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Financial Institutions and Insurance

F-3 Privilege Tax on Certain Financial Institutions

The Kansas Privilege Tax

Statutory citation. Chapter 79, Article 11, *Kansas Statutes Annotated*.

Enacted. In 1963, effective January 1, 1964, in lieu of the former 5 mill intangibles tax on banks, savings and loan associations, and trust companies. The tax is imposed on these institutions "for the privilege of doing business within the state" (KSA 79-1106 and 1107).

The privilege tax is not a tax on income; rather, the tax is measured by income earned in the preceding year. These financial institutions are exempted from the payment of a corporate income tax (KSA 79-32,113).

History. Prior to January 1, 1964, shares of stock issued by national banks, state banks, savings and loans, or other banking or trust organizations were subject to an *ad valorem* tax, assessed to the individual shareholders at the place where the bank was located.

Collection requirements and tax base. The privilege tax is due by the 15th day of the fourth month following the close of the institution's federal tax year, but estimated payments have been required since tax year 1993 (similar to requirements on corporations paying income tax).

Tax base. Tax base is considered net income, as defined by the law, for the preceding taxable year. (*Note:* Legislation enacted in 1996 provided an apportionment formula for the income of multi-state institutions. Additionally, 1998 law required institutions to file consolidated returns with any subsidiaries owning, holding, or managing part of the institutions' securities portfolios.)

Net income. Kansas law defines "net income" as "the Kansas taxable income of corporations as defined in K.S.A. 79-32,138, and amendments thereto, determined without regard to the provisions of K.S.A. 79-32,139, and amendments thereto, and the provisions of paragraph (xiv) of subsection (c) of K.S.A. 79-32,117, and amendments thereto, plus income received from obligations or securities of the United States or any authority, commission or instrumentality of the United States and its possessions to the extent not included in Kansas taxable income of a corporation and income received from obligations of this state or a political subdivision thereof which is exempt from income tax under the laws of this state; less dividends received from stock issued by Kansas Venture Capital, Inc. to the extent such dividends are included in the Kansas taxable income of a corporation, interest paid on time deposits or borrowed money and dividends paid on withdrawable shares of savings and loan associations to the extent not deducted in arriving at Kansas taxable income of a corporation" (KSA 79-1109).

Deduction. The law further states "[s]avings and loan associations shall be allowed as a deduction from net income, as hereinbefore defined, a reserve established for the sole purpose of meeting or absorbing losses, in the amount of 5% of such net income determined without benefit of such deduction, but no further deduction shall be allowed for losses when actually sustained and charged against such reserve, unless such reserve shall have been fully absorbed thereby; or, in the alternative, a reasonable addition to a reserve for losses based on past experience, under such rules and regulations as the secretary of revenue may prescribe" (KSA 79-1109).

Present rates. Banks—2.25 percent plus 2.125 percent surtax on taxable income over $25,000; Savings and Loan Associations and Trust Companies—2.25 percent plus 2.25 percent surtax on taxable income over $25,000. (*Note:* Calculation is discussed following information on historical rates and credits.)

Historical Rates (1963-Present)					
Beginning in Tax Year	***1963***	***1970***	***1972***	***1979***	***1998***
Banks – Taxable Income					
First $25,000	5.00%	5.50%	5.00%	4.25%	2.25%
$25,001 +	5.00%	7.75%	7.25%	6.375%	4.375%
Savings and Loans and Trust Companies – Taxable Income					
First $25,000	5.00%	5.00%	4.50%	4.50%	2.25%
$25,001 +	5.00%	7.25%	6.75%	6.75%	4.50%

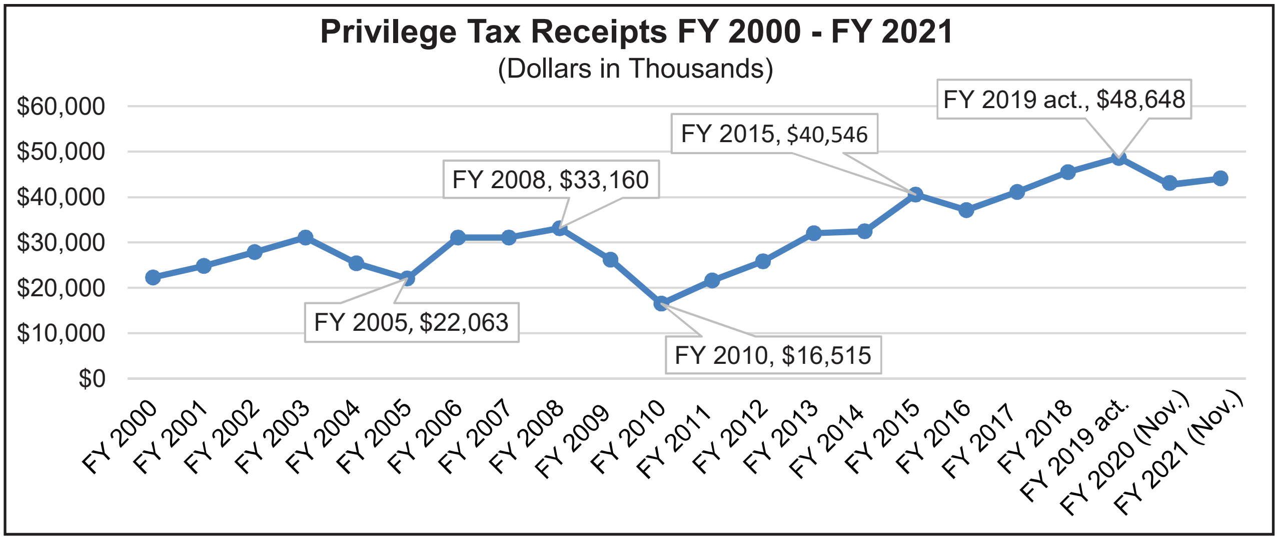
Credits against tax liability. Taxpayers may be allowed nonrefundable credits against the tax for expenditures for certain historic preservation expenditures, expenditures to ensure access of disabled individuals, contributions to certain community service organizations, contributions to organizations granting scholarships to certain low-income students, and under the Kansas High Performance Incentive Program. Taxpayers may be allowed refundable credits against the tax for providing child day care assistance and for a portion of contributions to certain community service organizations. Beginning in tax year 2019, taxpayers may be allowed to claim a nonrefundable credit against the tax for certain contributions to the Kansas Center for Entrepreneurship (2019 SB 90).

Privilege Tax Calculation

The following provides a high-level illustration of the calculation of a financial institutions' privilege tax liability.

Federal Taxable Income
+ U.S. Interest
+ Other net additions (losses)
= Apportionable Tax Base
× Apportionment Percent
= Kansas Tax Base
× 2.25%
+ 2.125% of amount over
$25,000 (S&Ls: 2.25%)
= Privilege Tax Liability

Net collections. The following table illustrates actual privilege tax receipts for state fiscal years (FY) 2001-2019 and also includes the Consensus November Revenue Estimate Group's estimates for FY 2020 and FY 2021.



Privilege tax filer data. The following chart outlines tax filer data, published by the Kansas Department of Revenue (KDOR), for tax years 2002-2016.

KDOR Annual Report (Year)	Filing Year	Tax Year	Banking	Savings and Loans	Total Filers
2018	2017	2016	339	25	364
2017	2016	2015	347	25	372
2016	2015	2014	365	40	405
2015	2014	2013	371	30	401
2014	2013	2012	391	31	422
2013	2012	2011	416	40	456
2012	2011	2010	436	45	481
2011	2010	2009	402	29	431
2010	2009	2008	421	31	452
2009	2008	2007	434	44	478
2008	2007	2006	425	26	451
2007	2006	2005	462	36	498
2006	2005	2004	398	38	436
2005	2004	2003	386	45	431
2004	2003	2002	251	15	266
Source: KDOR, Annual Reports.					

Prior Legislative Study and Response

Legislative Budget Committee, 1997 interim report. Included comment on the financial institutions' privilege tax. During the 1997 Interim, the Legislative Budget Committee received updates on the financial institutions' privilege tax from representatives of Kansas Department of Revenue, the Office of the State Bank Commissioner (OSBC), and the Kansas Bankers Association (KBA).

The KDOR representative provided general information on the tax and the estimate of privilege tax revenues by the Consensus Revenue Estimating Group. It was noted the estimate was revised downward by $18.0 million in FY 1998 to "reflect the ability for state banks to establish subsidiaries for the purpose of managing the bank's securities. Moving U.S. securities to these subsidiaries results in the interest earned on U.S. assets not being taxed, thus reducing privilege tax revenue." The revised estimate of financial institutions privilege tax receipts for FY 1998 was $20.0 million and $10.0 million in FY 1999.

The State Bank Commissioner reviewed Special Order 1995-6 (issued by a prior commissioner in 1995), noting special orders were issued based upon a finding of competitive inequality between state and national banks. The OSBC records indicated, at the time, there were 69 of 290 state banks that had investment subsidiaries. The Commissioner testified given the benefits derived by the establishment of an investment subsidiary, many state-charted banks may have chosen to convert to a national charter if the special order on subsidiaries had not been issued in 1995.

The representative of the KBA testified state-chartered banks should be treated equally to national banks for tax purposes in order for them to remain competitive in the banking industry. The representative indicated the decreasing revenue trends in the financial institutions' privilege tax were not mainly the result of investment subsidiaries being formed, but was the result of the sizable increases in Federal Deposit Insurance Company premiums last year for savings and loans, the possibility of reduced tax liability for non-Kansas financial institutions that had banking operations in Kansas, and the increased use of the tax credit for community service program contributions.

SB 6 (1998) and privilege tax estimate. The 1998 Legislature considered and passed SB 6 requiring banks and their subsidiaries to file a consolidated or combined return (restoring the federal securities income to the tax base for the privilege tax by including income from both the bank and its investment subsidiary). The bill also reduced the financial institutions' tax rate. (*Note:* Historical tax rate analysis is provided earlier in this article.) In May 1998, the estimate was raised by $15.5 million to reflect the passage of SB 6.

Special Committee on Financial Institutions and Insurance, 1998 interim report. During the 1998 Interim, the Committee was convened to consider topics assigned by the Legislative Coordinating Council. Among the topics, the Committee considered the taxation of state banks. (*Note:* The Committee also considered another topic affecting financial institutions—the reorganization of state regulatory supervision of the Executive Branch applicable to financial institutions, including banks, credit unions, securities, and consumer credit.)

The Committee received testimony from representatives of KDOR, the KBA, Heartland Community Bankers Association, and the Kansas Association of Community Bankers, as well as information provided by staff in response to member requests. Among information presented by staff was comparative bank data in the United States, Kansas, Colorado, Missouri, Nebraska, and Oklahoma and a review of the estimates of the Consensus Revenue Estimating Group for the privilege tax for FY 1994-FY 1999.

The KDOR representative presented a study of bank taxes, comparative information between the privilege tax and the corporation income tax, and the recent history of the privilege tax rate. The KDOR representative also described the apportionment of multistate bank income to Kansas (*e.g.*, based on factors of property, payroll, and receipts).

The Committee concluded it "recognizes that comparison of the taxation of financial institutions is difficult because of the variety of tax structures used by the states. Nevertheless, the Committee concludes that Kansas financial institutions are not unduly taxed based on the most meaningful comparisons. Recognizing that estimated privilege tax revenues for FY 1999 were reduced by approximately $12.5 million or about 33 percent, the Committee recommends that the issue of privilege tax rates be referred to the appropriate legislative committees for further consideration during the 1999 Session. The Committee recognizes a need for continued diligence to the subject. The Committee makes no recommendation on this study."

The interim report was presented to both a House subcommittee and Senate Committee during the 1999 Session.

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