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To: House Taxation Committee
From: Mark Tomb, VP of Governmental Affairs
Date: January 29, 2020

Re: Testimony in Support of HB 2005

Honorable Chairman Johnson and members of the committee:

On behalf of the Kansas Association of REALTORS® (KAR), thank you for the opportunity to appear before you today to express support for HB 2005, which would allow Kansas income tax filers the ability to take state level itemized deductions regardless of whether they take the standard deduction or itemize on their federal returns. Through the comments expressed herein, we hope to provide additional legal and public policy context to the discussion on this issue.

KAR represents over 10,000 members involved in residential, commercial and agricultural real estate and has advocated on behalf of the state's property owners for nearly 100 years. REALTORS® serve an important role in the state's economy and are dedicated to working with our elected officials to create better communities by supporting economic development, a high quality of life and providing affordable housing opportunities while protecting the rights of private property owners.

REALTORS® believe that the private ownership of real property is the foundation of our nation's free enterprise system. Homeownership is the cornerstone of the American Dream and deserves a preferred place in our system of values as it contributes to community responsibility; business, civic, and economic stability; family security; and quality of life. We believe every family deserves a decent home and a suitable living environment and our members are committed to helping every single citizen, who so desires, to realize the American Dream of homeownership. It is because of these beliefs that REALTORS® strongly support policies that prioritize private property ownership. As such, private property ownership, specifically homeownership, deserves a preferred place in our Kansas tax policy.

<u>Summary of the Current Law and Issue Before the Committee</u>

Current Kansas law provides that, "[i]f federal taxable income of an individual is determined by itemizing deductions from such individual's federal adjusted gross income, such individual may elect to deduct the Kansas itemized deduction in lieu of the Kansas standard deduction."[1] In other words, Kansas income tax filers may only itemize deductions on state income tax filings if they itemize on their federal return. Due to the doubling of the federal standard deduction late in 2017, very few Kansas taxpayers will benefit from the itemized deductions provided in Kansas tax law (charitable, mortgage interest, property taxes and medical).

To avoid an ongoing state income tax increase on Kansans that historically took the Kansas itemized deductions, the Kansas Legislature needs to allow individuals the option of itemizing deductions on Kansas tax

[1] Kan. Stat. Ann. §79-32,120(a)(1)(Supp. 2018).

filings regardless of whether or not an individual's federal return allows itemized deductions. This may be accomplished by adding to K.S.A. 79-32,120(a)(1) the following language:

> *For tax year 2018, and all tax years thereafter, an individual may elect to deduct the Kansas itemized deduction in lieu of the Kansas standard deduction regardless of whether or not such individual's federal taxable income is determined by itemizing deductions from such individual's federal adjusted gross income.*

Section 1 of HB 2005 provides this language, this was also the same language that was included in Section 2 of SB 22, a broad based tax reform bill that was passed in 2019 but was vetoed by the Governor. The tax year for this to start is an important policy choice for the legislature to make. As written, the bill allows for taxpayers to file an amended return by what is now an obsolete date of December 31, 2019. HB 2005 (and the same provisions included in SB 22) were intended to allow immediate relief allowing those impacted to begin with tax year 2018. REALTORS® are advocating for the dates in this legislation to be amended to allow those impacted to file an amended return for tax year 2019 by the end of this calendar year. First and foremost, this change needs to occur moving forward. The longer this issue is not addressed, the more likely meaningful change will never occur for these taxpayers.

Kansas Legislative History on Itemized Deductions

Repeatedly, the policy of whether to allow itemized deductions for Kansas income taxes has been brought before the Kansas Legislature. On all prior occasions, after lawmakers reviewed the policy rationale for the deductions, the Legislature preserved Kansans' ability to take these deductions. For example, in 2012, as part of the early tax packages that were recommended by the administration at the time, the Kansas itemized deductions were targeted for full repeal. Kansas REALTORS® strongly objected and the Legislature responded by preserving these tax benefits for Kansas homeowners.

During the 2013 legislative session, the Kansas Legislature enacted HB 2059, which made number of significant changes to Kansas itemized deductions. Of these changes were systematic reductions, or "haircuts", to these historic deductions. Under 2013 HB 2059, mortgage interest (MID) and property tax (PTD) deductibility were as follows: 100% in tax year 2012, 70% in tax year 2013, 65% in tax year 2014, 60% in tax year 2015, 55% in tax year 2016, 50% in tax year 2017 and 50% in tax year 2018. The intent was that as individual income tax rates stepped down, the MID and PTD would as well. This was a preferable alternative to immediate loss of these important deductions, which the Legislature was being asked to do.

Tax legislation passed in 2015 accelerated, but froze the deductibility to 50% starting in tax year 2015, where both deductions stood for tax years 2017 and 2018. During the 2017 legislative session, the Legislature engaged in extensive tax reform debate. During the discussions, KAR sought restoration of the PTD and MID. This was based upon KAR's growing concern that many of the tax proposals circulating at the time increased individual rates but failed to restore, even partially, either of these critical deductions. The Legislature responded in passing legislation that put both deductions, along with the medical deduction, on a path to full restoration by 2020.

Federal Tax Reform of 2017 – Unintended Kansas Income Tax Increase on Middle Class Homeowners

On December 22, 2017, President Trump Signed the "Tax Cuts and Jobs Act". As it relates to Kansas itemized deductions, federal reform modified the federal MID by putting a limit on deductible mortgage debt at a $750,000 cap. Furthermore, the state and local tax itemized deduction, which included property taxes paid on real property, was capped at $10,000. However, the provision affecting Kansas homeowners and their ability to deduct mortgage interest and property taxes from their Kansas income tax, was the federal provision doubling the standard deduction. According to the National Association of REALTORS®, by doubling the standard deduction, Congress has greatly reduced the value of the mortgage interest and property tax deductions as tax incentives for homeownership. Congressional estimates indicate that only 5-8% of filers will now be eligible to claim these deductions by itemizing, meaning there will be no tax differential between renting and owning for more than 90% of taxpayers.

Based upon IRS data from 2016, nearly 250,000 Kansans took the MID and over 300,000 claimed the PTD.[2] Of filers that took the federal MID, PTD, and charitable deductions in tax year 2016, about half had adjusted gross incomes of less than $100,000. It is this segment of taxpayers that will no longer qualify for current state itemization because they fall short in federal itemized deductions. It is important that middle class Kansas homeowners continue to be able to claim these deductions regardless of whether they are in a position to itemize federally. The following tables show the breakdown, by adjusted gross income, of Kansas taxpayers that took the federal itemized deductions in 2016 for mortgage interest and property taxes.

Share of Taxpayers who used the mortgage interest deduction by AGI category (Kansas)

$1 under $10,000	$10,000 under $25,000	$25,000 under $50,000	$50,000 under $75,000	$75,000 under $100,000	$100,000 under $200,000	$200,000 under $500,000	$500,000 under $1,000,000	$1,000,000 or more
1.1%	3.1%	11.0%	16.1%	16.9%	38.2%	11.5%	1.6%	0.5%

Share of Taxpayers who used the property tax (real estate) deduction by AGI category (Kansas)

$1 under $10,000	$10,000 under $25,000	$25,000 under $50,000	$50,000 under $75,000	$75,000 under $100,000	$100,000 under $200,000	$200,000 under $500,000	$500,000 under $1,000,000	$1,000,000 or more
1.7%	4.6%	12.0%	16.1%	16.1%	35.6%	11.6%	1.8%	0.7%

Kansas Voters Support Proposals to Protect the Itemized Deductions

In addition to the strong legislative history that supports these itemized deductions, KAR is led to believe that Kansans strongly support the deductions. Our belief of this public support is driven by a recent poll of registered voters in Kansas conducted by American Strategies, Inc. for KAR.[3]

This polls showed that most Kansans believe that the state home mortgage interest deduction is a factor in the decision to buy a home and that weakening the deduction would have an adverse effect on the state housing market and overall Kansas economy. Furthermore, voters strongly support the mortgage interest deduction and agree that the “tax windfall” from federal tax reform should be returned to taxpayers. Other findings:

- 70% of Kansas voters say the mortgage interest deduction is a factor in encouraging homeownership.
- Nearly two-thirds see elimination of the state mortgage deduction as a negative for both the housing market (63%) and the overall Kansas economy (64%).
- **Overwhelming support (72%) for a proposal to change the Kansas tax law so that families and individual who take the new federal standard deduction can itemize on their state income taxes.**

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[2] https://www.irs.gov/statistics/soi-tax-stats-historic-table-2.

[3] American Strategies designed and administered this telephone survey conducted by professional interviewers. The survey reached 600 adults, age 18 or older, who indicated they were registered to vote in Kansas and voted in the November 2018 midterm election. The data were weighted to ensure an accurate reflection of the population. The survey was conducted from December 6 to 8, 2018. The overall margin of error is +/- 4.0%.

This support was strong across party lines with **73% of Democrats** and **74% of Republicans** supporting the proposal to change Kansas tax law to allow Kansas families the ability to continue to take the state itemized deductions regardless of whether they take the federal standard deduction.

Return on Investment

Strong homeownership provides returns to the state and local communities through economic and social benefits. In 2017, the real estate industry accounted for more than $24 billion, or 15.4% of the gross state product, for the Kansas economy.[4] Each home sale generates income from the transaction in the form of construction cost, brokerage fees, inspection cost, mortgage lending and insurance. This income is re-circulated into the economy, amplifying its impact. KAR estimates, that for the sale of a median priced home in Kansas, there is $61,095 of economic impact.[5]

In 2016, NAR published a paper that reviewed the existing academic research on the social benefits of homeownership.[6] In addition to the economic benefits, "homeownership brings substantial social benefits for families, communities, and the country as a whole."[7] This paper demonstrated that stable housing through homeownership fostered positive outcomes for educational achievement; civic participation; health benefits; reduced crime; less reliance on public assistance; and property maintenance and improvement. Given the economic and social benefits of homeownership to Kansas, the Legislature should support policies that encourage and sustain strong homeownership. Tax benefits specifically for homeownership, such as the mortgage interest and property tax deductions, should be prioritized.

Conclusion

Legislative history and public sentiment toward these deductions provide strong guidance for Kansas lawmakers in responding legislation related to federal tax reform. Economic growth depends on a stable investment environment with a consistent tax code. Since 2012, the Kansas Legislature has passed a series of alterations to Kansas tax policy followed by a repeal of many of those measures in 2017. Throughout the turmoil, Kansas lawmakers have preserved the ability of Kansans to claim the mortgage interest and property tax deductions on state income tax returns.

As mentioned, in 2017, the Kansas Legislature put both of these deductions on a path to full restoration. Failure to act now would result in a significant number of Kansans losing these tax benefits while invalidating years of legislative intent that these deductions be available and preserved in Kansas tax law. The mortgage interest deduction and property tax deduction are favorable tax policies for Kansas homeowners. The State of Kansas should be encouraging homeownership, rather than making homeownership harder. These deductions not only make homeownership more affordable, they recognize the critical importance of the housing industry to the Kansas economy.

Thank you for the opportunity to appear and provide testimony on our support for HB 2005. KAR request that the House Taxation Committee act on HB 2005 favorably.

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[4] Copyright © 2017 "Economic Impact of a Home Sale in Kansas." *NATIONAL ASSOCIATION OF REALTORS®.* All rights reserved. Reprinted with permission. January 25, 2019, https://www.nar.realtor/sites/default/files/documents/2019-01-State-Economic-Impact-KS-01-08-2019.pdf.

[5] *Id.*

[6] Yun, L., & Evangelou, N. (2016). Social Benefits of Homeownership and Stable Housing. National Association of REALTORS®. https://www.nar.realtor/research-and-statistics/research-reports/social-benefits-of-homeownership-and-stable-housing.

[7] *Id*. at 1.