Approved On: 3/30/87

Minutes of the House Committee on Taxation. The meeting was called to order by E. C. Rolfs, Chairman, at 9:00 a.m. on March 20, 1987 in room 519 South at the Capitol of the State of Kansas.

The following members were absent (excused):

Representatives Vancrum and Wunsch

Committee staff present:

Tom Severn, Legislative Research
Chris Courtright, Legislative Research
Don Hayward, Reviser of Statutes
Millie Foose, Committee Secretary

Mr. Don Schnacke, representing Kansas Independent Oil & Gas Association, presented written testimony in support of HB-2405 (Attachment 1) and introduced Mr. Dick Randall, General Counsel for Petroleum, Inc., and chairman of the KIOGA Legislative Committee who spoke in support of this bill. (Attachment 2)

Mr. Charles Peterson, TXO Production Corporation, Wichita, spoke as a proponent of HB-2405 and presented the testimony of Petroleum Management, of Wichita. (Attachment 3) He also submitted 1987 Oil & Gas Appraisal Guide.

Mr. Larry Tenk, an independent oil producer from Ottawa, Kansas, spoke on behalf of Eastern Kansas oil & Gas Association. (Attachment 4) He said a temporarily abandoned well does not contribute to the ability of a lease to produce income and should not be taxed. He believes the continued operation of these marginal wells is essential to the future economic growth of Kansas.

Mr. Chip Wheelen of Pete McGill & Associates appeared in opposition to HB-2405. (Attachment 5) His organization believes that a temporarily abandoned oil or gas well retains anticipated future benefits. This concluded the public hearing on HB-2405.

Representative Wagnon explained SB-309 - AN ACT relating to sales taxation, and introduced Terry Humphrey, Executive Director of Kansas Manufactured Housing Institute. Ms. Humphrey spoke as a proponent and stressed the fact that the manufactured housing industry is not asking for special treatment or the complete elimination of a tax - only for equal treatment with similar forms of housing. (Attachment 6)

Mr. Lionel Clark, representing KIT Manufacturing Company, of McPherson. He said the industry is asking for parity with the rest of the housing industry in Kansas. (Attachment 7)

Mr. Bill Ewert, Division Manager of Skyline Corporation in Halstead, also spoke as a proponent. (Attachment 8) His firm believes the passage of SB-309 should be looked at as an investment in the future of the manufactured housing industry in Kansas.

Mr. Dick Dilsaver, representing the Coleman Company, spoke as a proponent. His firm believes that its passage would help save the 1000 jobs that are left. (Attachment 9)

Mr. Rod Taylor, representing Doug's Mobile World, Inc., spoke as a proponent of SB-309 as he believes its passage would put the manufactured housing industry more in line with conventional housing since consumers pay only on building materials when they purchase a conventional home, and this would have a positive effect. (Attachment 10)
There were questions from the committee concerning whether the appliances would be included and not subject to sales tax. It was explained that they were included in the 60% that was taxed.

The meeting was then recessed following adjournment of the house.

The meeting was reconvened at 12:30.

The Chairman brought TESA up for consideration. Representative Roe moved, second by Lowther, that the social security exemption apply to Tax Years 1988 and after. Motion carried. Representative Wagnon moved, second by Roe, that TESA be recommended favorably as amended. Motion carried with Fox and Spaniol being recorded as voting no.

SB-309 was then considered. Representative Leach moved, second by Reardon, that all publicly funded 501(c)3's be exempt from the sales tax. Representative Lowther moved, second by Leach, that the community MH & MR centers be totally exempt from the sales tax. Motion carried.

The chairman then adjourned the meeting.

Ed C. Rolfs

Ed C. Rolfs, Chairman

Written testimony was submitted by Rich McKee, Kansas Livestock Association regarding SB 309. (Attachment 11)

KIOGA

KANSAS INDEPENDENT OIL & GAS ASSOCIATION

500 BROADWAY PLAZA • WICHITA, KANSAS 67202 • (316) 263-7297

March 20, 1987

TO: House Committee on Taxation

RE: HB 2405

We have appeared before your committee before this session and have told you that our industry has been greatly contributing to the economic downturn in Kansas.

The Kansas Department of Human Resources has advised us recently that the U.S. Department of Labor has recently broadened its oil and gas worker retraining and relocation effort to 42 Kansas counties. Since a year ago, our industry has caused unemployment for approximately 5,000 Kansans and an equal number of jobs have been lost indirectly. This is merely the tip of the iceberg!

Our industry operates in ninety producing counties and the recent drop of oil prices has severely impacted on state sales and income tax collections. For the first time in my memory our industry is creating SRS clients in areas not before affected by chronic unemployment. There are several heretofore no-aid school districts that will begin to receive state school aid.

Governor Mike Hayden, before the last election, made a joint appearance with Lt. Governor Docking at our annual meeting in Wichita. Both candidates expressed concerns about the application of the Kansas ad valorem tax reflected in the annual renditions issued by the state due to large price swings. Both candidates indicated corrective action should be taken to relieve this problem. We're enclosing a transcript of Governor Hayden's remarks (then candidate Hayden) concerning this subject.

We are also attaching a compilation of the ad valorem tax collections by each county for 1986. The total is $100 million in taxes. It was $17 million in 1973 - only fourteen years ago.

At our Board of Directors meetings and Ad Valorem Committee meetings we often discuss solutions that could be offered that would relieve some of the unfair applicaions of the Kansas ad valorem tax to oil and gas properties.

Our federal government is very concerned about the plight of the oil industry in the United States, We would like to think Kansas legislators are also concerned about the future of the second largest industry in the state.

We are enclosing a clipping from this week's papers reflecting a special study released by the U.S. Department of Energy which supports tax incentives and regulatory changes to help stimulate the domestic oil industry in the United States.

House Tax Com. - 3/20/87 - Attach. 1

Perhaps more symbolic than substantive tax relief would be that provided for in HB 2405. This bill would simply exempt all property attached to a well officially designated by the KCC as Temporary Abandoned (TA). Used equipment, stacked in yards, waiting for better times to be used on future wells, would be exempt.

There are witnesses to testify in support of HB 2405 that have a practical view of how this might be of some help. They are Larry Tenk, President of EKOGA, Dick Randall, Vice President of KIOGA (Petroleum, Inc.), and Chuck Peterson, Chairman of the KIOGA Ad Valorem Tax Committee (TXO).

Mr. Chairman and members of the Committee, in these extraordinarily bad times for our industry, we are waiting to hear some good news arising from this legislature that can help us. This legislature is considering a package of bills that is supposed to improve the economic development of Kansas. As far as I know, our industry is not the subject of any of those proposals. Our economic development proposals are contained in SB 1, which would provide modest relief from the severance tax for a few low producing wells, and HB 2405, which is more symbolic than anything, but in the name of tax fairness.

We would urge your support of HB 2405.

Donald P. Schnacke

DPS:pp
Attch

CANDIDATE FOR GOVERNOR MIKE HAYDEN RESTATING AND ANSWERING A TAX QUESTION AT THE KIOGA CONVENTION, AUGUST 25, 1986

"Essentially, to paraphrase, Dick, what he said was that the severance tax on oil was 4.33% and it was enacted at a time when oil prices were considerably higher than they are today---in fact, twice as high as they are today---and, in the ad valorem situation, because of the recent decline in prices, ad valorem taxes are based on a price that is, in fact, far greater than the real price today and the industry is going to have to pay on an artifically inflated price and actually pay more taxes than the price would warrant, and do I have any suggestions or thoughts on those.

I would say that on the severance tax itself, that it is a percentage. It's a sales tax in that respect and, in fact, being on a percentage, as the price declines, even though the percent stays the same, that the actual dollar tax declines.

The other that you referred to however, the ad valorem, is much more unfair and the truth is that our current system is not modernized enough to take tremendous fluctuations in price, especially tremendous declines, on very short notice, and be able to compensate for that by reducing the taxes. I personally, Dick, think that the ad valorem situation is unfair right now to the oil and gas industry. I think that everybody--you know, uniform and equal is what the constitution says, and the truth is, it should not be based on an inflated price. And right now, we've experienced a situation where the prices fell drastically, in very short order and you're going to have to pay more taxes than you really should if it reflected the actual price.

I very much favor changes or improvements to the system and would call for them as Governor. I would call our ad valorem system to react to those immediate, short-term changes so that, in fact, you pay your fair share of taxes based on the real price, not based on some arbitrary price agreed to what the price of oil might have been six or eight months ago. So, I'm very much sympathetic, especially in the ad valorem situation because there isn't any doubt but what our system did not react fast enough to these declining prices and you're paying on artifically inflated price. I'm certainly opposed to that and, hopefully, we would design a system---this is an anomaly, our system---our ad valorem system's been in place for a long, long time and for many, many years, it was static, and so our system really wasn't modernized to take these tremendous rises and declines, especially those in very short order. Obviously, we're going to have to make some changes to that if that is going to be the future of the market. We all hope that these sudden falls and rises aren't the future of the market. We all hope for stability at a much higher level than currently exists today, but obviously, our ad valorem system has got to undergo some changes to react to it so that, in fact, you are assessed fairly on the oil out there that's still in the ground, and not on a deflated (probably meant "inflated") price and I'll very much support those changes."

Enc ry Study Supports Tax I entives, Regulatory Changes to Help Oil Industry

By Andy Pasztor
Staff Reporter of The Wall Street Journal

WASHINGTON—A comprehensive Energy Department report provides support for various tax incentives and regulatory changes to prop up the U.S. petroleum industry, while dimming prospects for any fee on oil imports.

The long-awaited study, which was requested by President Reagan, also highlights the need to harness nuclear power, coal and natural-gas reserves to protect against what it predicts may be a near-doubling in oil imports by the mid-1990s. And it suggests that despite White House opposition, accelerated filling of the government's Strategic Petroleum Reserve would be an important move to safeguard U.S. energy security.

Calling the report a "warning signal," Energy Secretary John Herrington told reporters that current production and consumption trends pose "a clear risk" to U.S. long-term national-security interests that can't be ignored. Based on the report's main findings, Mr. Herrington asserted, "it is time to plan" new initiatives and reassess some of the administration's longstanding energy policies.

The report is likely to help shape intensifying congressional and cabinet debate over the problems of domestic oil producers. The report doesn't contain any firm policy recommendations, however, and doesn't go nearly as far in proposing solutions as many oil-state lawmakers and domestic oil producers advocated.

Renewable Energy Resources

Other critics asserted that the report understates the role of renewable energy resources, and that its findings will be used to reduce environmental protection for offshore drilling sites and in Alaska's Arctic National Wildlife Refuge.

In a series of detailed cost-benefit analyses, the report indicates that imposition of a $10-a-barrel fee on imported oil would slash at least $32 billion in one year from the nation's gross national product. "I don't see this as a viable option," Mr. Herrington said.

The oil industry itself is sharply divided over the issue, with independent producers overwhelmingly supporting such a fee while some major international oil companies oppose it as an invitation to other taxes and a potentially cumbersome measure to enforce.

A spokesman for the American Petroleum Institute said the "thrust of the report seems to be in the right direction, although it may somewhat understate the problem." Reflecting the views of many independents in the oil patch, George Mitchell, chairman of Mitchell Energy & Development Corp., said the report "all but rules out" an import fee, which he called "the only option that can make an immediate difference" for the industry.

Palatable Compromise

The report and Mr. Herrington's comments suggest that the administration is searching for a politically palatable compromise that will demonstrate its commitment to help the industry without abandoning free-market principles. "It's an effort to buy the White House some political peace," asserted Edwin Rothschild, a spokesman for Citizen/Labor Energy Coalition, "rather than practical prescriptions for a sound and coherent national energy policy."

By the end of 1995, according to the report, Persian Gulf producers will provide as much as 65% of the free world's total oil consumption.

In discussing the most effective ways to spur domestic production, the report suggests higher depletion allowances, repeal of the 1980 windfall-profits tax, and repeal of the so-called transfer rule, which relates to tax treatment of certain properties purchased by independents from major oil companies.

Western Digital Plans To Redeem Certain Debt

IRVINE, Calif.—Western Digital Corp. said it plans to redeem April 6 all $47 million of its 6¾% convertible subordinated debentures due 2011.

Each $1,000 face amount of debentures is redeemable for $1,090.94, including accrued interest, the company said.

Until the close of business April 6, each $1,000 face amount of debentures is convertible into common stock at $17.50 a share. Western Digital has about 23 million common shares outstanding.

Bentsen Seeks Tax Breaks To Boost U.S. Oil Output

By a Wall Street Journal *Staff Reporter*

WASHINGTON—Sen. Lloyd Bentsen said he has asked congressional tax specialists to prepare a list of possible tax incentives to boost domestic oil production.

"I think you need more direct incentives for new drillings at the well," the Texas Democrat told reporters. He said he had the staffs of the Senate Finance Committee, which he heads, and the Joint Tax Committee, of which he is vice chairman, "looking at numbers" for proposals to accomplish that end.

An Energy Department study to be released today concludes that tax breaks are the least costly and most efficient way to stimulate U.S. oil exploration and development. The report lists several options, including a 5% tax credit for drilling and a boost in the oil depletion allowance, which is a deduction based on the value of the oil produced.

Energy Secretary John Herrington briefed Sen. Bentsen and a few other oil-state lawmakers on the study yesterday. The study, as expected, states that the cost of oil import fees would exceed their benefits for the economy as a whole.

Sen. Bentsen suggested the sale of offshore leases and the sale of oil from federal lands in Alaska to pay for incentives to boost domestic oil production. Both ideas are likely to be controversial, though Sen. Bentsen called them "very plausible options." Asked if a gasoline tax was another option, he replied, "At this point, I'm not ready to say that."

TO: House Committee on T ation
BY: R. D. Randall
RE: Support of H.B. #2405 March 20, 1987

STATEMENT

Mr. Chairman and members of the Committee, I am Dick Randall, General Counsel for Petroleum, Inc., and Chairman of the KIOGA Legislative Committee. I am appearing in support of H.B. No. 2405.

My company is a medium sized, independent oil and gas exploration company with its home office in Wichita, Kansas. Petroleum, Inc. was founded in 1948, and we explore and have production in 13 Midwestern states. We operate approximately 300 oil and gas wells in the State of Kansas. We are still drilling wells in Kansas, but on a very reduced budget in 1986, and again in 1987.

The Kansas oil and gas industry is in a severe economic depression, as you know. At the last count, only 48 rotary rigs were running in the entire State of Kansas. 1986 Kansas crude oil production fell 11% from 75.4 million barrels in 1985 to 67 million barrels in 1986. Natural gas production fell 13% from 517 BCF in 1985 to 452 BCF in 1986.

Both crude oil and natural gas prices have also fallen substantially. The oil price is down 40% from $28/barrel in January, 1986 to $17/barrel today. Six months ago oil was selling for only $12/barrel. Is it any wonder that Kansas operators are in a severe cash flow crunch, and that many have sold or gone into bankruptcy?

Because of low oil and gas prices, Kansas operators are plugging their most unprofitable wells. Petroleum, Inc. plugged and abandoned 15 marginal Kansas wells during 1986. However, we have also temporarily abandoned 81 oil wells and 10 gas wells since 1-1-86. These wells are still fully equipped and capable of being returned to production when economic conditions permit. After being shut in 100 days, these wells were reported to the Kansas Corporation Commission as temporarily abandoned (T.A.) wells. Such T.A. well status must be renewed by KCC application annually.

The Kansas operator's problem is that most wells in Western Kansas producing less than 4 barrels of oil per day are now marginal or unprofitable. In most cases, each lease has a different group of W.I. owners. The decision about whether to temporarily abandon or to permanently abandon each marginal lease is in the hands of those investors. Although there are some operating expenses to maintain shut in wells, the main cost item is the ad valorem tax on lease equipment. Many such lease owner groups want to plug T.A. wells when they get their annual ad valorem tax bill in December.

H.B. #2405 is designed to encourage Kansas operators and lease owners to temporarily abandon marginal wells, rather than to plug them. When such wells are plugged and abandoned, the remaining oil or gas reserves are lost forever. This small incentive is substantial lease by lease for the oil industry, although total tax revenue to the county from assessment of T.A. well production equipment is minimal.

As you know, Kansas oil and gas lease owners are heavily taxed as a result of having both a severance tax and an ad valorem tax. It makes economic sense for the State of Kansas to encourage the temporary abandonment of marginal oil and gas wells so that such wells can be produced again when price increases make them profitable. I urge you to vote in favor of H.B. #2405. Thank you.

* * * * * *

House Tax Com. - 3/20/87 - Attach. 2

Gasoline prices

(Approx. prices for self-service unleaded gasoline)

	Price ex. tax 3-11-87	Pump price* 3-11-87	Pump price 3-12-86
Atlanta	72.8	91.5	88.4
Baltimore	66.8	89.3	103.0
Boston	70.8	90.8	96.8
Buffalo	70.4	92.1	101.9
Miami	71.4	90.1	92.3
Newark	73.5	90.5	95.6
New York	73.9	95.9	107.9
Norfolk	65.6	92.1	91.3
Philadelphia	67.5	92.5	98.9
Pittsburgh	70.2	95.4	98.5
Wash., D.C.	65.4	89.9	109.1
Others† Avg.	72.8	95.9	99.0
PAD I Avg.	71.5	94.1	98.8
Chicago	64.5	90.3	100.7
Cleveland	66.6	87.6	84.6
Des Moines	66.6	91.6	87.6
Detroit	59.6	86.0	88.6
Indianapolis	55.0	80.7	85.5
Kansas City	60.9	76.9	74.2
Louisville	65.8	89.8	88.9
Memphis	69.5	95.5	97.4
Milwaukee	63.1	89.6	92.9
Minn.-St. Paul	61.9	87.9	97.5
Oklahoma City	62.2	81.2	76.2
Omaha	64.5	91.7	79.1
St. Louis	65.4	81.4	77.4
Tulsa	62.7	81.7	75.3
Wichita	66.6	86.6	77.2
Others† Avg.	66.9	88.5	90.1
PAD II Avg.	64.2	86.9	86.3
Albuquerque	68.5	88.5	87.6
Birmingham	72.9	94.9	103.6
Dallas-Ft. Worth	65.9	89.9	89.9
Houston	65.3	89.3	87.7
Little Rock	72.5	95.0	85.4
New Orleans	70.7	96.4	99.8
San Antonio	67.0	91.0	92.5
Others† Avg.	65.7	89.2	97.7
PAD III Avg.	67.8	91.1	94.3
Cheyenne	74.1	91.1	86.8
Denver	66.3	93.3	80.5
Salt Lake City	72.4	95.4	91.0
Others† Avg.	71.6	96.4	93.9
PAD IV Avg.	71.2	94.5	89.2
Los Angeles	80.3	103.1	103.1
Phoenix	78.0	103.0	105.0
Portland	72.5	93.5	104.3
San Diego	83.2	106.2	105.6
San Francisco	77.5	100.1	100.7
Seattle	66.2	93.2	107.5
Others† Avg.	81.7	104.7	111.8
PAD V Avg.	79.0	102.3	108.1
Week's Avg.	**70.32**	**93.22**	**95.81**
Feb. Avg.	**69.45**	**92.34**	**106.92**
Jan. Avg.	**68.18**	**90.93**	**113.86**
1987 to date	**68.90**	**91.72**	..
1986 to date	**85.77**	**107.89**	..

*Pump price includes state and federal motor fuel taxes and state sales tax. Some local governments may impose additional taxes.
†Includes other major cities within the PAD district.
Source: Oil & Gas Journal
Data available in Oil & Gas Journal Energy Database.

Hughes rig count

	3-9-87	3-10-86
Alabama	7	15
Alaska	6	18
Arkansas	5	17
Arizona	0	0
California	47	73
Land	39	62
Offshore	8	11
Colorado	24	39
Florida	1	1
Illinois	6	5
Indiana	2	1
Kansas	48	50
Kentucky	0	2
Louisiana	105	186
N. Land	9	9
S. Inland Waters	16	26
S. Land	32	58
Offshore	48	93
Maryland	0	0
Michigan	28	31
Mississippi	9	22
Montana	6	12
Nebraska	3	2
New Mexico	32	31
New York	0	0
North Dakota	8	17
Ohio	22	10
Oklahoma	111	169
Pennsylvania	19	19
South Dakota	0	0
Texas	227	413
Offshore	19	24
Inland Waters	0	3
Dist. 1 & 4	33	54
Dist. 2 & 3	34	58
Dist. 5 & 6	27	65
Dist. 7B & 9	21	44
Dist. 7C,8 & 8A	77	153
Dist. 10	16	12
Utah	2	12
West Virginia	18	10
Wyoming	28	41
Others–Nv.-2	2	16
Total U.S.	**766**	**1,212**
Cum. Avg. to Date	**844**	**1,547**
Canada	179	393
Canada-Offshore	1	5
Grand Total	**946**	**1,610**

Source: Hughes Tool Co.
Data available in Oil & Gas Journal Energy Database.

Rotary rigs from spudding in to total depth

OGJ production report

Crude oil and lease condensate (1,000 b/d)

	3-6-87*	3-7-86†
Alabama	56	63
Alaska	1,870	1,895
California	1,082	1,162
Colorado	72	80
Florida	19	29
Illinois	78	93
Kansas	158	203
Louisiana	1,370	1,459
Michigan	65	83
Mississippi	78	85
Montana	71	81
New Mexico	194	218
North Dakota	113	133
Oklahoma	365	436
Texas	2,145	2,397
Utah	92	118
Wyoming	330	342
All others	183	181
Total	**8,341**	**9,058**

*OGJ estimate †Revised
Source: Oil & Gas Journal
Data available in Oil & Gas Journal Energy Database.

Refined product & world crude prices

(Dollars per barrel)

	Feb. 27 1987	Feb. 20 1987	Jan. 2 1987	Feb. 28 1986	% change Feb. 1987/1986
Spot market product prices					
Motor gasoline					
Rotterdam (98 octane)	19.69	19.69	18.00	19.22	+ 2.4
New York (87 octane)	19.01	19.53	19.43	18.16	+ 4.7
Heating oil (No. 2)					
Rotterdam (0.3% sulfur)	17.56	18.96	20.04	26.80	−34.5
New York (0.2% sulfur)	18.48	19.53	19.68	23.45	−21.2
Residual fuel oil (No. 6)					
Rotterdam (1% sulfur)	14.48	15.54	15.39	15.46	− 6.3
New York (1% sulfur)	15.25	16.00	17.50	17.05	−10.6

Crude oil prices*	Current price	Previous week	Jan. 2 1987	Feb. 28 1986	% change 1987/1986
Total OPEC	17.31	17.35	16.10	26.88	−35.6
Total non-OPEC†	16.42	16.94	16.44	18.73	−12.3
Total world†	16.96	17.19	16.24	23.73	−28.5
U.S. imports††	16.42	16.74	15.32	20.80	−21.1

*Official sales prices or estimated term contract prices.
†Average price (FOB) weighted by estimated export volume.
††Average price (FOB) weighted by estimated import volume.
Source: DOE Weekly Petroleum Status Report.
Data available in Oil & Gas Journal Energy Database.

PETROLEUM
MANAGEMENT
INC. 400 N. WOODLAWN, SUITE 201 WICHITA, KANSAS 67208 (316) 686-7287

March 18, 1987

Mr. Charles Peterson
TXO Production Corporation
155 North Market
Wichita, Kansas 67202

Re: House Bill No. 2405

Dear Mr. Peterson:

I will appreciate your conveying the information contained herein to the House Committee on Taxation when you appear before the Committee on March 20.

Incorporated in 1952, Petroleum Management, Inc. has drilled about 550 wells in western Kansas, including more than 100 wildcats, and during the 1970's purchased more than 200 wells from major oil companies. We remained active in exploration and development drilling through 1985, drilling 36 wells between January 1984 and December 1985. Most of our production is in Phillips, Graham, Ellis, Russell, Trego and Rooks Counties, so I believe that our statistics are representative of an active independent producer operating in that general area.

On January 1, 1986 we had 168 active producing wells and 55 active injection wells. An additional 90 wells were in a temporarily abandoned status. During 1986 we shut down 62 producing wells and 14 injection wells, 37% of our active operations.

We plugged 49 wells in 1986 at a cost of $184,376, more wells than we had plugged in the preceding 10 years. Three or four of the wells were plugged due to massive mechanical failure, but the rest were plugged under pressure from KCC-KDHE that resulted from the State's unwise decision to declare the Dakota Sand to be productive of useable water. On the wells not equipped with tubing and a packer, it would have cost about $1,500 per well to run a mechanical integrity test, and we elected to plug many of those wells rather than to spend the money for the test. The bleeding had to stop somewhere.

House Bill No. 2405 addresses an important segment of the tax problem facing oil and gas producers. It is one thing to be taxed on oil or gas produced; it is quite another to be taxed on idle equipment or non-producing wells.

House Tax Com. - 3/20/87 - Attach. 3

In the counties where we operate, the 124 wells which are either shut down or temporarily abandoned represent a significant liability hanging over our heads, since plugging and lease restoration costs exceed the value of the equipment. For one thing, casing recoveries at abandonment average only about 1200 feet, and it is less costly to call a cementing company and simply cement down casing than it is to attempt to recover the pipe.

Both the state and counties must realize that the current system of taxation of oil properties is an anachronism, ill-suited to the crisis of the past fourteen months. They must also realize that reluctance to afford tax relief to producers will only hasten the day when there will be no oil and gas taxes to collect. The industry is no longer the goose that lays the golden eggs. It is a turnip from which too much blood has already been taken, and it is not over yet - - we still have to come up with $97,000 in June to pay second half ad valorem taxes, based on 1985 production, plus equipment.

Oil production in Kansas declined 23%, from 216,000 barrels per day in January 1986 to 158,000 barrels per day in March 1987. The old wells have thus shown dramatically that they are a rapidly dwindling tax base. I feel confident that we can find significant oil reserves after the shock of recent months is absorbed and put behind us, but we will need the full cooperation of the state and counties in the matter of tax relief.

Please express my respectful request to the Committee for the favorable reporting out of House Bill No. 2405.

Sincerely,

PETROLEUM MANAGEMENT, INC.

President

RDReber:bb

1987 OIL & GAS APPRAISAL GUIDE

EXERPTS PERTAINING TO HOUSE BILL NO. 2405

Section XI Equipment Value (Page 9 of guide)

(This Section covers equipment on oil leases)

b. A temporarily abandoned well (TA) is defined as a well that has had the equipment removed in anticipation of plugging prior to abandonment. If the well qualifies as a "TA" well, it has no market value and is appraised at zero value.

c. A shut-in well (SI) is defined as a lease which has equipment in place but production has been stopped, or shut-down, or curtailed due to economic reasons such as a lack of market demand or negative cash flow rather than reserve depletion. A "SI" well is valued at $1.50 per ft. per well for wells 2001 ft. and deeper; and $.50 per ft. per well for wells 2000 ft. and less shallow.

GAS SECTION

(13) TA, SI & SWD Wells (Page 18 of guide)

a. A "temporarily abandoned" (TA) well is defined as a well that has had the equipment removed in anticipation of plugging prior to abandonment. If the well qualifies as a "TA" well, it has no market value and is appraised at zero value.

b. A "shut-in" (SI) well is defined as a well which has equipment in place but production has been stopped or shut-down or shut-in due to economic reasons such as lack of market demand rather than reserve depletion and a "SI" well is valued per Paragraph 6, page 16, if new; and $1.50 per ft. of depth if shut-in longer than two years except for leases addressed per Paragraph 14 following.

(Paragraph 14 covers gas wells that produce but are heavily curtailed.)

There are no provisions in the guide specifically covering equipment value on gas wells which are no longer economic and have been shut-in less than 2 years. Interpretations of the guide for valuing this equipment could range from using $1.50/ft. of depth of equipment value or itemizing the equipment value.

ITEMIZED EQUIPMENT SECTION (Pages 24-27 of guide)

This Section itemizes values for various oilfield equipment for New, Used and Salvage categories. This Section would be used to value idle "Yard" equipment.

LEGISLATIVE IMPACT ON OIL & GAS GUIDE

HOUSE BILL 2405

1) Redefine TA wells to be either wells without equipment or equipped wells having filing status of "TA" with the Kansas Corporation Commission as of 7/1 of the prior year to rendering.

2) Equipped wells without "TA" status will continue to be valued as either producing or shut-in wells.

3) All idle equipment being temporarily stored would no longer be valued per the Itemized Equipment Section of the guide.

HOUSE BILL 2405

FISCAL IMPACT

Temporarily Abandoned Wells (filed w/KCC)

1986 - 5216 filings made

1987 - 2750 filings made through 3/16/87

Valuation of '87 TA Wells

A. Project 5500 filings by 7/1/87
B. Assume 50% of wells w/equipment = 2750 wells
C. Average Depth = 3000'
D. Mill levy for '86 was 75.19 mills

1. TOTAL STATE VALUATION

Value = 2750 wells x 3000 x $1.50/ft = $12,375,000
Assessed Value = $12,375,000 x 30% = $3,712,000
Tax = $3,712,500 x .07519 = $279,000

2. PER WELL VALUATION

Value = 3000' x $1.50/ft = $4500/well
Assessed Value = $4500 x 30% = $1350/well
Tax = $1350 x .07519 = $102/well

Idle Equipment Valuation

Five major independents* in Kansas average $100,000 of idle yard equipment.

Assessed Value = $100,00 x 30% = $30,000
Tax Value = $30,000 x .07519 - $2260/operator

1986 Total Oil & Gas Tangible Tax = $100,817,602.

*Most Kansas Independents will have considerably less than $100,000 of idle yard equipment.

Eastern Kansas Oil & Gas Association, Inc.
15 N. Lincoln · Box 355 · Phone 431-1020
Chanute, Kansas 66720

HB 2405

TESTIMONY BEFORE THE HOUSE COMMITTEE ON TAXATION

My name is Larry Tenk. I am an independent producer from Ottawa, Kansas. For the past two years I have served as president of Eastern Kansas Oil & Gas Association with offices in Chanute, Kansas. I am appearing before this committee on behalf of EKOGA.

The oil industry in Kansas is in a holding pattern. The uncertainty and direction of the crude market has resulted in many wells being placed in a temporarily abandoned status. Oil and gas properties in Kansas are taxed on their ability to produce income. A temporarily abandoned or shut-in well does not contribute to the ability of a lease to produce income and should not be taxed.

The Eastern Kansas Oil & Gas Association feels that the continued operation of these marginal wells is essential to the future economic growth of Kansas.

We ask that the committee give favorable consideration to this bill.

Thank you.

KLPG

Kansas Legislative Policy Group
301 Capitol Tower, 400 West Eighth, Topeka, Kansas 66603, 913-233-2227
TIMOTHY N. HAGEMANN, Executive Director

March 20, 1987

opponent

TESTIMONY
to
HOUSE TAXATION COMMITTEE
House Bill 2405

Mr. Chairman and members of the Committee, I am Chip Wheelen of Pete McGill and Associates. We represent the Kansas Legislative Policy Group which is an organization of rural county commissioners. We appear today in opposition to House Bill 2405.

As you may know, K.S.A. 79-329 pertains to ad valorem taxation of "all oil and gas leases and all oil and gas wells, producing or capable of producing oil or gas in paying quantities". There is an important distinction between a temporarily abandoned well and a plugged well because the abandoned well remains "capable of producing oil or gas" and therefore has a market value. By contrast, a permanently abandoned well has no market value and is not subject to property taxation.

Those of you who are acquainted with taxation of mineral properties are aware that such properties are appraised using the income approach to value. That methodology includes

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consideration of production history as well as price trends, reserve declines, and other factors. As a result, curtailed production because of temporary abandonment is already taken into account upon appraisal of the well.

According to Property Assessment Valuation by the International Association of Assessing Officers, the income approach to value "restates market value by converting the future benefits of property ownership into an expression of present worth." The same text explains that "Investors, the typical owners of income producing properties, place chief emphasis on the income approach in making decisions to buy or sell."

The investor makes decisions based on one of the fundamentals of determining market value; "present worth of all the anticipated future benefits to be derived from the property" (Property Assessment Valuation). We respectfully submit that a temporarily abandoned oil or gas well retains anticipated future benefits. Therefore HB 2405 defies one of the most fundamental principles of property appraisal and taxation.

In addition to our theoretical concerns, we are opposed to HB 2405 for a practical reason. If this bill became law, an operator could notify the Corporation Commission before July first that the well had been temporarily abandoned, claim an exemption for the entire year, and then resume production during the second half of the year; thus escaping taxation of a producing well. We respectfully submit that this loophole would be inherently unfair.

For these reasons, we respectfully request that you report HB 2405 <u>not</u> <u>recommended</u> for passage. Thank you for your consideration.

TESTIMONY BEFORE THE HOUSE

TAXATION COMMITTEE

TO: Representative Ed Rolfs, Chairman
and Members of the Taxation Committee.

FROM: Terry Humphrey, Executive Director
Kansas Manufactured Housing Institute

DATE: March 20, 1987

Mr. Chairman and members of the Committee, I am Terry Humphrey, Executive Director of Kansas Manufactured Housing Institute. Thank you for the opportunity to appear before you in support of Senate Bill 309.

Senate Bill 309 creates a 40% reduction on sales tax paid on new manufactured housing. Currently when an individual buys a new manufactured home, sales tax is paid on the full retail cost of the home. This is in contrast to stick built housing where sales tax is paid only on construction materials used in building.

Under the provision of Senate Bill 309, home buyers will pay sales tax on 60% of the purchase price of a new manufactured home. This percentage ensures that sales tax is being collected on construction materials and any additional items added to the sale at the retail level for set up. The Howard P. Gates study revels that the cost of materials in a new manufactured home are approximately 43.67% of the retail cost of the home.

If Senate Bill 309 becomes law, two important results will be achieved. First, our consumer who is often a "first time home buyer" in the low to moderate income range, will no longer be taxed unfairly. A recent survey found the medium household income of manufactured home buyer to be $16,881 annually and the average cost of a new manufactured home approximately $20,000. Obviously, this group of home buyers should not be asked to bare a larger tax burden.

To show you how the sales tax bill can impede the home buyer lets do the sales tax calculation. The average new manufactured home of $20,000 generally requires a 10% down payment which would be $2,000. In Ottawa, Kansas where sales tax is 6% the tax bill is $1,200. In some cases finance companies will not finance the sales tax since in the case of default, sales tax is a nonrecoverable item.

The second point I would like to make is that the manufactured housing industry has been an important part of the Kansas economy, however, in the past three years we have lost nine manufacturers and

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four suppliers representing a minimum of 1,140 jobs and 640 of those jobs were lost in the last nine months. In addition, it is estimated that the closing of those plants has resulted in the state losing more than one million dollars in corporate taxes and Kansas communities losing in excess of 16.5 million in payroll.

Today, there are five manufactured housing plants left in Kansas and a few suppliers, and they need your help if they are going to be able to stay in Kansas. Certainly the present health of the manufactured housing industry is tied to the overall Kansas economy, but certain negative marketing factors such as sales tax inequity hinder them as well.

It is encouraging to see the Legislature direct it's attention towards economic development; and the economic development legislation that is going through the Legislature is over due and will benefit everyone in the long run. However, at this time, none of the economic development proposal will specifically help the manufactured housing industry, but, Senate Bill 309 will. I agree with the Redwood Report from the 1986 session which states that Kansas should be concerned with the industry that already resides within it's borders and our efforts should be directed to enhance their business climate.

Already 17 states have taken steps to eliminate sales tax inequities and some of those states are: Arkansas, Colorado, Georgia, Indiana, Iowa, Minnesota, Texas, and Wisconsin.

In conclusion, I would like to remind the Committee that the manufactured housing industry is not asking for special treatment or the complete elimination of a tax - only for equal treatment with similar forms of housing. It is well known that the primary obstacle to the passage of Senate Bill 309 is the small fiscal note that it carries. However, it is our contention that the revenue loss will actually be lessened due to an increase in sales and a stronger industry. KMHI urges your support of Senate Bill 309 and we thank you for your attention to this matter.

TH:mn

MANUFACTURED HOME PLANTS OF KANSAS - 1987

KIT Manufacturing Company
P.O. Box 738
McPherson, Kansas 67460

Liberty Homes, Inc.
P.O. Box 18
Yoder, Kansas 67585

Schult Homes Corporation
P.O. Box 409
Plainville, Kansas 67663

Skyline Corporation
920 W. 2nd Street
Halstead, Kansas 67056

Skyline Corporation
P.O. Box 719
Arkansas City, Kansas 67005

CLOSED MANUFACTURED HOME PLANTS IN KANSAS

BelleVista Homes - Closed 1984
Russell, KS - 85 Employees

Classic Designs, Inc.- Closed 1985
Hutchinson, KS

DMH Company, Inc. - Closed 1985
Newton, KS - 125 Employees

Commodore Home Systems Inc. - Closed 10/86
Ottawa, KS - 70 Employees

Zimmer Homes of Kansas - Closed 11/86
Newton, KS - 100 Employees

Guerdon Industries, Inc. - Closed 7/85
Manhattan, KS - 75 Employees

Marlette Homes - Closed 2/85
Great Bend, KS - 125 Employees

River Oaks Homes - Closed - 3/86
Hutchinson, KS - 275 Employees

DMH Company, Inc. - Closed 1985
Hutchinson, KS - 100 Employees

CLOSED SUPPLIERS IN KANSAS

Congoleum Corporation - Closed 6/86
Newton, KS - 110 Employees

Hajoca Corporation - Closed 9/86
Newton, KS - 10 Employees

Kansas Forest Products - Closed 1986
McPherson, KS - 10 Employees

Donovan Company - Cloased 1985
Newton, KS - 5 Employees

KIT MANUFACTURING COMPANY
One Kit Boulevard, P.O. Box 738 ■ McPherson, Kansas 67460 ■ (316) 241-1500

March 20, 1987

Chairman Rolff and Members of the Committee:

My name is Lionel Clark and I represent Kit Manufacturing Company located in McPherson. I am here in support of SB 309. Kit has been producing manufactured housing for the past 27 years in Kansas. We presently employ about 70 people with an annual payroll of $900,000.

Our industry has declined from 27 plants operating in the 70's to the present 4 manufacturers with a total of 5 plants. The 27 plants created employment for over 3,000 with an annual payroll in excess of 60 million dollars. In addition to the 27 plants, Kansas was also the distribution center for many of the industries support businesses.

The decline of manufacturing facilities in the state caused the majority of these support businesses to relocate in other states creating additional lost employment.

The remaining five plants in Kansas are operating at less than 40% capacity, making it increasingly difficult to justify to the Board of Directors and Stockholders why we should remain in Kansas.

I do not profess, by simply reducing the amount of sales tax charges on the sale of new manufactured homes, all of our problems will go away and next year we will see 27 plants operating again, but it will help.

We as an industry, ask only for parity with the rest of the housing industry in Kansas, and by your support of SB 309, this will become a reality.

So much has been said about economic development. I consider your support of SB 309 as an investment into the future of our industry here in Kansas and the employment it creates.

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Skyline Corporation
920 West Second Street
P.O. Box 311
Halstead, Kansas 67056
[316] 835-2214

To: Chairman Ed Rolfs and Members of the House Taxation Committee

Date: March 20, 1987

Re: S. B. 309; Sales Tax Equity

I am Bill Ewert, Division Manager of Skyline Corporation in Halstead. I appreciate the opportunity to testify today in favor of S. B. 309.

Skyline Corporation has two plants in Kansas; the other plant is located in Arkansas City. Both plants have produced homes continuously for over twenty-seven years. During this time, each plant has paid out thousands of dollars in local and state taxes and millions of payroll dollars. At one time, annual employment stood at 275 with a payroll of 4 million dollars. However, because of the present economy, our total employment now stands at 70 with an annual payroll of $1.2 million. This translates to a per plant efficiency rating of 25%, obviously a money losing situation.

Fourteen years ago our industry claimed to be the third largest industry in Kansas. Now it is a struggle just to stay in existence. In the last year alone, three manufactured housing manufacturers in Kansas have closed their plants. Should this happen in the small community of Halstead, the loss of jobs and revenue would be devastating.

We think it is important to the future of our industry to only pay sales tax on materials used. As things stand now, our customers pay tax on the full retail cost of the home.

Since some finance companies will not finance sales tax, reducing the amount of tax by 40% would lower the dow payment and help more people qualify for home ownership. Selling more homes will allow us to recall laid off workers which will bring in new tax dollars, not cost the state tax dollars.

The passage of S. B. 309 should be looked at as an investment in the future of the manufactured housing industry in Kansas and a boost to the state's economy. Thank you for your consideration.

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Coleman

The COLEMAN COMPANY, INC.
General Offices
P.O. BOX 1762
WICHITA, KANSAS 67201
AREA CODE 316 261-3211

March 20, 1987

TESTIMONY FOR THE KANSAS HOUSE OF REPRESENTATIVES COMMITTEE ON TAXATION

Good morning, Chairman Rolfs and members of the committee. I am Dick Dilsaver, representing The Coleman Company. We appreciate this opportunity to present our views on why Senate Bill 309 definitely deserves your support.

When the substance of this bill first came to my attention early this year, I wondered why I and my company -- knowing the dire financial squeeze the Legislature is in -- could have the audacity to back a measure that apparently could reduce state income. We found good reason to stand up and be counted on behalf of S.B. 309: Our state could very possibly gain much more overall from this bill than it might lose.

We take our position on the basis of first-hand knowledge. You probably know The Coleman Company best as a world-famed manufacturer of outdoor recreation products. But you may not know that almost one-third of Coleman's business comes from production of heating and air conditioning equipment; and almost two-thirds of that portion is in producing heating and air conditioning for the manufactured housing industry.

Kansas has been a very bright light in that field, and we supply almost 90 percent of the heating and air conditioning in manufactured homes made in our state. But we have seen that industry plummet in Kansas, and our sales to Kansas manufactured housing producers are down 60 percent in the past three years.

When Coleman experiences such a sharp drop in business, we do not just shrug it off. We look hard for the reasons. What we found is an industry in distress. The slide in the Kansas economy, particularly in agriculture and energy, has struck many potential buyers of manufactured housing, and thus it has hit manufacturers hard. It cost Kansas nine manufactured housing plants, several suppliers and more than 1,100 jobs.

However, we also found this industry is not being treated equitably. It is handicapped in Kansas because it is not on a level playing field with other housing. And every little bit of handicap hurts manufactured housing a lot.

Buyers of manufactured homes, unlike those buying conventional housing, must in effect pay a premium: full sales tax. S.B. 309 would end some of the inequity this industry faces.

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Fortunately for Coleman, the impact of lost manufactured housing sales has been offset by improvements elsewhere in the company. It would have been good, though, to add workers to handle the increased business, instead of just moving some from the down area.

Unfortunately for communities such as Hutchinson, Ottawa, Manhattan, Great Bend, Newton and Russell where manufactured home plants have closed, the lost jobs have not been replaced. Coming on top of energy and agriculture job losses there, that's tragic, with far-reaching consequences throughout Kansas.

In these trying times, the state would rightfully go to virtually any lengths to attract 1,100 jobs. We contend it should go the relatively small length of S.B. 309 to try to help save the 1,000 jobs left. You regularly hear huge figures, such as a payroll of $2 million to $6 million for just 100 new jobs, plus great concentric amounts in such areas as retail sales and tax revenues. Think what it has cost to lose 1,100 jobs, what it will save if we prevent more job losses and what we will regain if we restore some jobs.

Some local governments oppose this bill, fearing loss of sales tax revenue. That is over-reaction and short-sighted. Anything that stimulates manufactured home sales, which this bill could do, will help not only the industry but their communities, local governments and the state overall as well.

Surely an economic impact statement would show the relatively small amount of tax revenue foregone through this legislation would be repaid several times over if this industry can be salvaged.

Last year, a bill similar to S.B. 309 came close to adoption before it was pushed aside by political considerations late in the session. Since then, closings of manufactured housing plants have cost Kansas 640 jobs. I can virtually guarantee you that if this industry does not get a fair shake and S.B. 309 does not pass this session, more manufactured housing plants and suppliers will be closed -- and more jobs will be lost to Kansas -- by the time the Legislature meets again.

I earnestly encourage you to vote for S.B. 309.

DOUG'S
mobile world inc.
* your energy minded dealer *

TO: Representative Ed Rolff, Chairman
Taxation Committee

DATE: March 20, 1987

RE: Sales Tax Reduction on New Manufactured Homes

Mr. Chairman and Members of the Committee:

My name is Rod Taylor. I am president of Doug's Mobile World, Inc., a manufactured housing dealership and South Village, Inc., a manufactured housing community, both located in Topeka. I am here today to urge your support of SB 309 which would reduce the sales tax on new manufactured houses by 40%.

The average price of a single wide home in Topeka is $20,000. At a tax rate of 5%, the consumer would be required to pay $1,000. in sales tax making the total cost of the home $21,000. With the 40% reduction provided by SB 309, the consumer would be paying $400. less sales tax, which is a significant amount of money to most purchasers.

Lack of down payment is the biggest reason that people are renting homes instead of buying. Many lending institutions require sales tax as part of the down payment, meaning the purchaser must pay 10% down plus sales tax. The addition of sales tax increases the down payment by 50%. Therefore, you can see that a reduction in sales tax would allow more qualified buyers to realize their dream of home ownership.

If the home were to be financed, the reduction in sales tax would result in a lower down payment and a lower amount to be financed. This could mean a great deal to the potential buyer especially when the financing institution bases their allowance for housing expense on a percentage of the purchaser's income. This could make the difference in whether or not a loan would be approved for funding.

4010 SOUTH TOPEKA BLVD. • TOPEKA, KANSAS 66609 • (913) 862-0321

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Those who would benefit from the reduction would include young people just starting their careers at a base income level and older people who are at or near retirement age facing a fixed income level. Young people, single and married, usually have a limited amount of funds available for down payment and housing expense. Therefore, they look to manufactured housing as an affordable first home. It is the fixed income level of retired or retiring individuals that persuades them to choose manufactured housing as an alternative to the high maintenance costs of conventional homes.

The tax savings proposed in SB 309 would be another positive reason, in addition to affordable and economic housing, for consumers to make a buying decision and I'm sure it will have a positive effect on many families of all ages in the future.

Please remember that this reduction in sales tax will now put the manufactured housing industry more in line with conventional housing since consumers only pay tax on building materials when they purchase a new conventional home.

I thank you for the opportunity to appear and testify today and I appreciate your support of SB 309.

Respectfully submitted,

Rod Taylor

Rod Taylor, President
Doug's Mobile World, Inc.
South Village, Inc.

Kansas Livestock Association

2044 Fillmore • Topeka, Kansas 66604 • Telephone: 913/232-9358
Owns and Publishes The Kansas STOCKMAN magazine and KLA News & Market Report newsletter.

STATEMENT

OF THE

KANSAS LIVESTOCK ASSOCIATION

TO THE

COMMITTEE ON

TAXATION

REPRESENTATIVE ED ROLFS, CHAIRMAN

REPRESENTATIVE KEITH ROE, VICE CHAIRMAN

WITH RESPECT TO SB 309

SALES TAX

PRESENTED BY

RICH MCKEE
EXECUTIVE SECRETARY, FEEDLOT DIVISION

MARCH 20, 1987

Mr. Chairman and members of the committee, I am Rich McKee. I am here representing the Kansas Livestock Association. KLA represents a broad range of over 9,000 livestock producers who reside in virtually every geographic corner of the state. A good number of our members feed, water, doctor and generally care for livestock. Some of these members feed, water, doctor and generally care for livestock on a custom or "for hire" basis.

We ask for your support for SB 309 in attempt to prevent a segment of our membership from receiving what in effect would be a tax increase.

With the passage of SB 686 during the 1978 legislative session feedlots or individuals who raise livestock (beef, dairy, swine, sheep) in more confined pens have been entitled to a sales tax exemption on the purchase of used farm machinery and equipment, repair and replacement parts therefor and services performed in the repair and maintenance of such machinery and equipment. To clarify this point I have attached Department of Revenue Information Guide 19-78-2. Please note on page 2 that feedyards are specifically listed as to be included in the exemption.

written testimony only

Attachment 11

The Department of Revenue is proposing to reverse their interpretation and begin taxing commercial feedyards on the purchase of their used farm machinery and equipment. The Department is changing their interpretation due to a Kansas Supreme Court ruling on a property tax case dealing with farm machinery. Unless legislation is passed clarifying that feedyards should continue to be entitled to this exemption a tax increase will be experienced.

Because this is an exemption livestock feeding operations are and have been entitled to this provision of the bill is revenue neutral.

Information Guide 19-78-2

Sales Tax

Exemption for Used Farm Machinery and Equipment

Kansas Department of Revenue

REFERENCE. K.S.A. 79-3606 (u) and proposed regulation P-3606 (u)-1.

PURPOSE. This information guide is intended to assist persons in the application of the sales tax exemption for used farm machinery and equipment, repair and replacement parts and repair and maintenance of used farm machinery and equipment.

This information guide includes the rules and principles of proposed regulation P-3606 (u)-1 which has been printed on page 3. THE RULES AND PRINCIPLES IN THE PROPOSED REGULATION WILL BE APPLIED BY THE DEPARTMENT BEGINNING JUNE 1, 1978. Comment on the proposed regulation is invited from all interested parties and should be addressed to the Director of Taxation, Division of Taxation, P. O. Box 692, Topeka, Kansas 66601. The Department will hold hearings in December, 1978, concerning the permanent adoption of this regulation.

I. GENERAL RULE.

K.S.A. 79-3606 (u) provides that from May 1, 1978 to July 1, 1981, all farmers and ranchers will be exempt from paying Kansas sales tax on the following:

a. Purchase of used farm machinery and equipment;
b. Purchase of repair and replacement parts for used farm machinery and equipment; and,
c. Charges for service performed in the repair and maintenance of used farm machinery and equipment.

In order to qualify for the exemption contained in K.S.A 79-3606 (u), both of the following conditions must exist:

a. The purchaser is a farmer or rancher; and,
b. The property purchased, repaired or serviced will be used only in farming or ranching.

II. DEFINITIONS.

a. "Farm machinery and equipment" means all machinery and equipment which is purchased by a farmer or rancher and which is used only in farming or ranching. However, the phrase "farm machinery and equipment" does not include buildings, building materials, silos, fence, land, passenger vehicles, trucks, truck tractors, trailers, semitrailers, or pole trailers, other than a farm trailer. Therefore, any piece of machinery or equipment other than those just listed, can qualify as farm machinery and equipment if it is purchased by a farmer or rancher and if it is used only in farming or ranching.

For example, if a person who is neither a farmer nor a rancher purchases a hay baler, then the hay baler would not be considered farm machinery or equipment because it was not purchased by a farmer or rancher (See subsection b below for definition of "farmer or rancher"). On the other hand, if a used mower were purchased by a farmer for use only in farming, then the used mower would qualify as farm equipment. However, if a mower were purchased by a farmer for use partially in farming and partially in maintaining the yard of his personal residence, then the mower would not qualify as farm equipment because it was not purchased for use only in farming or ranching.

Examples of items which may qualify as farm machinery and equipment, if purchased by a farmer or rancher for use only in farming or ranching, are: combines,

Issued May, 1978

cultivators, discs, farm tractors, forage blowers, grain grinders, hay balers, loaders, mowers and rakes, harrows, irrigation equipment, mechanical ensilage cutters, milking machines and related equipment, planters, plows, sprayers, fans, blowers and ventilating units, feed handling equipment, feeding troughs, fire extinguishers, water hose for livestock use, gas cans and funnels, log chains, protective covers for farm machinery and equipment (other than buildings), rope, space heaters, stock waterers, water heaters and welding equipment.

b. "Farmer or rancher" means a person who:

(i) owns, leases or sharecrops real property used for farming or ranching; and,
(ii) is engaged in the business of farming or ranching on such real property (See subsection (c) below).

As an example, the owner of a commercial feedlot would qualify as a farmer or rancher if the feedlot owner leases or owns the real property on which the feedlot is located and if the feedlot owner is farming or ranching as defined below. On the other hand, neither a custom cutter nor a crop duster will normally qualify as a farmer or rancher unless the two conditions listed above are met.

c. "Farming or ranching" means engaging in activity which is ordinary and necessary for the growing or raising of agricultural products. "Farming or ranching" does not include activity occurring after the harvesting of crops or after the time immediately preceding slaughter of livestock. For example, a person in the business of storing grain would not be considered engaged in farming or ranching. Neither would a slaughterhouse be considered farming or ranching.

d. "Sales of used farm machinery and equipment" means the sale or lease of farm machinery and equipment other than the original retail sale or lease of such farm machinery and equipment. To qualify as "used", an item must be sold or leased to someone other than the original user. For example, if Mr. X leases a new tractor for one month (taxable as original lease) and then purchases it after one month's use, the sale will not constitute the sale of used farm machinery and equipment because the sale was not made to someone other than the original user. A dealer or retailer will not be regarded as the original user of property unless the dealer or retailer has paid sales or use tax on the purchase price of such property.

e. "Repair and replacement parts" means those parts which replace an existing part, or which are necessary to maintain the working condition of a piece of farm machinery or equipment. For example, the sale of a new air conditioner for the cab of a tractor which was not previously air conditioned would not be considered the sale of a repair or replacement part because the new air conditioner is not replacing any existing part nor is it necessary to maintain the working condition of the tractor. However, if a cab without air conditioning is totally replaced by a new air conditioned cab, then the whole new cab would qualify as a "replacement part" because it is replacing an existing part of a piece of farm machinery.

Other examples of "repair and replacement parts" are air filters, antifreeze, batteries, belts, bolts, cable and clamps, gear, hydraulic cylinders, lubricants, oil filters, paint (but not for buildings), plow points, plow shares, sickle sections, spark plugs and tires. However, the sale of these items are exempt only if: 1) purchased by a farmer or rancher; and, 2) the parts are to repair or maintain machinery or equipment used only in farming or ranching.

III. PROCEDURES.

a. Used machinery and equipment. In order to qualify for this exemption, the purchaser of used machinery and equipment must certify in writing on a copy of the invoice or sales ticket that the purchaser is engaged in farming or ranching and that the farm machinery or equipment purchased will be used only in farming or ranching. The retailer must retain this signed certification for a period of at least three years.

b. Repair and replacement parts and service. In order to sell parts or repair and maintenance service without tax, the retailer must secure an exemption certificate from the purchaser (or a certification as in subsection (a) above). A retailer who repeatedly makes the same type of exempt sale to the same purchaser may take a blanket exemption certificate covering all such sales, rather than a separate exemption certificate for each transaction. However, with a blanket exemption certificate, the retailer will be required to keep a record of all exempt sales showing the date, amount, customer's name, item(s) sold, and invoice number if applicable. This record can be kept by maintaining a listing at the cash register; sales tickets or invoices are not necessary for parts and service. These records and exemption certificates must be retained by the retailer for a period of at least three years.

A retailer who secures an exemption certificate from a purchaser is relieved from sales tax liability if the exemption certificate has been accepted in good faith. An appropriate exemption certificate form appears on page 4 of this information guide. This form may be reproduced for use by retailers.

Questions concerning the application of K.S.A. 79-3606 (u) or this information guide should be directed to Sales and Excise Tax Bureau, Kansas Department of Revenue, Topeka, Kansas 66625, or phone number 913-296-2461.

PROPOSED REGULATION P-3606 (u)-1. USED FARM MACHINERY AND EQUIPMENT, REPAIR AND REPLACEMENT PARTS THEREFOR, AND REPAIR AND MAINTENANCE SERVICE THEREFOR.

(a) General Rule.

In order to qualify for the exemption contained in K.S.A. 79-3606 (u), both of the following conditions must exist:

(1) The purchaser is a farmer or rancher; and
(2) The property purchased, repaired or serviced will be used only in farming or ranching.

(b) Definitions.

(1) "Farm machinery and equipment" shall mean any machinery and equipment which is purchased by a farmer or rancher and which is used only in farming or ranching, but shall not include buildings, building materials, silos, fence, land, passenger vehicles, trucks, truck tractors, trailers, semitrailers, or pole trailers, other than a farm trailer.

(2) "Farmer or rancher" shall mean a person who:

(i) owns, leases or sharecrops real property used for farming or ranching and,
(ii) is engaged in the business of farming o ranching or such real property.

(3) "Farming or ranching" shall mean engaging in activity which is ordinary and necessary for the growing or raising of agricultural products, but shall not include activity occurring after the harvesting of crops or after the time immediately preceding slaughter of livestock.

(4) "Sale of used farm machinery and equipment" shall mean the sale or lease of farm machinery and equipment other than the original retail sale or lease of such farm machinery and equipment; to qualify as "used", an item must be sold or leased to someone other than the original user.

(5) "Repair and replacement parts" shall mean those parts which replace an existing part, or which are necessary to maintain the working condition of a piece of farm machinery or equipment.