

January 4, 2010

**Update to Analysis of Kansas Corporate Income Tax Dated October 14, 2004
To Reflect Tax Year 2007 Sample Data**

The Analysis dated October 14, 2004 focused on the Kansas corporate income tax during tax years 2000, 2001 and 2002 and the impact of the 4 largest business income tax credit incentive programs on corporate income tax receipts, in an effort to determine how the corporate income tax burden falls within various industry sectors. This Analysis has been annually updated to reflect sample corporate income tax data from the new tax year. Attached are updates to Tables 2 and 3 of the Analysis, to reflect tax year 2007 sample data. The discussion of the Top 20 claimants of the Business and Job Development (B&J) income tax credit is updated for tax year 2007 data. Data on the Top 20 claimants of the High Performance Incentive Program (HPIP) tax credits for tax year 2007 is also discussed.

Recent History of Corporate Income Tax Receipts

Annual Kansas corporate income tax receipts (by fiscal year) since 1995 are shown below:

Fiscal Year	Amount Collected	Percent Change
1995	\$229,421,376	
1996	\$218,586,552	-4.7%
1997	\$263,573,332	20.6%
1998	\$281,651,300	6.9%
1999	\$227,369,923	-19.3%
2000	\$250,122,826	10.0%
2001	\$211,906,919	-15.3%
2002	\$93,958,484	-55.7%
2003	\$105,222,316	12.0%
2004	\$141,173,000	34.2%
2005	\$226,071,634	60.1%
2006	\$350,200,874	55.0%
2007	\$442,448,739	26.3%
2008	\$432,088,732	-2.3%
2009	\$240,258,000	-44.4%

Although corporate income tax receipts recovered well after FY 2002, the current revenue forecast and trend is not encouraging. Fiscal Year 2009 corporate income tax receipts fell drastically (-44.4%) below FY 2008 receipts. Corporate income tax revenues are expected to remain essentially flat in the near future, as reflected in the November 2009 Consensus Revenue Estimate of \$245 million for FY 2010 and that same amount

for FY 2011. Thus far in FY 2010, corporate income tax receipts of \$140.2 million through the end of December 2009 are running 19.3% above the current Consensus Revenue Estimate but still are 5% below actual corporate income tax receipts for this same time period last fiscal year.

Corporate Income Tax Burden

In updating the Analysis dated October 14, 2004, tax returns from a sample of the largest 279 corporate income taxpayers for tax year 2007 were reviewed in order to determine how much impact the business tax credit programs (Business & Job Development, High Performance Incentive Program, Research & Development, Business Machinery & Equipment) have on the corporate income tax burden. These corporations accounted for at least 75% of the corporate income tax base for tax year 2007. The North American Industry Classification System (NAICS) code, Kansas taxable income, Kansas corporate income tax liability before credits, credits claimed, and the net tax receipts (amounts paid to the state) after credits for tax year 2007 for each of these corporations were captured in the database.

The update to Table 2 (attached) summarizes the results by NAICS code categories (using the first 2 digits of the NAICS code) for tax year 2007. The number of corporations included in each NAICS code category is shown in parenthesis in the first column.

Consistent with the Table 2 in the prior Analysis, the Update to Table 2 for tax year 2007 shows some disparity between the various industry sectors in the proportion of tax liability that is reduced or eliminated by tax credits through participation in business incentive tax credit programs. The "payment percentage" column shown on the Update to Table 2 reflects the percent of tax liability (measured before credits are taken) actually paid after credits were applied to reduce tax liability. Manufacturers experienced a moderately low tax payment percentage rate, 77.61%, slightly higher than the 76.28% tax payment percentage rate for tax year 2006, 72.8% for tax year 2005 and significantly higher than the 45.6% tax payment percentage rate for tax years 2000 through 2002 and 59.9% for tax year 2004. The manufacturing sector generated the largest portion of tax liability before credits (32.5% of the sample total) as well as corporate income tax receipts (31.3% of the sample total), compared to any other sector in the sample of 279 corporations for tax year 2007. The retail sector generated the next largest share of tax liability before credits (16.2%) and tax receipts (17.6%) of the sample for tax year 2007, experiencing a tax payment percentage of 87.84%, slightly lower than 90.08% for tax year 2006, higher than the manufacturing sector tax payment percentage, and higher than the 80.43% tax payment percentage for the retail sector for tax year 2005. The wholesale trade sector had a significantly lower tax payment percentage than the retail sector or manufacturing sector in tax year 2007, 65.61%, and accounted for 11% of total tax liability before credits and 9% of tax receipts of the sample.

The Analysis dated October 14, 2004 (see Charts 2 and 3 of that document) indicated that manufacturers represented the largest portion of Kansas tax liability before credits (and Kansas taxable income) in the sample during tax years 2000 through 2002.

The 2007 tax year sample data is consistent with that. As Update to Table 2 for tax year 2007 indicates, the manufacturing sector's total corporate income tax liability taken from the sample before credits was \$124.4 million and tax payments after credits (see "net receipts" column) were \$96.5 million, while the next largest sector, the retail sector, had total corporate income tax liability before credits of \$62.8 million and tax payments after credits of \$54.4 million.

B&J Credit Data

Within the sample of 279 corporations, the group of top 20 corporations that claimed the most B&J credits during tax year 2007 were identified. Corporations in this group were divided into 2 broad categories by NAICS code: manufacturing/transportation/warehousing/mining and retail/wholesale/other. The effective tax rate for each corporation was computed, as well as the average effective tax rate for each of the two categories. The results are shown below.

Top 20 B & J Credit Claimants Tax Year 2007

Tax Year 2007

8 in Manu./Transp./Warehous./Mining
 Total Taxable Income: \$557.8 million
 Total Net Tax: \$35.627 million
 Ave. Effective Tax Rate: 6.39%
 Range: 0% to 7.23%

12 in Retail/Wholesale/Other
 Total Tax. Inc.: \$432.72 million
 Total Net Tax: \$24.8 million
 Ave. Effective Tax Rate: 4.96%
 Range: -9.4% to 6.82%

The tax year 2007 results show a lower average effective tax rate for the retail/wholesale/other category among the 20 largest B&J tax credit claimants (4.96%) than the manufacturing/transportation/warehousing category (6.39%) within that same group. The range of effective tax rates for each corporation is narrower for the manufacturing/transportation/warehousing category (0% to 7.23%) than the retail/wholesale/other category (-9.4% to 6.82%).

The Update to Table 3 for tax years 2000 through 2007 (attached) compares the manufacturing firms and retail firms within the group of corporations included in the "top 20" in B & J credit claimants during each of tax years 2000 through 2007 (a sample size of 256 corporations). The amount of tax liability (measured before credits are taken), credits and net tax receipts to the state (tax paid after credits were taken) for all six tax years for manufacturing and retail firms in the group are listed. Of the 256 corporations in the group, 67 were manufacturing corporations and 66 were retail trade corporations. The "total" row at the bottom sums the information not only for these 67 manufacturers and 66 retailers, but also the rest of the 256 corporations in the group.

The Update to Table 3 for tax years 2000 through 2007 shows that manufacturing firms that are large B & J credit claimants continue to succeed in offsetting significant tax liability with tax credits, paying only 57.94% of the amount of their tax liability measured before credits were applied, while retailers that are large B & J credit claimants offset a much smaller portion of their tax liability, paying 84.41% of the amount their tax liability

measured before credits. The average payment percentage for all 256 corporations in this group of largest B&J credit claimants is 69.44%.

HPIP Data

Within the sample of 279 corporations, the 20 corporations claiming the largest amount of HPIP credits during tax year 2007 were identified. Corporations in this group were divided into 2 broad categories by NAICS code: manufacturing, transportation, warehousing and mining in the first category, and retail, wholesale and other in the second category. The effective tax rate for each corporation was computed, as well as the average effective tax rate for each of the two categories. The results are shown below.

Top 20 HPIP Credit Claimants Tax Year 2007

5 in Manu., Transp., Warch., Mining	15 in Retail, Wholesale, Other
Total Taxable Income: \$401.2 million	Tot. Tax. Inc.: \$387.8 million
Total Net Tax: \$14.1 million	Total Net Tax: \$300,000
Ave. Effective Tax Rate: 3.51%	Ave. Eff. Tax Rate: 0%
Range: -1.09% to 6.79%	Range: -9.46% to 4.77%

The tax year 2007 data indicates that large-scale HPIP participants benefited significantly from the HPIP program, with claimants in the Manufacturing, Warehousing and Mining category paying a low average effective tax rate of 3.51% of Kansas taxable income, and claimants in the Retail, Wholesale and Other category paying an even lower average effective tax rate of 0%. Seven of the claimants in the Retail, Wholesale, Other category had either zero or negative effective tax rates, eliminating their corporate income tax liability entirely with credit offsets and refunds. This data shows that large-scale HPIP participants are able to offset most, if not all, of their corporate income tax liability with tax credits. Interestingly, for the first time since this corporate income tax study began, of the Top 20 HPIP claimants for tax year 2007, companies in the Manufacturing, Transportation, Warehousing and Mining NAICS codes were significantly less effective than companies in the Retail, Wholesale and Other category in offsetting entirely their Kansas taxable income with HPIP credits, and were also significantly outnumbered by them.

Updated Conclusions

Many of the conclusions in the Analysis dated October 14, 2004 remain valid for the tax year 2007 corporate income tax data sample: manufacturers continue to utilize the business tax credit incentive programs heavily. However, for tax year 2007, a much wider variety of NAICS codes show up among the Top 20 HPIP credit claimants: this group was not dominated by manufacturers. Instead, retailers, wholesalers and others outnumbered manufacturers in this group. Retailers/wholesalers/other companies also outnumbered manufacturers/wholesalers/transportation/mining companies among the Top 20 B & J credit claimants. Because tax credits are used to lower tax burden, the effective tax rates continue to vary within industry groups of all types. The tax year 2007 data indicates that the average tax payment percentage for manufacturers increased from

76.28% for tax year 2006 to 77.61% for tax year 2007, while the average tax payment percentage for all corporations in the sample decreased from 84.19% for tax year 2006 to 80.65% for tax year 2007. See Update to Table 2 for tax year 2007. Also, in contrast to prior years, among the top 20 B&J credit claimants for tax year 2007, the retail/wholesale/other category average effective tax rate (4.96%) was less than the average effective tax rate for the manufacturing/transportation/warehousing/mining category (6.39%).

For tax year 2007, as with tax year 2006, the manufacturing sector generated largest share of the corporate income tax liability and corporate income tax receipts, compared to the income tax liability and income tax receipts generated by other sectors of the economy. See Update to Table 2 for tax year 2007. The tax year 2007 data contrasts with the tax year 2004 and 2003 data (see the annual updates for those tax years), which showed the retail sector as the most dominant portion of the corporate income tax base, generating the largest amount of Kansas corporate income tax liability and contributing the largest portion of the corporate income tax receipts. In tax years 2000, 2001 and 2002, the manufacturing sector generated the largest amount of Kansas corporate income tax liability (but not corporate income tax receipts).

Update to Table 2: Tax and Credits Statistics by Industry from a sample of 279 Corporations for Tax year 2007.

Industry	Total Tax Liability	Total NR Credits	B&J	R&D	HPIP	BM&E Credit	Other Ref. Credits	Net Tax	Payment Percentage
Agriculture, Forestry, Fishing and Hunting (5)	\$2,742,422	\$0	\$0	\$0	\$0	\$66,058	\$0	\$2,676,364	97.59%
Mining (10)	\$32,578,462	\$386,577	\$61	\$13,781	\$302,239	\$474,625	\$0	\$31,717,260	97.36%
Utilities (6)	\$12,531,050	\$12,500	\$0	\$0	\$0	\$0	\$0	\$12,518,550	99.90%
Construction (6)	\$3,145,543	\$805,581	\$28,500	\$29,137	\$747,542	\$202,617	\$0	\$2,137,345	67.95%
Manufacturing (55)	\$124,363,759	\$22,748,347	\$2,120,708	\$329,595	\$21,740,742	\$5,065,581	\$36,790	\$96,513,041	77.61%
Wholesale Trade (50)	\$42,187,023	\$13,012,073	\$121,500	\$6,850	\$11,967,948	\$1,496,534	\$0	\$27,678,416	65.61%
Retail Trade (45)	\$61,967,889	\$5,379,568	\$2,635,911	\$0	\$1,842,013	\$1,804,899	\$353,616	\$54,429,806	87.84%
Transportation and Warehousing (8)	\$22,990,465	\$790,304	\$249,500	\$13,315	\$401,989	\$1,598,859	\$837,087	\$19,764,215	85.97%
Information (19)	\$18,757,755	\$2,785,314	\$507,261	\$144,635	\$2,133,322	\$5,143,786	\$4,138,414	\$6,690,241	35.67%
Finance and Insurance (18)	\$15,000,743	\$1,155,247	\$198,651	\$0	\$931,840	\$722,918	\$30,000	\$13,092,578	87.28%
Professional, Scientific, and Technical Se (13)	\$7,375,433	\$1,783,124	\$235,565	\$164,171	\$1,359,888	\$49,926	\$0	\$5,542,383	75.15%
Management of Companies and Enterprises (21)	\$24,482,282	\$1,342,974	\$0	\$36,837	\$1,294,040	\$525,844	\$0	\$22,613,464	92.37%
Other Industries (23)	\$14,403,134	\$873,480	\$87,000	\$349,774	\$448,106	\$405,318	\$0	\$13,124,336	91.12%
Total All Industries (279)	\$382,525,959	\$51,075,089	\$6,184,657	\$1,088,095	\$43,169,669	\$17,556,965	\$5,395,907	\$308,497,998	80.65%

Other industries includes: Real Estate and Rental and Leasing; Administrative and Support and Waste Management; Educational Services; Health Care and Social Assistance; Arts, Entertainment and Recreation; Accommodation and Food Services; and other service and industry sectors

Update to Table 3. Summary information for the corporations that claimed most B&J Credits from TY 2000 to 2007

Sector (# of sample)	Total Tax Liability	Total NR Credits	B&J	R&D	HPIP	BM&E	Total Ref. Credits	Net Receipts	Payment Percentage
Manufacturing (67)	\$114,649,975	\$41,807,951	\$20,830,219	\$6,576,737	\$15,019,617	\$6,120,558	\$298,675	\$66,422,791	57.94%
retail Trade (66)	\$139,825,095	\$18,640,604	\$18,956,042	\$0	\$2,599,171	\$2,810,354	\$353,616	\$118,020,521	84.41%
Total (256)	\$393,442,309	\$87,265,964	\$82,369,077	\$10,370,538	\$34,983,128	\$20,924,756	\$11,444,074	\$273,199,706	69.44%