the result of a significant income tax increase the state passed earlier this week." Moody's went on to say that the increased revenues will reduce the state's fiscal problems.

Also on Monday, June 5, the legislature considered the CCR that used SB19 as its shell to set out the plan for K-12 funding, including the new finance formula mandated by the Supreme Court. While not without some debate and disagreement, largely focusing on whether the overall amount of new funding was enough to be deemed constitutionally acceptable by the Court, both chambers adopted the CCR for SB19. The House voted 67-55 in favor, and the Senate agreeing 27-13, sending the bill to the Governor with the Court's June 30 deadline approaching.

It seems the votes generally split two ways. Those voting in favor were heard saying that while the plan was not perfect and had aspects that were somewhat troubling, they did not want to let the perfect be the enemy of the good. This plan appeared to represent a real serious effort by many in the legislature to begin serious steps toward correcting what the Court had ruled was a real problem. In view of all of the circumstances; e.g., the realities of the financial challenges facing the state in addition to school funding and the political realities attached to their attempts to address those challenges, as well as the urgent need for some resolution as the school districts all across the state were well into their own budget processes without the advantage of knowing what the funding resolution would be; it was time to send the results of a sincere effort to the Supreme Court.

On the other hand, many members voting against SB19 said they did so because of a sincere belief the plan did not include enough additional money to be deemed by the Court to be constitutionally adequate. No one knows for sure how this legitimate concern will turn out until the Court issues its ruling.

Hopefully, the Court will recognize the political realities this legislature faced, while also understanding the changed makeup of the legislature and the work it did this session will be evidence enough of its willingness to make the difficult decisions asked of them by the majority of those voters who sent them to the Capitol last fall and give them the opportunity to continue to help strengthen public education in Kansas by taking additional incremental steps forward. Forcing the infusion of $500 million, $800 million, $1 billion more into K-12 funding at a time where the state is digging out of a deep financial hole while still dealing with a generally stagnant economy at the expense of other well-founded challenges could very well have unintended consequences, including a possible voter backlash in upcoming elections.

On June 15, a press release was issued with the good news that Governor Brownback had, in fact, signed SB19 into law. Now everyone (including schools all across the state who are well in to the budgeting process for the upcoming school year) must wait for the new plan, both the underlying formula and the amount of money put into it, to be reviewed by the Supreme Court in the context of the adequacy part of the *Gannon* case and issue its opinion as to its constitutionality.

Highlights of the new plan, designated in the bill as The Kansas School Equity and Enhancement Act, include:

- Provides additional funding of approximately $195 million in school year 2017-18 and an additional sum of approximately $100 million in school year 2018-19, resulting in a total infusion of nearly $500 million over the next two school years ;
- Increases the base state aid per student to $4,006 for school year 2017-18, $4,128 for school year 2018-19, and adjusted each school year thereafter by the average Consumer Price Index-All Urban Consumers, Midwest (CPI) for the immediately preceding three school years;
- Funds all-day kindergarten by counting students enrolled as 1.0 FTE (up from 0.5);
- Retains the local option budget (LOB) authority, capped at 33%, and increasing the artificial base amount used to calculate the LOB authority, currently $4,490, according to the average CPI for the immediately preceding three school years;
- Reauthorized the 20 mill statewide property tax levy dedicated to K-12 funding for two years, retaining the $20,000 homestead exemption;
- Continues to permit abatement of the 20 mills for purposes of economic development programs, but prohibits abatement of the 8 mill capital outlay levy;
- Continues to define "at risk" students as those who are eligible to receive free lunch, increases the weighting used to adjust the FTE count from 0.456 to 0.484 as recommended by Legislative Post Audit, and establishes a floor for a district's at-risk count at 10% of that district's total number of students;

- Adds utility fees, property and casualty insurance premiums, and maintenance costs associated with existing fixtures and permissible expenditures for which capital outlay funds may be used;
- Changes the Tax Credit for Low Income Students Scholarship Program by requiring private schools to be accredited by July 1, 2020 in order to participate in the Program, allowing individuals and LLC's to make contributions to the Program (previously only corporations could be contributors) subject to an annual cap of $500,000; and
- Sunsets the formula on July 1, 2027.

State Budget. As you know, Kansas recently moved to a two-year budget cycle in which the legislature analyzes and prepares annual budgets for state spending for the upcoming two years every other session. This session marked the time for preparing budgets for FY2018 (which begins on July 1) and FY2019, and finalizing those budgets was the last legislation that this legislature passed before adjourning until *Sine Die.*

On Saturday, June 10th, after several days of conference committee negotiations, both the Senate and House passed the budget bill, Senate Sub for HB2002, by strong margins, the Senate voting 27-11 to adopt the CCR on the bill followed by the House vote of 88-27. The bill has been enrolled and was sent to the Governor on June 15th, beginning the ten days in which he has to either sign or veto the bill, or he can simply let it become law on the expiration of the 10-day period by simply doing nothing (just as he did with the gun bill discussed next). We are betting against a veto.

The bill provides for total spending of just over $15.5 billion in FY2018, including nearly $6.4 billion of state general funds. For FY2019, the budget anticipates a total of $15.8 billion that includes about $6.3 billion from the state general fund. The state is projected to have ending balances of approximately $157 million (2.5%) and $209 million (3.3%) for FY2018 and FY2019, respectively.

A few highlights in the upcoming budget:

- Eliminates 179.5 FTE positions from state government across the state;
- Provides most state employees their first pay raise in nine years, calling for a 2.5% increase for those having been employed by the state for fewer than five years, while those with over five years of service will receive a 5.0% increase;
- Includes additional funding for operation of the state's hospitals, including funds for 20 additional patient beds at Osawatomie State Hospital, as well as more funds for senior care, domestic violence prevention and safety net clinics;

- Increases the cap on KDOT's bonding authority by $400 million, stipulating that bond funds raised be used for maintenance and repair of state transportation infrastructure over the next two years; and
- Restores some of the funding to KU and K-State that resulted from disproportionate cuts imposed on those universities during the last legislative session.

Guns; Governor Allows the Bill to Become Law Without His Signature.

The legislature was able to tiptoe through what appeared to be a particularly fragile situation and pass HB2278 that would continue to permit state and municipal-owned medical care facilities and adult care homes, community mental health centers, indigent health care clinics and the KU Medical Center to prohibit the carrying of concealed handguns in buildings and public areas of their institutions after the pending July 1, 2017 sunset of current law without having to invest in, install, and maintain metal detection equipment and staff them with additional trained security personnel. On Thursday, June 1, the Senate voted in favor of the bill, 24-16; later the same day, the House also passed HB2278 by a 91-33 vote. And Governor Brownback chose to let this bill become law without his signature by holding it for the entire 10-day period during which he has the option of signing or vetoing a bill.

Unfortunately, the tenuous grouping of "yes" votes, especially in the Senate, caused the decision to be made to keep the bill clean and not add amendments that risked alienating enough members who supported it, thereby doing all possible to pass the bill. This was probably the right decision, but it does mean that on July 1, 2017, Kansas colleges and universities will have to allow concealed carry on their campuses unless they choose to implement the additional security required by current law.

Upcoming events:

Public Policy and Advocacy Committee Meeting. The next meeting of this committee will be noon-1:30 p.m. on Friday, **June 23,** at the Overland Park Chamber office. We will begin discussing what to include in the Johnson County Delegation's Voting Record for the 2017 Legislative Session.

Registration information and further details for the meeting can be found at www.opchamber.org.