

M I N U T E S

SPECIAL COMMITTEE ON ASSESSMENT AND TAXATION

June 29 and 30, 1977
(Room 532 - State House)

June 29, 1977
Morning Session

The meeting was called to order by Chairman John Simpson at 10:00 a.m. Representatives Eddy, Fry, and Slattery were absent. Staff present: Bill Edds, Richard Ryan, Roy Johnson and Robert Taylor.

On a motion by Senator Chaney, seconded by Senator Janssen, the minutes of the May 27, 1977 meeting were approved.

Proposal No. 6 - Inheritance Tax (Background Material)

Staff reviewed a memorandum on an analysis of inheritance tax returns filed with the Kansas Department of Revenue for ten months during 1976 (a copy of this memorandum is in the Committee notebooks). This analysis concluded that in 1976 the effective average inheritance tax rate for all shares of all classes of heirs was 1.88 percent of the total value of the shares. This ranged from an effective average tax rate of .53 percent for spouses who received 45.0 percent of the total value of all shares, to an effective rate of 10.0 percent for class C heirs who received 10.0 percent of the total value of all shares.

F. Kent Kalb, Secretary of Revenue, presented testimony which reviewed the existing inheritance tax law and its administration, the federal Tax Reform Act of 1976, the various types of death taxes the Committee might consider if a change in existing Kansas law is to be contemplated, and suggested areas in the existing law the Committee may wish to review. Mr. Kalb was accompanied by Ms. Nancy Suelter from the Department's legal staff, Ms. Janice Markum from the Department's research staff, and Mrs. Ethel Salts from the Department's Inheritance Tax Section. (A copy of Mr. Kalb's testimony together with an example of a completed inheritance tax return and copies of other forms are in the Committee notebooks.)

Mr. Kalb suggested several areas the Committee may want to review, including: (1) the contemplation of death presumption; (2) the valuation of farms and closely held businesses for inheritance tax purposes; (3) an exemption for spouse's contributions to an estate; (4) self assessment; (5) adjustment of current exemptions and tax rates; (6) problems with certain types of joint property escaping taxation; (7) the role of the probate court and county officials in inheritance tax administration; (8) conformity with the federal law; and (9) the valuation procedure used for life estates and remainders.

Mr. Kalb was asked if the participation of the probate court and other county officials was necessary for the proper administration of the inheritance tax. He responded that in many areas this county involvement is not necessary. However, he noted that, in certain cases, it was convenient for the Department to be able to use the probate court in collecting delinquent taxes and in enforcing liens.

A Committee member asked if there was a problem in collecting inheritance taxes on joint property that is not probated. Mr. Kalb noted that the law requires an inheritance tax return to be filed even if the estate is not probated. However, he also noted that in many cases where an estate consists of jointly held property which is not probated, there is no way for the Department to insure that a return is filed. During a brief Committee discussion on this matter it was noted that if the ten-year statute of limitation lapses following the death of the decedent, there is no way for the Department to collect taxes that might have been due but were not reported because a tax return was never filed.

During a brief Committee discussion on the current Kansas contemplation of death presumption, Mr. Kalb noted that rebuttals of the one-year presumption are not too common. However, they are frequently successful if a general pattern of giving can be established or if medical evidence suggests no expectation of death.

In response to a Committee question Mr. Kalb noted that conforming to the federal law for assets to be included in the estate and on the three-year "gross up" rule for adding back gifts would enable the Department to utilize federal audit information and data on the federal estate tax return in order to minimize state expenses in the administration of the inheritance tax. Mr. Kalb also noted that the current cost for collecting approximately \$17.4 million in inheritance taxes was \$225,000.

A Committee member inquired if a spouse's contribution had ever been allowed in the past. Mr. Kalb noted that some courts have allowed personal services at the prevailing wage in business and farming operations, provided the spouse was not paid a wage. However, a housewife has never been allowed a contribution for personal services.

When asked if an attorney's services were required to probate an estate, Mr. Kalb responded that it was not and that he was not aware of any states that required counsel to probate an estate.

Mr. Kalb noted in response to a question from the Committee that installment payments of inheritance taxes are not authorized by Kansas law. However, he also noted that some courts do accept partial payments of inheritance tax liability and then hold the estate open until the total liability is satisfied.

A Committee member asked if self-assessment of inheritance taxes would save the Department enough to reduce the number of positions required for administration. Mr. Kalb noted that it would save the Department some work but he did not know if the total savings would be reflected in fewer positions. He noted the current relatively small cost for existing operations. When asked why the current system was established as it is, Mr. Kalb responded that the rationale or justification for the present procedure of state assessment is unknown and lost in history. He stated that the procedure was set up in 1919 and it has not been changed since then.

Mr. Kalb noted in response to a question that counties currently retain five percent of gross inheritance tax collections (in Fiscal Year 1977 this amounted to an estimated \$.9 million). He assumed that the reason for allowing counties to share in the receipts was due to the involvement of the probate court in the administration process.

A Committee member noted that 30 other states have an inheritance tax similar to Kansas and asked what these other states are doing in response to the 1976 federal law. Mr. Kalb responded that he had no definite information on what all of these other states are doing. However, he noted that many are conducting studies at this time in order to determine what the correct response should be. He also noted that states with "estate pick up" type taxes were having much worse problems with the new federal law than states like Kansas. Mr. Kalb also noted that if Kansas went to an "estate pick up" type tax and adjusted the tax rates to raise the same amount of revenue, there would be a shifting of the incidence of the inheritance tax. He also noted that while conformity with the federal law could be of great assistance in standardizing definitions and in determining the gross estate, there were other areas where conformity could cause problems.

Proposal No. 81 - Solar Energy Tax Incentives

Staff reviewed a background memorandum on this proposal and gave the Committee supplemental materials for further review. Copies of the memorandum and supplemental materials are in the Committee notebooks.

The Chairman noted that if there were no objections, the Committee would review this proposal in conjunction with Proposal No. 8 - Income Tax.

Afternoon Session

Hearing on Proposal No. 6 - Inheritance Tax

Mr. Bill Turgeon, representing the Kansas Farmers Union, presented a statement from Mr. Ivan Wyatt, Vice-President, Kansas Farmers Union, recommending the Kansas inheritance tax law be amended to provide larger deductions for the surviving spouse, use valuation of estates for inheritance tax purposes, and increased steps in the various graduated tax rate tables and a reduction of tax rates for smaller estates. A copy of Mr. Wyatt's statement is in the Committee notebooks.

In response to a question from the Committee Mr. Turgeon stated that he could support higher tax rates for larger estates in order to minimize the revenue loss of lowering taxes on smaller size estates.

Mr. John Blythe, Kansas Farm Bureau representative, presented a statement encouraging the adoption of use value appraisal of farms and small businesses for inheritance tax purposes and a larger deduction for spouses or other family members wishing to continue farming operations. A copy of Mr. Blythe's statement is in the Committee notebooks. Mr. Blythe noted the Farm Bureau had no specific policy on the Kansas inheritance tax. However, he expected a statement of policy would be developed at the organization's meeting in December.

Following Mr. Blythe's presentation was a brief exchange concerning the effect of reducing inheritance taxes on farmers and any shifting of the tax burden to other taxpayers as a result of this action, the effect of inflation on farmers and small businessmen as contrasted to the government's need for revenues, and the necessity for a recapture provision under a use value appraisal system.

A Committee member noted that giving the surviving spouse a larger deduction or conforming to the new federal law for spouse's contribution to the estate would seem to have the effect that the Farm Bureau was recommending. Mr. Blythe responded that while such a move would be very desirable, it did nothing to aid children who may have contributed greatly to the estate by continuing to work on the farm under marginal conditions when other "off the farm" opportunities would have provided more financial reward.

Mr. Dee Likes, representing the Kansas Livestock Association, presented a statement in which he emphasized the lack of liquidity in most agricultural estates and the problem this creates due to the current inheritance tax. He suggested that when considering changes to the inheritance tax the Committee consider adopting a short recapture period for estates that would use a use value appraisal to avoid harming the credit potential of the survivors, increasing exemptions for all heir classes to recognize the effect of inflation, allowing unlimited tax free transfers between spouses, and authorizing use value appraisal of agricultural activities for inheritance tax purposes. A copy of Mr. Likes' statement is in the Committee notebooks.

In response to a question from the Committee Mr. Likes stated that urban and rural properties should be treated differently for taxation purposes. He further stated that in his opinion use valuation of farms for inheritance tax purposes would not necessarily be less than the market value established for property tax purposes. A Committee member noted that in most instances market value appraisals of farm land for inheritance tax purposes is significantly higher than market values established for property tax purposes, therefore adopting a use value appraisal for inheritance tax purposes would result in revenue losses for the state.

Ms. Sharon Kunard, C.P.A., of Elmer Fox, Westheimer and Company, representing the Kansas Society of Certified Public Accountants, presented a statement concerning Proposal No. 6. Ms. Kunard noted that the Kansas Society of C.P.A.'s had no formal position on the inheritance tax. However, she presented seven areas the Committee may want to review in considering changes to the Kansas inheritance tax. These seven areas include: (1) a statement of policy is needed on the inheritance tax treatment of annuities and individual retirement accounts; (2) problems associated with the new federal spouse contribution rule if the "wrong" spouse dies first; (3) identification of items transferred in contemplation of death from the federal estate inventory; (4) inheritance tax free transfer of property between spouses (with retention of the pick up tax); (5) taxation of all or a portion of insurance proceeds; (6) conformity to federal definitions and adjusted gross estate; and (7) adoption of self assessment of inheritance tax. A copy of Ms. Kunard's statement is in the Committee notebooks.

In response to a question from the Committee Ms. Kunard noted that if use value appraisal were used for inheritance tax purposes, it would still be necessary to compute fair market value if a limit were to be placed on the maximum reduction allowed to the adjusted gross estate under a use value appraisal. She noted that fair market would still be required in the computation of the federal gross estate in order to compute the \$500,000 limit.

In commenting on problems associated with Kansas determining how much of the three-year add back on the federal return represented those items transferred within one year of death, Ms. Kunard stated that it was her understanding that the federal Form G would still be used for a few years and it would be possible to make such a determination from this form.

Mr. James K. Logan, representing the Tax Section of the Kansas Bar Association (KBA) offered the technical assistance of the KBA in drafting any proposed changes to the Kansas inheritance tax law. He noted that the KBA had no official position in this area. He stated that, in pointing out several factors the Committee may want to consider in its review of the inheritance tax his remarks should be considered his personal opinions.

Mr. Logan observed that in the opinion of most attorneys the changes in the new federal law are so severe and represent such a drastic departure from what existed prior to the new law that making radical changes to the Kansas law at this time would only add to the confusion. As an alternative he suggested that the Committee consider only making those changes that are really necessary due to the changed federal law and to "let the dust settle" before embarking on a major revision of the Kansas law.

Mr. Logan noted that the new federal estate tax law changes combined with changes in the federal income tax relating to the adjusted basis for income tax purposes of inherited assets will have a very profound effect in breaking up large accumulations of inherited wealth over the next two or three generations (70 years). He expressed the belief that by 2047 no one in America will have an estate in excess of \$1.5 million. He further stated that once the far reaching effects of this new federal law becomes evident there will be massive lobbying attempts to revise it by reducing its impact on the transfer of inherited wealth to successive generations.

Mr. Logan outlined nine areas of the Kansas inheritance tax that, in his opinion, need attention, regardless of any action that the Committee might consider in response to the new federal law. These nine areas include: (1) consideration of conforming to the federal law in regard to those expenses which are authorized in computing the adjusted gross estate; (2) clarification of the tax treatment of "special" and "general" powers of appointment; (3) adoption of a consistent and concise policy concerning the tax treatment of inherited retirement benefits (for example, lump sum transfers are taxable, whereas installment payments are not taxable); (4) conformity to the federal interest factor for computing the present value of life estates (currently Kansas uses an interest factor of five percent while the federal factor is six percent); (5) a review of Kansas probate law, since the federal tax incidence is determined by Kansas law in this area (he also suggested a review of laws relating to joint tenancy and the establishment of irrevocable trusts); (6) establishment of a procedure for self assessment of inheritance taxes which would include forwarding the tax payment directly to the Department of Revenue with the tax return. (Bypassing probate court would allow the state to earn interest on these tax receipts instead of allowing counties to earn the interest. The court would hold the estate open until notified that all taxes had been paid.); (7) discontinuance of the practice of allowing double deductions for attorney's fees; (8) consideration of revising the law to allow inheritance tax liens to apply to the proceeds from the sale of an asset to allow for the emergency liquidation of perishable assets or assets whose value is declining. (Present procedure calls for obtaining a waiver from the Department of Revenue prior to disposing of assets. An alternative may involve posting a bond to cover any potential tax liability.); and (9) consideration of including all or a part of insurance proceeds in the gross estate subject to taxation.

Mr. Logan noted several areas relating to changes in the federal law where the Committee may want to consider corresponding changes in the Kansas law. These areas include: (1) consideration of revising Kansas exemptions in light of the fact that after 1981 no federal estate tax return will be filed for estates with a value of less than \$175,000 (this could create audit problems for the Department of Revenue.); (2) consideration of a special marital deduction equal to \$250,000, or 50 percent of the estate,

whichever is greater; (3) use valuation of farms and other closely held businesses (Mr. Logan noted a problem with tax liens during the recapture period that will need to be addressed if the state proceeds in this area.); (4) adoption of a unified gift and death tax (Mr. Logan advised against adopting a separate gift tax due to the limited revenue that would accrue from such a tax.); (5) taxation of generation skipping trusts (Mr. Logan recommended no changes to current Kansas law in this area except as needed to clarify the tax treatment of powers of appointment.); (6) the income tax treatment of inherited assets; (7) a review of the Kansas Disclaimer Act (K.S.A. 59-2291 et seq., Mr. Logan recommended no change.); and (8) consideration of joint tenancy and allowance of spouse's deduction for "non-traditional" marriages.

Mr. Logan observed that there would be a great temptation for the Committee to recommend the adoption of an estate tax. He cautioned against such a drastic change. However, he did note that there would be advantages to the state in conforming to the federal law insofar as definition of terms and the determination of the adjusted gross estate, with the state retaining its present inheritance tax heir classifications, exemptions, and tax rates.

Mr. Logan also recommended against amending existing Kansas law relating to formula bequests to provide for a larger marital deduction for those estates between \$350,000 and \$500,000. He observed that it would be better to require those persons desiring to take advantage of the larger tax free transfer to spouses to amend their wills rather than to arbitrarily change the law. He felt such action would be of a greater benefit to smaller estates below \$350,000.

Mr. William L. Hogle, CLU representing the Kansas Association of Life Underwriters, presented a statement to the Committee that recommended: (1) increasing inheritance tax exemptions; (2) waiting for the effects of the new federal law to "settle in" before making any other changes to the Kansas law; and (3) the continuance of the inheritance tax exemption for names beneficiaries on insurance policies. A copy of Mr. Hogle's statement is in the Committee notebooks.

Following Mr. Hogle's statement was a brief Committee discussion concerning the advantages and disadvantages of taxing insurance proceeds. Several members of the Committee expressed the belief that taxing insurance proceeds would only harm those persons with very small estates comprised primarily of insurance proceeds with very little else in assets.

June 30, 1977

Morning Session

The meeting was called to order by the Chairman at 9:00 a.m. Representatives Eddy, Fry, and Slattery were absent.

Hearing on Proposal No. 6 - Inheritance Tax (Continued)

Mr. Mark Elrod of the First National Bank of Topeka, representing the Trust Division of the Kansas Bankers Association, presented a statement to the Committee recommending: (1) conformity with the federal law in all possible areas; (2) increasing the various exemption classes; and (3) self-assessment of inheritance tax liabilities. A copy of Mr. Elrod's statement is in the Committee notebooks.

In response to a question from the Committee, Mr. Elrod stated that, in his opinion, tax returns should be filed directly with the Department of Revenue and not go through the probate court in order to insure confidentiality in listing of the assets of the estate.

Mr. Lee Hornbaker, an attorney from Junction City, presented his personal opinions to the Committee concerning the Kansas inheritance tax. His comments and observations included: (1) the valuations used to determine the Kansas gross estate should be the same as the federal valuation; (2) tax returns and inventory certifications should be filed directly with the Department of Revenue, and the attorney or estate representative should certify the inventory as being correct, rather than the probate judge; (3) the current law is so loosely written and administered that Kansas is missing millions

of dollars in tax revenues; (4) the first \$200 of a bequest should be totally exempt from taxation; (5) other exemptions for various classes of heirs should be adjusted to reflect average levels of exemptions in other states; (6) the statute of limitations should not begin to run until the tax return is filed; (7) K.S.A. 79-1536 and K.S.A. 9-1205 should have penalty provisions to require banks and savings institutions to freeze joint accounts of a decedent until they have been inventoried by the Department of Revenue and to report all such accounts over a specified minimum amount to the Department of Revenue; (8) provide that no stock in any corporation may be transferred until a waiver is obtained from the Revenue Department; and (9) include insurance proceeds in the gross estate for tax purposes. A copy of a letter from Mr. Hornbaker covering his remarks is attached.

Mr. Lewis Cline, representing the Kansas State Grange, presented a statement to the Committee encouraging an increase in inheritance tax exemptions. A copy of Mr. Cline's statement is in the Committee notebooks.

Mr. William P. Trenkle, Jr., an attorney from Dodge City, presented several personal opinions and observations to the Committee concerning the inheritance tax. Mr. Trenkle's comments included his observations that: (1) there should be more tax brackets that provide lower tax rates for nieces and nephews (these relatives are currently class C heirs); (2) the Kansas gross estate for inheritance tax purposes should include all lifetime gifts to avoid large tax losses now and in the future (Mr. Trenkle observed that under the existing federal law \$340,000 can be given away in a lifetime with no taxes due. In addition, more persons are making gifts now to avoid effect of inflation on estate value.); (3) since there is increased activity in the establishment of generation skipping trusts a review should be made of the Kansas tax consequences in this area; (4) Kansas should conform to the federal law except for the classification of heirs and tax rates; and (5) there could be problems when attaching liens to a gift brought back into an estate for inheritance tax purposes and when attaching a lien on property subject to a recapture tax due to change in use (Mr. Trenkle noted that in his opinion, such problems were not insurmountable.) A copy of Mr. Trenkle's remarks are attached.

Following Mr. Trenkle's presentation was a brief discussion on various elements of conforming certain aspects of the Kansas inheritance tax to the federal estate tax.

A letter from Senator Joseph Harder in support of S.B. 271 was received by the Committee. A copy of Senator Harder's letter is in the Committee notebooks.

Representative Homer Jarchow presented a statement in support of H.B. 2288. A copy of Representative Jarchow's statement is in the Committee notebooks.

Representative Marvin Littlejohn appeared in support of H.B. 2321. Representative Littlejohn stated that the other reform measures being discussed before the Committee would offset the cost of increasing the exemptions and reducing the tax rates as proposed in H.B. 2321. He also noted that the provision of this bill increasing the amount to be retained by counties from inheritance tax receipts was not critical to the bill but, rather, that it was done in an effort to prompt discussion on the issue.

Fred Allen, representing the Kansas Association of Counties, appeared on H.B. 2361 and addressed several comments to the inheritance tax generally. Mr. Allen observed that the wealth taxed by the inheritance tax is a creature of the county in which it is located and, as such, he stated that county governments should share in this revenue source to a greater extent than at present. When asked by the Committee if, in light of the state's participation in the funding of the court system, there was still any justification for the county receiving five percent of inheritance tax receipts, especially if the returns would be filed directly with the Revenue Department in the future, Mr. Allen commented that the state should pay the total cost for administering the judicial system.

Ms. Polly Wilhardt, an attorney from Garden City, submitted a letter to the Committee that raised four points concerning the tax treatment of surviving spouses who held property as a co-tenant with the decedent. She noted that: (1) the spouse's contribution as a housewife has considerable monetary value; (2) most claims of contribution by a non-wage earning spouse are audited by the IRS and usually end up in court; (3) allowing a non-wage earning surviving spouse to claim a contribution to the estate would seem to be in the interest of good public policy; and (4) by not allowing for an adequate spouse's contribution property taxing between spouses is taxed twice in the same generation which aggravates the liquidity situation of the estate for the remaining heirs. Ms. Wilhardt's letter is attached to the minutes.

Policy Questions Checklist

No. 6. Staff reviewed several of the major policy questions associated with Proposal. A copy of the policy questions checklist is in the Committee notebooks.

Afternoon Session

Committee Discussion

The Committee reviewed the policy questions checklist, the testimony of the conferees, and the staff reports, and discussed various alternative approaches that could be considered in amending the Kansas inheritance tax.

The Committee decided to make as many decisions as possible concerning changes to the inheritance tax to enable the staff to draft a bill or bills to provide a vehicle for further discussion at a later meeting.

It was moved by Representative Braden (seconded by Representative Crowell) that: (1) the inheritance tax should be "self assessing" with the tax liability being computed by the person who completes the return, and (2) the inheritance tax should be paid directly to the Revenue Department and not go through the probate court and the county treasurer. Motion carried.

There was some discussion concerning what should be done with the five percent of gross collections currently retained by the counties. No decision was reached, except that the Committee should discuss the matter at a later time.

It was moved by Representative Braden (seconded by Representative Wilkin) that the attorney or estate representative certify the assets included in the estate inventory and not the probate judge and that the inheritance tax return be filed directly with the Revenue Department with the Department certifying to the probate court when all tax liabilities had been satisfied. Motion carried.

It was moved by Senator Janssen (seconded by Representative Braden) that Kansas conform to the federal estate tax by: (1) allowing for use value appraisal of real property assets of farms or other closely held businesses; (2) limiting the reduction in the gross estate due to use valuation to \$500,000; (3) providing for a 15-year recapture where the use of the asset changes; (4) allowing the same options for use value appraisal as found in the federal code; and (5) providing that the same valuation option as used on the federal tax return must be used on the state tax return. Motion carried.

The Committee discussed at length the taxation of insurance proceeds. One member explained how it would be easy to avoid taxation by transferring a policy to another person's ownership, thus including the proceeds in the taxable estate would greatly injure those persons with very small estates not now subject to taxation. Other members expressed an interest in taxing insurance proceeds above a specified minimum such as \$50,000 or \$100,000. Another member expressed doubt that the significant level of revenues to be derived from such a move was really needed by the state. A Committee member observed that the primary purpose for insurance was to provide liquidity to the estate to pay taxes and other debts and to provide a safety valve or source of savings to younger persons, and he concluded that taxing insurance proceeds might be bad public policy. The Chairman directed the staff to check what other states were doing in this area and to report any findings to the Committee at a later date. It was the consensus of the Committee that no decision could be made on this matter at this time.

The Committee discussed at length the question of "grossing up" the estate to include all lifetime gifts as required in the new federal law. One member expressed doubt that there was a need for the increased revenues that would be derived from this action.

The Secretary of Revenue, responding to a question from the Committee stated that a provision to bring in all or some gifts would be needed or Kansas would lose existing tax receipts due to the increased incentive to give during a lifetime to avoid the effects of inflation on estate values. He noted if there was a desire to protect

existing revenues and not to increase tax receipts an exemption or credit procedure could be devised to maintain the same relative level of tax receipts.

A Committee member raised a question concerning collecting tax on a gift that may have been made 20 years prior to the decedent's death and asked how would any subsequent tax lien affect the title.

Senator Chaney moved (seconded by Representative Wilkin) that all gifts made after December 31, 1978 be added back into the gross estate for purposes of computing the inheritance tax, provided that there should be a \$3,000 exclusion per gift per year. In the discussion following the motion, Senator Chaney noted that some compromise was needed between protection of the state's tax base and the problems inherent in an "add back" period in excess of three or four years. His purpose for the motion was to provide a vehicle for further discussion of this issue. Motion carried.

Senator Janssen moved (seconded by Senator Sowers) that Kansas conform to the federal code in all areas except the inclusion of insurance in the gross estate for tax purposes and in the classification of heirs and determination of the tax liability. (The motion includes conformity on: (1) tax treatment of powers of appointment; (2) a deduction for spouses of 50 percent of the Kansas taxable estate or \$250,000, whichever is greater; (3) elimination of double deduction for attorney fees; (4) interest factor used in computing present values; (5) definition of terms included in the gross estate; (6) tax treatment of annuities and retirement benefits; (7) allowance of deductions for expenses; and (8) other items of conformity included in preceding motions.) Motion carried.

It was moved by Representative Crowell (seconded by Representative Wilkin) that, given the limited conformity with the federal code previously recommended by the Committee, current exemptions, tax rates, and heir classes should be adjusted, if necessary, to insure approximately the same relative level of tax receipts. Motion carried. The Chairman instructed the staff to review the fiscal impact of the Committee's recommendations and suggest alternatives for the Committee's consideration.

Representative Braden moved (seconded by Representative Crowell) that Kansas conform its statute of limitation (K.S.A. 79-1523 and 79-1529) to the federal statute of limitations (Generally, the federal statute of limitation is three years, in the case of an error in listing assets of the estate it is six years, and in the case of fraud there is no limit.), with the statutory time beginning only after the tax return is filed; the time limit on any assessment would not lapse until the tax is paid. Motion carried.

It was moved by Senator Janssen (seconded by Representative Shelor) that K.S.A. 9-1205 and K.S.A. 79-1536 be amended to include appropriate penalties for banks and other savings institutions that fail to report assets of a decedent to the Revenue Department. Motion carried. The Chairman instructed the staff to review the subject of penalties and to offer staff recommendations at a later time.

Representative Crowell moved (seconded by Representative Shelor) that installment payments be authorized for payment of taxes by heirs to estates where the principal asset is a farm or closely held business and where payment of the tax in a lump sum would cause an undue hardship. The federal guidelines in this area should be used as a guide; and statutory interest (six percent per annum) should apply. Motion carried.

The Chairman instructed the staff to: (1) review the questions raised by attaching tax liens to property previously passed as a gift and the real estate subject to recapture of taxes under a use value appraisal; (2) review Kansas disclaimer statutes and to report any findings or recommendations to the Committee; and (3) research the matter of the tax status of powers of appointment to see if any action should be considered by the Committee.

It was agreed that the matter concerning the income taxation of inherited assets would be discussed in conjunction with Proposal No. 8.

Agenda for Next Meeting

The agenda for the July 28-29, 1977, meeting will include staff reports, conferees, and Committee discussion on Proposal No. 8 - Income Tax. In addition there will be staff reports and a review of bill draft(s) on Proposal No. 6 - Inheritance Tax.

Prepared by Robert L. Taylor

Approved by Committee on:

July 28, 1977
(Date)

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May 16, 1977

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Senator John M. Simpson
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Dear Senator Simpson:

At the Legislative Changes meeting on May 13 you asked for suggestions for the interim tax committee which will study the state inheritance tax law between now and the next legislature. Senator Simpson, I do have some matters which I would like to present to you for your consideration and for consideration by your committee.

As you know, Kansas does have and has had for many, many years an inheritance tax law. However, it is my personal opinion that it is so loosely administered that it is of little value. I personally believe that the State of Kansas is missing millions of dollars in revenue because of the loose administration of the inheritance tax law.

Like so many laws, it really only catches the honest people. First, for example, if a man dies and no tax returns are filed upon his estate within ten years, then the estate escapes all inheritance taxes. This does not seem right to me. I personally know of instances where families deliberately take no action with respect to probate proceedings or determination of descent or sale of property for more than ten years for the avowed purpose of escaping the payment of any inheritance tax. Therefore, I would suggest that the law be amended to provide that if an inheritance tax return is filed then it will be presumed to have been accepted and proper if no action is taken by the State within a certain number of years thereafter. However, the law should further provide that in those instances where no inheritance tax return is filed or where property is not listed upon an inheritance tax return, then a lien attaches to the property and will remain attached until the proper inheritance tax return has been filed and the proper clearance obtained or tax paid.

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As you know, we have joint tenancy in Kansas both as to real property and as to personal property. With respect to real property, the suggestion above will cover the situation. However, with respect to personal property and especially with respect to intangible assets such as bank accounts and certificates of deposits in banks, and savings and loans, we have absolutely no control. John Doe could die with 25 different bank accounts in 25 different banks, each in joint tenancy with his wife and under the present slipshod method of management in the State of Kansas, all of those funds could and would be paid over to the wife and there would never be a need for inheritance tax return to be filed in the State of Kansas. I would recommend for your consideration that the law be changed to provide that upon the death of a joint tenant or upon the death of any individual, no funds could be withdrawn from any bank accounts held in his name or in any bank account wherein he is listed as a co-owner or as a joint tenant until such time as tax clearance has been obtained from the State of Kansas with respect to transfer. This would be somewhat similar to that law which we now have with respect to the transfer of stock certificates. Actually, it makes little sense to say that you cannot transfer ten shares of stock in ABC Corporation without a tax clearance but still you might be able to transfer \$50,000.00 in money or bank accounts without a tax clearance. It is further my opinion that in order to make this law enforceable, it must provide that if a bank should transfer these funds without a tax clearance then the bank or other financial institution could be and would be held liable to the State of Kansas for the tax which was due and payable to the State of Kansas and for a penalty for their failure to transfer the funds without proper clearance.

With respect to cash and other items of security, I would suggest that consideration be given to a law providing that no bank box of any deceased person can be opened or any property removed therefrom unless and until the proper order has been secured from the probate court and a representative of the State of Kansas is present to participate in the inventory of the contents of the lock box.

It seems rather strange to me that our law, K.S.A.79-1511, now makes it the responsibility of the probate judge to furnish the inheritance tax reports to the State of Kansas. This should be the responsibility of the executor or of the administrator. It is the responsibility of the executor and administrator to furnish and file the 706 forms to the federal government and for the life of me I do not see why the probate judge should certify to these matters in the

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State of Kansas. I would suggest that it be modified to provide that the executor or administrator complete and file the necessary forms with the inheritance tax division and that attached to those forms should be a certified copy of the inventory and valuation and of the will, if one is in existence. In other words, the burden and responsibility should be on the executor and administrator and not on the probate judge.

Under our inheritance tax law insurance left by the decedent is not included as a part of his estate. As you know, insurance is considered as a part of the estate for federal estate tax purposes. I would recommend that the Kansas law be brought into conformance with the federal law.

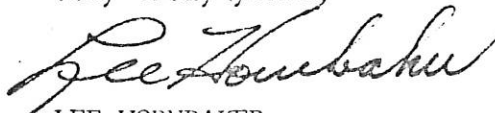
To cover the transfer of stock in Kansas corporations, I would recommend that the law be amended to provide specifically that no Kansas corporation shall transfer certificates of stock belonging to a decedent unless and until necessary tax clearances have been received from the State of Kansas. Actually, this is pretty well followed at the present time and especially by the larger corporations. You run into your problems with the small, closely held corporations.

The Kansas law with respect to gifts and transfers without adequate consideration now only relates to such transfers made within one year prior to the date of the death of the decedent. This is found in K.S.A. 79-1501, last paragraph. The federal law on this has recently been amended to provide that any transfer within three years is conclusively presumed to have been made in contemplation of death. I would suggest that the Kansas law should be the same as the federal law on this matter of gifts and transfers without adequate consideration.

John, I know that my suggestions will not be popular. However, I am equally convinced that the present Kansas law is more honored in the breach than in the observance and that the State of Kansas is missing millions of dollars in revenue because of the lax inheritance tax laws and the lax interpretation and application of the law.

By the way, the view expressed herein are my own and do not necessarily constitute the views or opinions of the remaining members of this firm.

Very truly yours,


LEE HORNBAKER

LH:lj

STATEMENT OF WILLIAM P. TRENKLE, JR., Attorney at Law, Dodge City,
Kansas, FOR THE SPECIAL COMMITTEE ON ASSESSMENT AND TAXATION,
JUNE 30, 1977

As an attorney in Western Kansas, I represent a number of businessmen, ranchers and farmers. My practice is primarily restricted to the areas of Estate Planning and Taxation. I represent no special interest group before this committee other than the interests of my clients in general.

The Department of Revenue is to be commended for the fine job they have done over the years in administering the Inheritance Tax laws. In polling a number of the local attorneys in Southwest Kansas, I found almost unanimous feeling that the Department was one of the finest in the country.

The only other comments which I received from the attorneys of any consequence was the classification of step-children and nieces and nephews as strangers, which results in a rather substantial amount of tax.

My primary concern is what effect the new Federal law will have on the revenues to the State of Kansas. First it should be stated that in most estate planning the Kansas Inheritance taxes are of minor consequence and almost all of the planning is centered around the Federal law. This is particularly true in the case of large estates.

Under the new Federal Tax Reform Act there are several areas which are of major concern. They are as follows:

1. The new Federal law increased the exemptions for gifts during life and provided for an add back of these gifts at the time of death. Through my estate planning practice, I can see a significant increase in the amount of gifts that are being given during lifetime to remove the property from future inflation and to provide for the earnings to go to the next generation. This is true even though the gift will be added back to the estate. Under Kansas law, once these gifts are made there will be no adding back of these gifts at the time of death. Therefore, Kansas is going to escape significant amounts of revenue.

2. The Federal law has restricted the amount of generation skipping transfers. In Kansas there is no provision which would cover this. I am seeing a significant increase in the amount of generation skipping transfers which are being made at this time. Primarily this interest arises by virtue of the fact that something has been taken away from the taxpayer and they are suddenly wanting to take advantage of what is left.

3. The new Federal small business and farm valuation provisions can be rather significant in the case of family

held enterprises. These provisions are extremely complicated and are waiting further interpretation in the way of regulations and rulings. It would seem to be rather complicated for the State of Kansas to attempt to adopt an independent and different means of valuation of small business and farm properties. It would seem to make more sense to adopt the Federal rules.

In summary, it would seem to me to be logical for the State of Kansas to adopt some form of conformity with the Federal law. This would cure the problems I have listed above and would also cure a number of other technical provisions which I have not discussed here.

In considering conformity, I would encourage you to utilize the assistance of the Tax Section of the Kansas Bar Association and other interested groups such as Certified Public Accountants. Possibly a special task force should be formed to fully study the impact and the technical provisions of a law of this type.

I would like to thank the Special Committee on Assessment and Taxation and Representative Dean Shelor for giving me the opportunity to present my thoughts.

Respectfully submitted,

WILLIAM P. TRENKLE, JR.

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DALE H. CORLEY

VAN SMITH

POLLY WILHARDT

June 28, 1977

MEMORANDUM

TO: Senator John Simpson and the Members of the Committee
on Assessment and Taxation:

At the present time, under Kansas Statutes Annotated 79-1501, all property within the jurisdiction of the state which passes upon the death of a joint tenant is taxable in its entirety except the part proven to have been contributed by the survivor.

Kansas, in defining "contribution by the survivor" follows the federal standard under IRC Section 2040 on joint interests in recognizing contribution only as consideration in money or money's worth. Further, both Kansas and the Internal Revenue Service place the burden of proving the extent of consideration furnished by the surviving joint tenant on the decedent's estate. And if it is shown that the surviving joint tenant originally contributed a fraction of the consideration for the acquisition of the property in money or money's worth, but the property has been improved or increased in value over the years, a mathematical calculation to show the survivor's contribution is further complicated.

In addition, the Internal Revenue Service has been forced to recognize an exception to their otherwise rigid rule, because the tax courts have ruled that in regard to jointly held property by a farm husband and wife, the wife's labor and services on the farm must count as a recognizable contribution towards the acquisition and increase in value of the jointly held property.

As you know, the Internal Revenue Code on joint interests has been changed by the Federal Estate and Gift Tax Reform Act of 1976. If the joint interest is "qualified", only one-half of the value of the property held jointly will be taxed in the decedent's estate. A "qualified" joint interest is a joint interest held only by husband and wife and on which, at the time of its creation, gift tax was paid.

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What Congress has done by this change has been to refuse to directly face the question of whether the contribution to the building of marital property by the spouse who works at home without receipt of wages should be counted in determining contribution by each joint tenant spouse. Rather, Congress has attempted to give the appearance of crediting the non-wage earning spouse's contribution towards the acquisition of jointly held property, when in actual fact, it has merely reinforced the same philosophical position it has always held in regard to contribution towards jointly held property but transferred the philosophy to the gift tax section. I would hope that your committee and the Kansas legislature would be more honest than Congress has been and admit the fact that the non-wage earning spouse contributes by his or her efforts as much to the acquisition and increase in value of marital property as does the wage earning spouse.

As a woman who has devoted many hours of work in the home for the benefit of her family, as an attorney who handles estates in a farming area, and as the wage earning spouse of a family in which the husband presently is contributing to our family's betterment by work in the home, I have several reasons for believing that the contribution made by a non-wage earning surviving spouse as joint tenant should be recognized under the Kansas inheritance tax laws.

First, most estates in which the question of taxing an interspousal joint tenancy interest arises are larger estates in which the husband and wife have lived together and worked together for many years to acquire what they have. The spouse remaining in the home, in most cases the wife, has probably worked in the home seven days a week for many years. A simple mathematical calculation based on the present federal minimum wage and an 8-hour day immediately gives some idea of the monetary value of her services for which the wage earning spouse would have to pay a third party: $\$2.30 \times 56 \text{ hr./wk.} \times 52 \text{ wks./yr.} \times 20 \text{ yrs.} = \$133,952.00.$

Second, in most instances the male joint tenant dies first, and the burden is on the attorney for the decedent's estate to show a monetary contribution by the surviving female spouse. Any contribution which he can show immediately encourages an audit by the Internal Revenue Service, which in turn creates more work for the decedent's attorney and causes more expense to the decedent's estate. These legal disagreements are intensified if the property since acquisition has been improved and the non-wage earning spouse's fractional contribution to the improvement differs from his or her fractional contribution to the acquisition. Add to this

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the fact that inflation has greatly enhanced real property values over the years, and it becomes anyone's guess as to the total fractional contribution made by the surviving spouse. Thus, this whole area of contribution to jointly held interests is one of the most heavily litigated areas under estate and inheritance tax laws. All of this litigation and the expense resultant therefrom would be wiped out by a simple recognition of the non-wage earning spouse's contribution to the value of the couple's property.

Third, tax laws at all times since their origination have been used not only to raise revenue but either foster or discourage certain of our society's beliefs and activities. It is the implementation of this latter purpose which makes tax laws so difficult to understand and administer. The resultant difficulty of comprehension and administration, however, has not altered the use of the tax laws through the years for such purposes. For example, the latest federal estate and gift tax reform act has totally new rules for valuation of farms and closely held businesses, which create further complexity for the attorney handling an estate and estate planning, but which rules were felt necessary in order to encourage the continued existence of family farms and small businesses. Thus, the excuse that one might hear that measuring the contribution to the acquisition of jointly held property by the non-wage earning spouse would be so difficult as to discourage such a regulation, is not a valid argument. As I am not a tax expert, I do not have a formula prepared to offer by which to measure such a contribution; however, I have full confidence that such a formula or method can be created by those of you in the legislature who are.

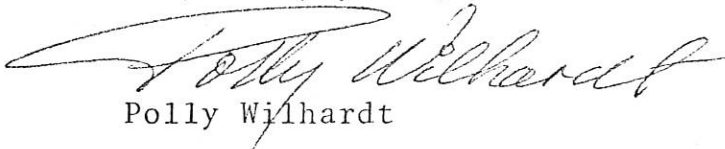
Fourth, in most of those estates which I have handled, the husband wage earning spouse dies first, and no monetary contribution to the jointly held property can honestly be shown to have been made by the surviving female non-wage earning spouse. Thus, the property is fully taxed in the husband's estate, and upon the wife's death is fully taxed again in her estate. However, under the exact mathematical circumstances in those fortunate families where the non-wage earning wife dies first, the property will only be taxed once, in the husband's estate. This is totally inequitable and cannot be rationalized to any of my clients. The burden of this inequity on the female non-wage earning surviving spouse is further increased, as she is often the one who does not have the continued needed income to pay this double taxation. In addition, when we are dealing in farm estates, the problem of lack of liquid assets also aggravates the situation.

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In closing, I would like to point out that I am advocating a change in the Kansas inheritance tax laws in this area only for those joint interests held by interspousal joint tenants. I believe the present rule as applied to nonmarried joint tenants is satisfactory. I would also like to point out that the memorandum issued to your committee from the Kansas Legislative Research Department dated May 18, 1977, indicates that the change I advocate in regard to interspousal joint interests would reduce Kansas inheritance tax collections by a lesser amount annually than any of the other changes in the inheritance tax laws proposed by bills introduced in the 1977 legislature.

Very truly yours,

A handwritten signature in cursive script, appearing to read "Polly Wilhardt". The signature is written in dark ink and is positioned above the typed name.

Polly Wilhardt

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