



Date: January 29, 2013

To: Senate Assessment & Taxation Committee
Senator Les Donovan, Chairman

From: Doug Wareham, Senior Vice President-Government Relations

Re: Amendment Request – S.B. 78 & S.B. 79

Mr. Chairman and members of the committee, I am Doug Wareham appearing on behalf of the Kansas Bankers Association (KBA). Our organization's membership includes 99% (286 of 289) of the commercially chartered banks in Kansas that provide financial services to Kansans in more than 400 cities and towns across Kansas.

We appreciate the opportunity to appear before this committee to request a specific amendment to address what we view as an unintended consequence of last year's tax reform package (House Bill 2117), which was signed into law by Governor Brownback on May 22, 2012. For the record, our organization supported the tax relief provisions contained in H.B. 2117, but upon closer scrutiny last summer, we found that Kansas banks organized as S corporations did not fare as well as other flow-through (Sub S) businesses.

As you are all well aware, the tax reform package adopted last year eliminated state income taxes on non-wage business income for small businesses organized as Sub S Corporations, LLC's or Sole Proprietorships. In spite of the fact that roughly 2 out of 3 banks in Kansas are organized as S corporations, this policy change did NOT benefit our industry. Kansas banks, including those organized as S corporations, are subject to the Privilege Tax; a special income-based tax that is collected from all Kansas banks. The Privilege Tax is collected from banks organized as S corporations before income is passed through to shareholders. Therefore, banks and more specifically bank holding company shareholders did NOT benefit from last year's elimination of income taxes on S corporations.

While the exclusion of S corporation banks from the tax relief contained in last year's tax reform package was not initially viewed as a negative (we would have accepted the status quo for Kansas banks and their shareholders), we learned last summer that House Bill 2117 also contained provisions that eliminated the ability of S corporation bank holding company shareholders to deduct their share of the holding company's tax loss on their individual Kansas income tax returns. **The loss of this deduction, according to an estimate from the Kansas Department of Revenue, amounted to a \$2.5 million tax increase for S corporation bank holding company shareholders in Kansas.**

Last summer a number of CPA firms began notifying their banking clients of the increased tax burden they would face in the wake of H.B. 2117. One of those firms shared this statement with their banking clients:

“It seems as though S-Corp banks are getting hit from both sides, the bank still has to pay tax on income in the form of the privilege taxes, yet the shareholders are no longer able to take advantage of holding company deductions.”

The language contained in our proposed amendment is specifically designed to allow loss deductions for S corporation bank holding company shareholders, as they were allowed prior to the adoption of House Bill 2117 last year. We hope this committee will recognize the unique nature of the privilege tax paid by S corporation banks. Income taxes for S corporation banks did not go away, and the loss of this deduction amounted to an inadvertent tax increase for their shareholders.

Once again, thank you for the opportunity to appear before this committee and we would respectfully request that our proposed amendment be included as part of the state legislature's 2013 tax reform package.

HB 2117

Section 12(b)(xix) For all taxable years beginning after December 31, 2012, the amount of any: (1) Loss from business as determined under the federal internal revenue code and reported from schedule C and on line 12 of the taxpayer's form 1040 federal individual income tax return; (2) loss from rental real estate, royalties, partnerships, S corporations **except those with wholly owned subsidiaries subject to the Kansas privilege tax**, estates, trusts, residual interest in real estate mortgage investment conduits and net farm rental as determined under the federal internal revenue code and reported from schedule E and on line 17 of the taxpayer's form 1040 federal individual income tax return; and (3) farm loss as determined under the federal internal revenue code and reported from schedule F and on line 18 of the taxpayer's form 1040 federal income tax return; all to the extent deducted or subtracted in determining the taxpayer's federal adjusted gross income. For purposes of this subsection, references to the federal form 1040 and federal schedule C, schedule E, and schedule F, shall be to such form and schedules as they existed for tax year 2011, and as revised thereafter by the internal revenue service.