

IMPACT OF AN AUSTERE FISCAL POLICY

*Prior Policy Choices Frame Questions
About Long-Term Implications for Kansas*

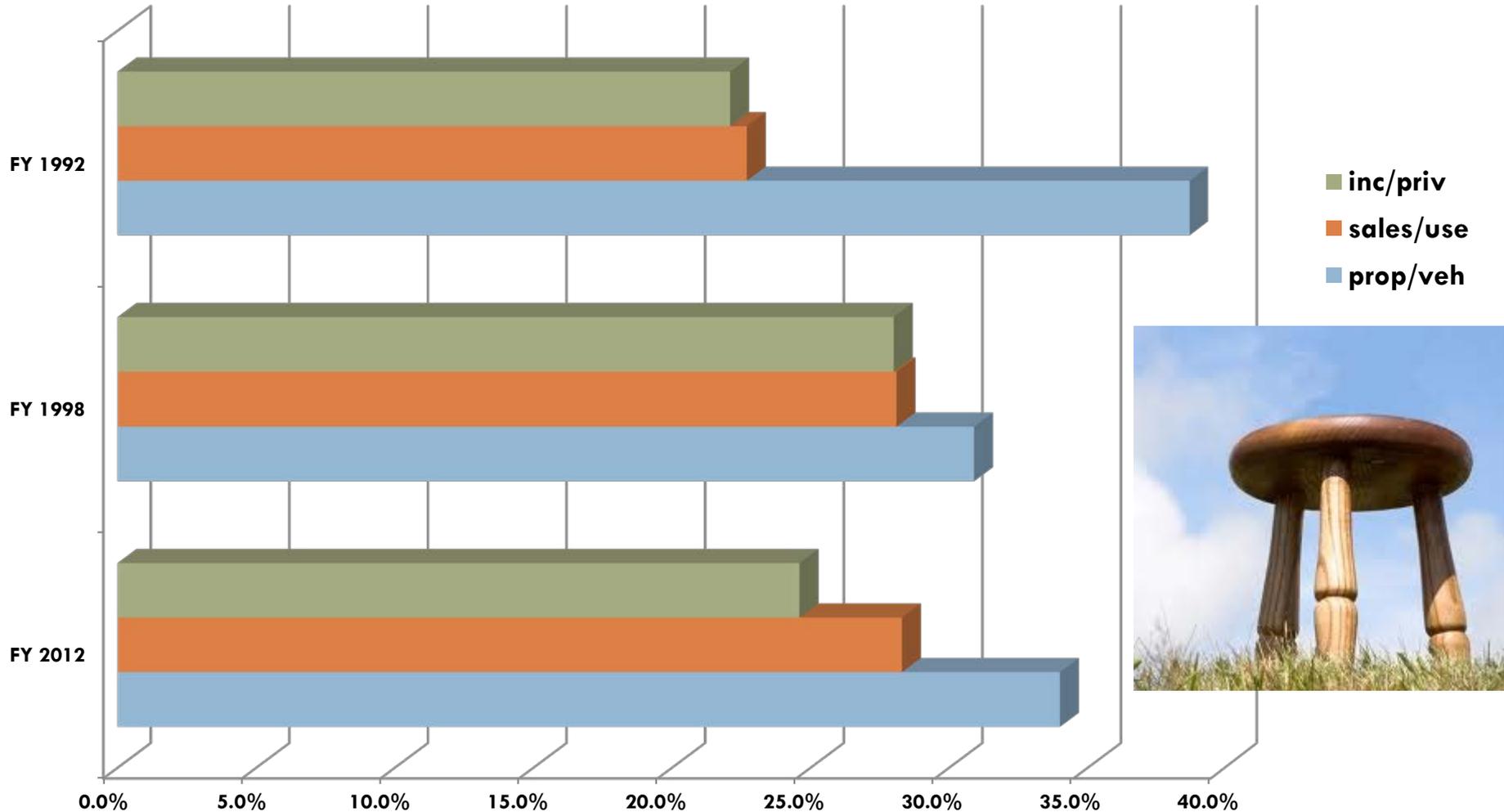
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Kansas Economic Policy Conference
University of Kansas – October 13, 2016

3 Legs of State/Local Finance “Stool”

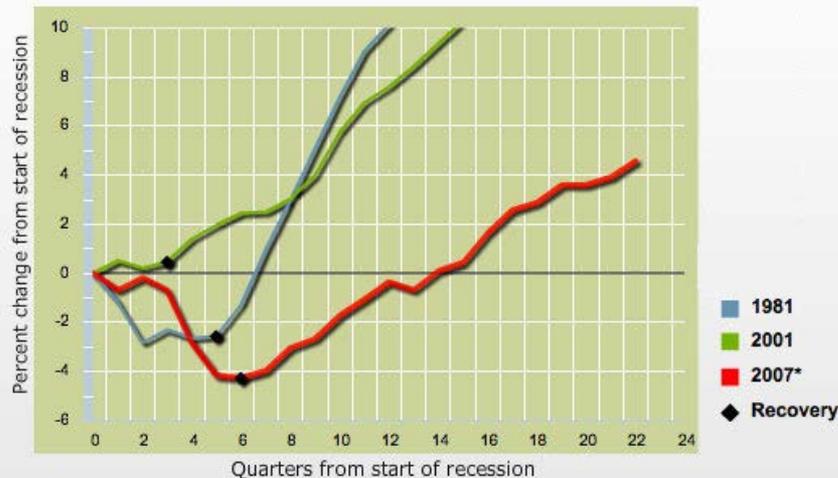
(Percent of State and Local Taxes by Source for Selected Years)



Great Recession Likely Triggered Change in Thinking About Tax Policy



Change in U.S. Output: Recessions

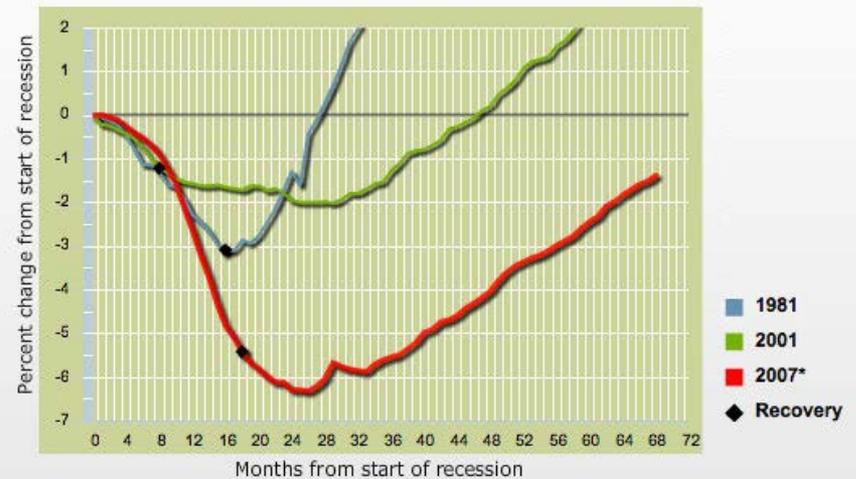


*Start of the recovery for the 2007 recession is June 2009 (the second quarter).

Source: Federal Reserve Bank of Minneapolis

Updated August 29 2013

Change in U.S. Employment: Recessions



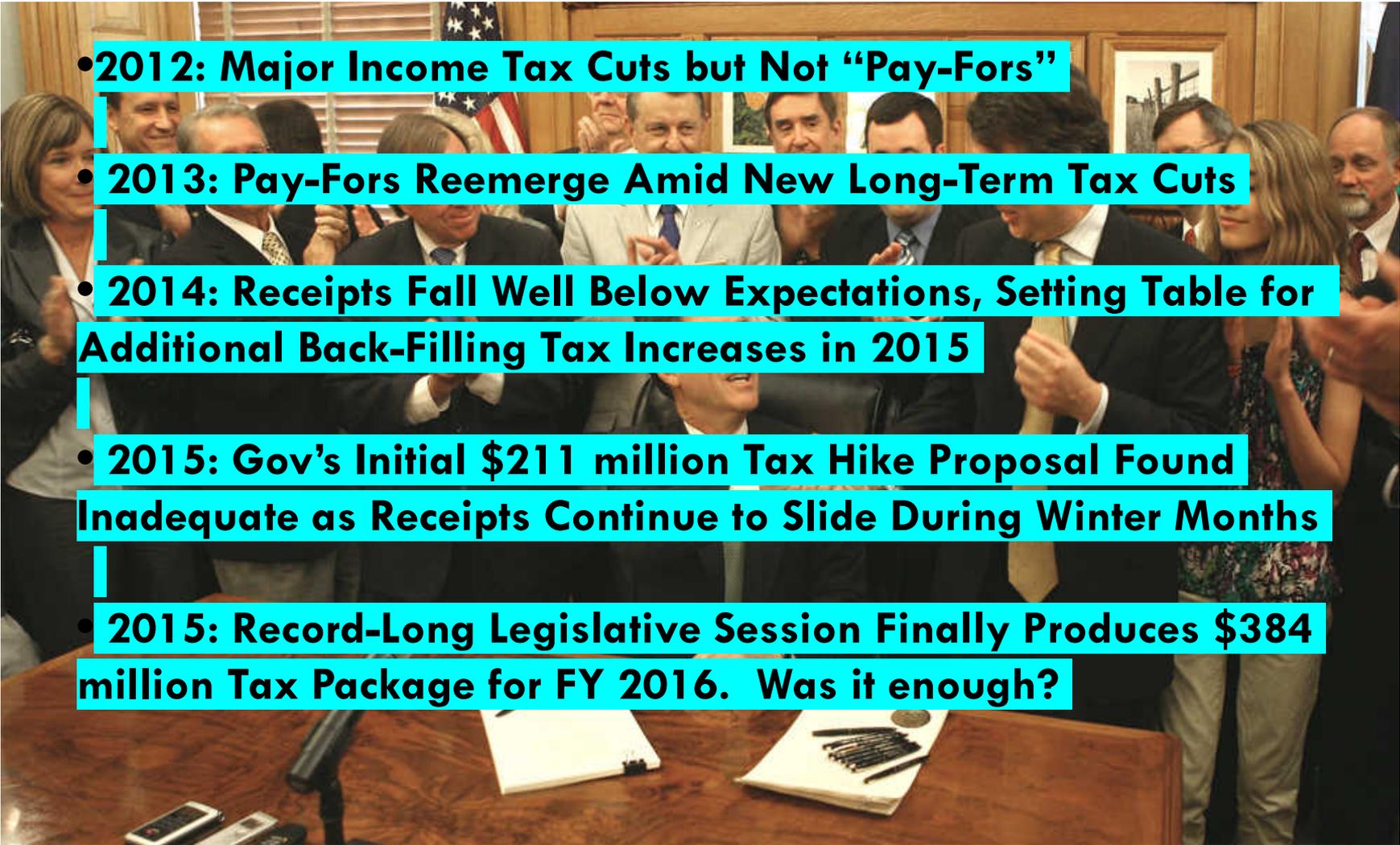
*Start of the recovery for the 2007 recession is June 2009.

Source: Federal Reserve Bank of Minneapolis

Updated September 6 2013



2012-15: Many Tax Policy Changes

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- A group of people, including men and women in business attire, are gathered around a wooden conference table. Some are clapping. The scene is set in a room with wood-paneled walls and an American flag in the background. Overlaid on the image are six cyan text boxes with black text, each preceded by a bullet point. The text boxes contain the following information:
- 2012: Major Income Tax Cuts but Not “Pay-Fors”
 - 2013: Pay-Fors Reemerge Amid New Long-Term Tax Cuts
 - 2014: Receipts Fall Well Below Expectations, Setting Table for Additional Back-Filling Tax Increases in 2015
 - 2015: Gov’s Initial \$211 million Tax Hike Proposal Found Inadequate as Receipts Continue to Slide During Winter Months
 - 2015: Record-Long Legislative Session Finally Produces \$384 million Tax Package for FY 2016. Was it enough?

Selected Major Policy Changes

Individual Income Tax Brackets, Married Filing Jointly

	<u>1992-2012</u>	<u>2016-17</u>	<u>2018-20</u>	<u>2021-</u>
\$0-30k	3.50%	2.70%	2.60%	“Glide- Path” Formula
\$30k-60k	6.25%	4.60%	4.60%	
\$60k+	6.45%	4.60%	4.60%	

Note: All non-wage business income exempt since 2013.

Sales Tax increase from 5.70% to 6.15% to 6.50%

Cigarette Tax increase from \$0.79 to \$1.29/pack

Food sales tax rebate credits made non-refundable

2016: No (More) New Taxes ...



Election Year with all 165 legislative seats on ballot

Governor said he would not put new revenues back on table in 2016 -- and did not. No major tax action taken.

But growing number of lawmakers publicly calling for changes to non-wage business income exemption.

Is fiscal crisis ongoing and institutionalized? Policy goal of sawing off income tax leg of stool in favor of extending sales/excise tax leg. Has it worked?

Est. Impact, 2012-15 Tax Changes

(\$ in millions)

	<u>FY 13</u>	<u>FY 14</u>	<u>FY 15</u>	<u>FY 16</u>	<u>FY 17</u>	<u>FY 18</u>	<u>6-yr total</u>
Individual Income Tax	(\$249.2)	(\$733.1)	(\$885.9)	(\$848.8)	(\$919.5)	(\$949.1)	(\$4,585.5)
Sales/Use Tax	\$0.0	\$193.2	\$218.7	\$391.1	\$422.1	\$438.0	\$1,663.1
Severance Tax	\$18.0	\$45.0	\$60.0	\$70.0	\$75.0	\$80.0	\$348.0
Cigarette, E-Cig Tax				\$40.4	\$38.4	\$38.0	\$116.8
Tax Amnesty				\$30.0			\$30.0
Total	(\$231.2)	(\$494.9)	(\$607.2)	(\$317.3)	(\$384.0)	(\$393.1)	(\$2,427.6)

Source: Kansas Department of Revenue

Other Issues Impact Fiscal Outlook

Are we seeing a recent acceleration of the long-term decline in sales tax revenue elasticity? (Internet, services, multiple exemptions)

Mississippian Lime oil play not as big as anticipated (Enhanced severance taxes were to be major “pay-for” for income tax cuts)

Key sectors of state’s economy have been struggling and are likely expected to do so for foreseeable future. (Energy, agriculture)

Late September BEA revision of state personal income data determining Kansas’ Federal Medical Assistance Percentage (FMAP) has declined for FY 2018, effectively reducing the share of Medicaid costs which will be paid by the federal government

State General Fund Overview

(\$ in millions)

	<u>FY 2011</u>	<u>FY 2012</u>	<u>FY 2013</u>	<u>FY 2014</u>	<u>FY 2015</u>	<u>FY 2016</u>	<u>FY 2017 (est)</u>
Beginning Balance	(\$27.1)	\$188.3	\$502.9	\$709.3	\$379.7	\$71.5	\$33.7
Final Receipts	\$5,882.1	\$6,412.7	\$6,341.1	\$5,653.2	\$5,928.8	\$6,073.5	\$6,326.0
Available Revenue	\$5,855.0	\$6,601.0	\$6,844.0	\$6,362.5	\$6,308.5	\$6,145.0	\$6,359.7
Expenditures	\$5,666.7	\$6,098.1	\$6,134.8	\$5,982.8	\$6,237.0	\$6,111.3	\$6,360.3
Ending Balance	\$188.3	\$502.9	\$709.3	\$379.7	\$71.5	\$33.7	(\$0.6)
% of Expenditures	3.3%	8.2%	11.6%	6.3%	1.1%	0.6%	0.0%
Receipts>Expenditures	\$215.4	\$314.7	\$206.3	(\$329.6)	(\$308.2)	(\$37.8)	(\$34.3)

Estimates for FY 2017 as of September 7, 2016.

The “Bank of KDOT” ...

What are long-term implications?

Hundreds of millions annually in fund sweeps from KDOT’s State Highway Fund – money previously earmarked for the “T-Works” (comprehensive transportation program).

Some history: Widespread belief that early 1990s recession not as bad in Kansas as nationally because of construction and spending going from major 1989 highway program.



ARRA: Federal 2009 Legislation

This Keynesian notion (government spending as fiscal stimulus) was an important component in the debate at the federal level over ARRA and how to best resuscitate the economy – shovel-ready public sector spending versus tax cuts.



Given the More Austere Reality ...

Given the accelerating propensity to divert KDOT money and potentially delay or even cancel certain infrastructure spending that otherwise would have occurred, some have begun asking if the state is missing out on economic expansion from these expenditures? And in the long run, of course, there is the argument that investing in and building a stronger infrastructure is better for economic development in the first place.



Demographic/Fiscal Issues Combine

As a result of aging population (especially rural), many school districts find it more challenging to get bond issues approved by voters than they did several decades ago. Retired, fixed-income seniors whose children left local K-12 schools many years ago may not feel as connected to their school districts.

grandparents day 



State/Local Partnership Issues

Three legs to stool notion necessitated a strong state-local partnership. Now that the effort has been made to significantly shorten the income tax leg of the stool, is there more pressure on the other two legs?



Sales tax has gone up twice at the state level, and to the extent that local units are feeling the squeeze and demands for additional services, especially in rural and slow-growth areas, are property tax increases going to further dis-equalize the stool and lead to additional state-local partnership tensions?

The 2017 Session ...



Is a third major (admittedly back-filling) tax increase possible in last 4-5 years?

How much public tolerance might there be for more increases, especially sales tax?

Where would any new K-12 money mandated by courts come from? Given the more austere reality, what are implications for non K-12 areas of budget if more school spending is needed?