Approved March 2, 1988
Date

MINUTES OF THE SENATE COMMITTEE ON ASSESSMENT & TAXATION.

The meeting was called to order by Senator Fred A. Kerr at
Chairperson

11:00 a.m./~~p.m.~~ on March 1, 1988 in room 519-S of the Capitol.

All members were present except:

Committee staff present:

Tom Severn, Research
Chris Courtwright, Research
Don Hayward, Revisor's Office
Sue Pettet, Secretary to the Committee

Conferees appearing before the committee:

Pat Barnes, Ks. Motor Car Dealers Assoc.
John Torbert, Assoc. of Counties
Gerry Ray, Johnson County Comm.
Don Schnacke, KIOGA
Barney Sullivan, Eastern Ks. Oil & Gas
Bob Barnett, Eastern Ks. Oil & Gas
Secretary Harley Duncan

Chairman Kerr called the meeting to order and announced the agenda for the day to be hearings on Senate Bills 77 and 75.

SENATE BILL 77

Pat Barnes testified in support of S.B. 77. (Att. 1) He stated that S.B. 77 would repeal the inventory tax stamp for motor vehicle inventories. If passed, this would be effective January 1, 1989. He stated that S.B. 77 would put motor vehicle dealers on the same level with other retail merchants after Jan. 1, 1989. He stated that everyone is paying inventory tax now, and the dealerships feel that they should not be the only segment of the retail community required to pay inventory tax after January 1. He said that Kansas would be the only state in the region which taxes motor vehicle inventories if S.B. 77 is not passed.

John Torbert testified in opposition to S.B. 77. (Att. 2) He stated that the Association of counties is against the bill because it represents another example of erosion of the local tax base. He felt that in counties with a large number of dealerships, this would be a significant revenue loss.

Gerry Ray testified in opposition to S.B. 77. (Att. 3) She stated that the bill would cost Johnson County and cities within close to half a million dollars in tax revenue. She stated that Johnson County Commission urged the committee to vote against S.B. 77.

SENATE BILL 75

Don Schnacke testified in support of S.B. 75. (Att. 4) He stated that last year the intent of S.B. 75 was to focus on two problems.

1. The lack of good definition for services rendered when drilling an oil and gas well.
2. To address a problem arising from a sales tax audit and a subsequent court decision relating to materials used in the drilling of oil and gas wells as consumables.

He said that one main purpose of S.B. 75 is to address a reversal the Kansas oil and gas industry suffered as a result of an audit of a small independent oil and gas company in Wichita. The audit and appeals resulted in the decision that drill bits, pipe, and cement used in drilling are not consumables as defined under 79-3602. The result was a permanent tax increase for the industry, which is currently in a depressed state.

Barney Sullivan testified. (Att. 5) He stated that economic conditions in the oil and gas industry are so severe that any savings are necessary to survive. This bill would be economic incentive. He urged support of the bill.

MINUTES OF THE SENATE COMMITTEE ON ASSESSMENT & TAXATION,

room 519-S, Statehouse, at 11:00 a.m./p.m. on March 1, 1988

Bob Barnett testified in support of S.B. 75. He felt that the industry is suffering greatly, and any incentive would be very helpful.

Secretary Harley Duncan testified on S.B. 75. (Att. 6) He stated that S.B. 75 amends K.S.A. 79-3602(m) which is the definitional section of the Retailers' Sales Tax Act regarding property consumed in the production, manufacture, etc. of tangible personal property. He stated that rewriting the definition of consumed property creates a situation in which a number of unintended consequences could result. He stated that the current definition has served well in its intended purpose for twenty years. He stated that if the policy in S.B. 75 is to be adopted, the Department would rather it be in an amendment to K.S.A. 79-3606, the normal sales tax exemption statute, by adding a new sub-section to cover the desired property rather than amending K.S.A. 79-3602(m). In response to a question, Secretary Duncan stated that a fiscal note would be approximatley $2.7 million per year.

SENATE BILL 491

Senator Salisbury gave a brief review of the information obtained by the Sub-Committee on S.B. 491. (Att. 7 is the proposed substitute for S.B. 491) (Att. 8 is sub-committee minutes) Senator Salisbury stated that the proposed substitute for S.B. 491 was not an exemption bill but an amnesty bill.

Senator Salisbury made a motion that the sub-committee report for S.B. 491 be adopted. Senator Burke seconded.

In response to a question, Keith Farrar stated that he felt S.B. 491 is a more fair approach in that it is not designed to handle one specific organization, but will deal more fairly on an overall basis. Motion carried.

Sen. Salisbury moved that the committee recommend Sub. S.B. 491 favorably for passage. Sen. Allen seconded. Motion carried.

Senator Mulich made a motion to adopt the minutes of the Feb. 29th meeting. Sen. Allen seconded. Motion carried.

Meeting adjourned.

3-1-88

Dana Fennell	Topeka	Budget
Loren Schechter	Hugoton KS	trucker
Georg Scobee	Topeka	gmca
BILL PERDUE	TOPEKA	Ks Comm. Serv. Agency
H Duncan	Topeka	Revenue
MARK BURGHART	"	"
DEAN TRIMMELL	Council Grove	Ks Motor Car Dealers
CARL O. ISCHEIDE	BURLINGTON	— — —
John T. Torbert	Topeka	ICAC
Jerry Ray	Olathe	Jo Co Comm
Marla Howard	Wichita	City of Wichita
Larry Stephens	Emporia	ESU
John Taylor	Topeka	KPL Gas Service
Jay Vocek	Topeka	KSCPA
T. C. Anderson	Topeka	KSCPA
Tom Whitaker	Topeka	Ks Motor Carriers Assn.
Ron CALBERT	NEWTON	United Transportation Union
Rich Dame	Hoisington	B. h. E.
Jim McBride	Topeka	observer
John O'Neal	Topeka	TRA
Jeff Chaney	Topeka	KIOGA
Lou CASTELLUCCI	CHANUTE	EKOGA
Ken Peterson	Topeka	KPC
Qingshan Wang	China	Visitor
Don Martin	CHANUTE	EKOGA
Walter Dunn	EKOGA	Topeka
J. B. Shang	Topeka	Automobile Dealer
Dwight Young	TOPEKA	Auto Dealer
Stu Yaugher	Topeka	auto Dealer
Jennifer Wise	TOPEKA	Visitor (student)
Cowin Smith	TECUMSEH	VISITOR
Kathy Young	Topeka	Visitor
John Blythe	Manhattan	KFB
Hyde Parker	Manhattan	KSU

G. BOB BARNETT	CHANUTE	Eastern Kansas Oil & Gas Assoc.
BARNEY SULLIVAN	✓	✓ ✓ ✓ ✓ ✓
Robert Anderson	Ottawa	Kirk Cantrell Oil & Gas
Ron Hein	Topeka	Mesa Limited Partnership
Don Schnacke	"	KIOGA -

Statement Before The

SENATE COMMITTEE ON ASSESSMENT AND TAXATION

By The

KANSAS MOTOR CAR DEALERS ASSOCIATION

Tuesday, March 1, 1988

Re: SB77

Mr. Chairman and Members of the Committee, I am Pat Barnes, legislative counsel for the Kansas Motor Car Dealers Association. Our trade association represents most of the franchised new car and new truck dealers in Kansas

As most of you are aware, we requested and have supported SB77, which would repeal the inventory tax stamp for motor vehicle inventories. If passed, the repeal of the Motor Vehicle Dealer Inventory Tax Stamp Act would be effective January 1, 1989. This is the same effective date for the Classification Amendment which the voters of Kansas approved in November, 1986. This is the same date when inventory tax on all retail merchants, except car dealers, will be eliminated.

We have visited with most of you about SB77. I doubt there is anyone on this committee who is not familiar with it at this point. However, we do appreciate the opportunity to once again outline the points which we believe require the passage of this bill. In so doing, I will review the history of the Inventory Tax Stamp Act.

In 1974 the Legislature passed SCR #3 which provided a constitutional amendment, which was approved by the voters at a special election in August, 1974. This amendment provided for the classification and taxation of motor vehicles as a class or the exemption of this class from property taxation and the imposition of taxes upon another basis in lieu thereof.

In 1978, K.M.C.D.A. proposed that motor vehicles held in inventory for resale by motor vehicle dealers be exempted from the usual basis of inventory taxation, and in lieu thereof, a tax be imposed at the time of the retail sale of the motor vehicle. Payment of the tax was to be verified by affixing a stamp to the title or manufacturer's Statement of Origin for the vehicle. This proposal became the present Inventory Tax Stamp Act and was effective January 1, 1979.

The Inventory Tax Stamp Act has been reviewed several times since 1979. An interim study in the summer of 1980 prompted an increase in the price of the tax stamps during the 1981 session. In 1985, the price of tax stamps was again raised to the current level which ranges from $2.00 for motorcycles to a maximum of $45.00 on heavy duty trucks.

For a number of years merchants in the State of Kansas desired to have merchants and manufacturer's inventory tax eliminated for a variety of reasons. This Legislature responded by

passing the Classification Amendment to the State Constitution and placing it before the voters for their approval, which they did. Voter approval came by a large majority and merchants and manufacturers' inventories will no longer be taxed after December 31, 1988, unless a merchant happens to be a car dealer.

Motor vehicle dealers have always paid merchant's inventory tax. Prior to 1979, this was done the same as all other merchants. After 1979, a system of checks and balances, i.e., the stamp tax, was put in place to assure that all tax was paid. This method was as much a benefit to the entire state as it was to car dealers. Tax no longer escaped due to inventory sell-offs prior to the time at which reporting was to be made, or due to outright under-reporting with this method of taxation. The unique manner in which vehicles are titled and sold made this method of paying inventory tax easily accomplished and verified.

Technically, the Inventory Stamp Tax may be called an excise tax in lieu of inventory tax. However, it is an inventory tax and we have been left out of the scheme granted all other merchants and manufacturers whereby inventories will not be taxed. We have to compete on the same basis as these individuals, we have the same costs and we operate in the same economies, good or bad, in which all other merchants operate. We need the repeal of this tax.

Most recently, we notice SB453 which dealt with Proposal No. 7 of the interim study reports. This dealt with the exemption of inventories from taxation and the bill is presently in the House Taxation Committee. What is interesting about the bill is that it defines "inventory" to mean all personal property owned or held, subject to the control of a merchant, which was purchased by the merchant for resale at an advanced price or profit. This is exactly what car dealers hold on their lots for resale to the public, and I don't believe anyone would seriously argue that we aren't paying an inventory tax under the present method of taxation.

SB77 will put motor vehicle dealers on the same level with other retail merchants after January 1, 1989. Everyone is paying inventory tax now, and we feel that we should not be the only segment of the retail community required to pay inventory tax after January 1. The effective date of SB77 is January 1, 1989, the same date as classification goes into effect, so dealers will not get a tax break ahead of any other retailer on inventory with the passage of this bill.

Kansas will be the only state in this region which taxes motor vehicle inventories if SB77 is not passed. Missouri, Colorado, Nebraska and Oklahoma all no longer tax motor vehicle inventories, and we compete with car dealers in those states. In

fact, when I made inquiry of Oklahoma and Colorado, the reaction was one of disbelief that this method of taxation still exists. Apparently, Oklahoma has not taxed motor vehicle inventories for some time. Missouri and Nebraska are only recent additions to the idea of exempting inventories from taxation.

Rather than belabor you further with our reasons as to why SB77 should be passed, I will provide you with a summary of our points and reasoning. This summary is attached to my testimony.

We believe the tax policy of this state as articulated in the past by the Legislature and the voters of Kansas is to exempt inventories. There is no fair and rational reason as to why an inventory tax should remain in place only upon our segment of the business community.

Thank you for your time and the opportunity to present our point of view to you. You have been very patient with us both in the committee room and outside. We appreciate the input you have allowed us to provide to you. This is an important issue for our members, one of fairness, and we request that you recommend SB77 favorable for passage by the full Senate.

Thank you for your time. I would certainly be happy to answer any questions you may have.

SB77 - INVENTORY TAX STAMP REPEALED

1. The voters of Kansas passed a constitutional amendment repealing inventory tax.

2. Motor vehicle dealer inventory tax was not included as it was contained in a separate section of the law. (In 1979, an exemption was made for dealers to pay inventory tax in the form of a stamp "in lieu of" inventory tax. This alternate method was as much an advantage to the counties-state as to dealers.)

3. Reclassification and reappraisal can only be expected to raise our property taxes and this higher property tax will off-set county inventory tax loss.

4. Dealers have always paid inventory tax as has every other merchant, but ours could be verified without adjustment.

5. Our stamp tax method was convenient, but no tax advantage was obtained over other retailers since no vehicle in inventory escaped tax. All tax was paid.

6. Car dealers will be the ONLY retail merchants who continue to pay inventory tax.

7. Car dealers seek only the equitable repeal of the inventory tax as accorded our fellow retailers.

8. Kansas will be the only state in this region taxing motor vehicle inventories if SB77 is not passed.

9. In 1987, 386,816 inventory tax stamps were sold with a dollar value of $2,758,665.00. These taxes will be off-set by other revenue, including the tax climate after income tax reform, increases due to reappraisal, and the affect of classification.

10. SB77 will put car dealers on an equal status with all other merchants.

Kansas Association of Counties

Serving Kansas Counties

212 S.W. Seventh Street, Topeka, Kansas 66603 Phone (913) 233-2271

March 1, 1988

Testimony

To - Members, Senate Assessment & Taxation Committee

From - John T. Torbert, Executive Director
Kansas Association of Counties

Subject - SB 77

The Kansas Association of Counties is opposed to Senate Bill 77 which would exempt motor vehicle inventories from taxation. The bill represents just one more example of erosion of the local tax base.

In counties with a large number of auto dealerships, this would be a rather significant revenue lose for all local taxing jurisdictions. I obtained the following information about the revenue losses which would occur if this legislation were enacted. These figures are actual 1987 receipts.

Douglas County	$ 62,896	Total
	$ 14,371	County share
Johnson County	$451,527	Total
	$ 79,536	County share
Sedgwick County	$525,063	Total
	$ 81,977	County share
Shawnee County	$217,643	Total
	$ 47,173	County share
Wyandotte County	$241,097	Total
	$ 42,042	County share

I would also point out that the state receives two percent of this revenue too so this legislation would also impact your own revenue sources.

Please keep our tax base in mind as you consider this and other exemption legislation. As I said before this committee earlier, tax exemptions don't lower taxes. They just mean that those who pay taxes pay more.

A & T

3/1/88

Att. 2

SENATE ASSESSMENT AND TAXATION COMMITTEE

TUESDAY, MARCH 1, 1988

HEARING ON SENATE BILL 77

TESTIMONY OF GERRY RAY, INTERGOVERNMENTAL COORDINATOR
JOHNSON COUNTY BOARD OF COMMISSIONERS

MR. CHAIRMAN, MEMBERS OF THE COMMITTEE, MY NAME IS GERRY RAY, REPRESENTING THE JOHNSON COUNTY BOARD OF COMMISSIONERS. THANK YOU FOR THE OPPORTUNITY TO SPEAK IN OPPOSITION TO SENATE BILL 77.

THIS IS A VERY BRIEF BILL THAT SIMPLY EXEMPTS THE INVENTORY OF ALL NEW AND USED AUTOMOBILE DEALERS FROM ALL PROPERTY OR AD VALOREM TAXES. IT IS STATED IN LESS THAN A PAGE, AND WILL CAUSE A LOSS OF CLOSE TO A HALF A MILLION DOLLARS IN TAX REVENUE TO JOHNSON COUNTY AND THE CITIES WITHIN IT. THE COUNTY ALONE WILL LOSE APPROXIMATELY ALMOST $80,000 ANNUALLY.

LOCAL GOVERNMENTS FIND THEMSELVES IS A DIFFICULT SITUATION, AS THEY COPE WITH CUTBACKS IN REVENUE RECEIVED FROM THE FEDERAL AND STATE LEVEL WHILE THE DEMANDS FOR SERVICES CONTINUES TO INCREASE. THE NEED FOR HUMAN SERVICES GROWS EACH DAY, PARTICULARITY IN THE AREA OF THE ELDERLY. THE EFFECTS OF REAPPRAISAL AND CLASSIFICATION ARE UNKNOWN AND DETERIORATION OF LOCAL INFRASTRUCTURE CONTINUES TO BE A MAJOR PROBLEM.

THIS YEAR IS BEGINNING TO BRING BACK MEMORIES OF 1986 WHEN GROUP AFTER GROUP REQUESTED A SPECIAL TAX EXEMPTION, UNTIL RECORDS CAME CLOSE TO BEING SET ON THE NUMBER OF TAX EXEMPTIONS BILLS INTRODUCED. INDICATORS SEEM TO BE POINTING TOWARD THAT SITUATION AGAIN. WE WOULD AGAIN POINT OUT THAT WITH EACH TAX EXEMPTION GRANTED THE TAX LIABILITY IS SPREAD OVER A SMALLER TAX BASE, CREATING THE POTENTIAL FOR A SERIOUS PROBLEM IN KANSAS FOR THE OWNERS OF RESIDENTIAL AND AGRICULTURAL PROPERTY.

THE JOHNSON COUNTY COMMISSION URGES THE COMMITTEE TO VOTE AGAINST SENATE BILL 77.

KIOGA

KANSAS INDEPENDENT OIL & GAS ASSOCIATION

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

March 1, 1988

TO: Senate Committee on Assessment & Taxation

RE: SB 75 – Sales Tax on Consumables

Last year the intent of SB 75 was to focus on two problems:

1) The lack of a good definition for services rendered when drilling an oil and gas well, to meet the intent of KSA 79-3603 (p); and

2) To address a problem arising from a sales tax audit and a subsequent court decision relating to materials used in the drilling of oil and gas wells as consumables under KSA 79-3602 (m).

SB 75 was held up last year pending a Kansas Supreme Court decision which related to cement, but as it finally developed, that decision had no bearing one way or another on the issues or merits of SB 75.

During the 1987 interim, the subject of the application of sales tax to services relating to the drilling of oil and gas wells was addressed. The result was that the Department of Revenue, in cooperation with our industry, promulgated a new rule relating to services that are believed to be exempt. That rule is considered to be helpful in defining those services that a taxpayer can rely upon as exempt. The rule doesn't change the law, but does make it more clear what the law intends to exempt. For that, we are grateful for the input of this Committee and to the Department for their efforts.

The main purpose of SB 75 is to address a reversal the Kansas oil and gas industry suffered as a result of an audit of a small independent oil and gas company in Wichita. The audit and subsequent appeals resulted in the decision that drill bits, pipe, and cement used in drilling oil and gas wells are <u>not</u> consumables as defined under 79-3602 (m). The result was a permanent tax increase for our industry.

KSA 79-3602 (m) states as follows:

> "´Property which is consumed´ means tangible personal property which is essential or necessary to and which is used in the actual process of and immediately consumed or dissipated in (1)...drilling...but the listing of such property shall not be deemed to be exclusive nor shall such listing be construed to be a restriction upon or an indication of, the type or types of property to be included within the definition of ´property which is consumed´ as herein set forth:..."

The audit and the findings of the Department and the confirmation by the courts had the effect of imposing the sales tax on these items when they have been considered by the taxpayers to be exempt. The Department, late in 1986 following this decision, started going back to taxpayers to collect back sales taxes they believed were owed.

We also understand the Department believes dynamite is not a consumable when used by the oil and gas industry in its geophysical work in preparation for drilling services. We would like your committee to add dynamite to line 0129 in SB 75.

The legislature exempted services relating to drilling of oil and gas wells under KSA 79-3603 (p). Further, it intended to exempt materials consumed in drilling wells under KSA 79-3602 (m). We believe cement, bits, and pipe used in drilling an oil or gas well, as well as dynamite, are exempt and, additionally, are consumed when they are not retrievable and are lost forever. That is the basis for SB 75.

We would suggest you modify the definition of "casing" on line 0129 to be "unrecoverable casing, pipe and tubing that is cemented in place."

Donald P. Schnacke

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

February 29, 1988

Mr. Chairman
Members of the Committee

RE: Senate Bill No. 75

EASTERN KANSAS OIL & GAS ASSOCIATION rise in favor of adding certain consumables into the existing exemptions.

Casing, drill bits and cement have been considered consumable by the department because there is no recoverable material once utilization commences. This position has been reversed by regulation and is punitive in nature.

Economic conditions are such that any savings are necessary to survive. This bill should be considered as an economic incentive to the oil and gas operators and drillers throughout the State of Kansas.

I urge you to vote this bill out of Committee.

Thank you.

EASTERN KANSAS OIL & GAS ASSOCIATION, INC.

Barney E. Sullivan

Barney E. Sullivan
Executive Director

BES:je

A & T 3/1/88

Att. 5

MEMORANDUM

TO: The Honorable Fred A. Kerr, Chairman
Senate Committee on Assessment and Taxation

FROM: Harley T. Duncan
Secretary of Revenue

RE: Senate Bill 75

DATE: February 9, 1987

Thank you for the opportunity to appear before you on Senate Bill 75. The Department opposes enactment of the bill in its present form. Our concerns stem not from the intention of the bill, but rather the manner in which it goes about it.

As introduced, Senate Bill 75 amends KSA 79-3602(m) which is the definitional section of the Retailers' Sales Tax Act regarding property consumed in the production, manufacture, etc. of tangible personal property. It does so by adding specific reference to "drill bits, casing and cement actually utilized in the exploration and production of oil or gas" as consumed property.

Background

Presently, the section defines property which is consumed as "property which is essential or necessary to and which is used in the actual process of and **immediately consumed or dissipated** in the production, manufacture" ... etc. of tangible personal property for sale in the normal course of business and **which is not reusable for such purpose.** The section works with KSA 79-3606(n) which provides a sales tax exemption for property consumed in the production, manufacture, etc. of tangible personal property.

The "consummable" exemption is one of several exemptions which exist (along with ingredient and component part and sales for resale) that enable the Retail Sales Tax to accomplish its intended purpose. That being the levy of an excise tax, once and only once, on all retail transactions and to insure that the consumer, not the retailer, bears the burden of the tax. Absent such exemptions, there would by a "stacking" or pyramiding of taxes and any given final product could bear the sales tax several times.

SB 75 is a direct response to a recent Kansas Court of Appeals decision, **In the Matter of the Appeal of George Angle, d/b/a Frontier Oil Company v. Department of Revenue, 11 Kan. App. 2d 62 (1986).** In **Frontier Oil**, the Court found specifically that drill bits, casing and cement **were not consumed** in the production of oil and gas within the meaning of KSA 79-3602(m). The Court applied its reasoning from a 1974 case (**R.L. Polk and Co. v. Armold**) and determined that all three items are standard products utilized in the drilling of any typical well, that they are not designed for a specific customer to perform a specific job, and that drill bits may be used on more than one drilling job and cement and casing serve a useful purpose for as long as fifty years.

The Polk decision held that property which is not standard, is designed solely for a specific customer to perform a specific task and has value only as scrap after performing said task is consumed within the meaning of KSA 79-3602(m). The Polk decision barred from exemption items which wear out, depreciate, break, erode or become obsolete.

Department Concerns

The Department's primary concern is with changing a definitional section to include something that the Courts through applying some longstanding tests have specifically ruled are not within the definition. We feel this could lead to one or more of three possible results:

1. It could be held as invalid as an unreasonable classification because it is limited to products used in oil exploration and production where the same products are used for other types of drilling and in other activities. Similarly, KSA 79-3603(p) and (q) impose taxability generally on contractors, subcontractors and repairmen. SB 75 would segregate oil and gas well contractors from these statutes.

2. It could be interpreted to indicate legislative intent to broaden the meaning of "consumed" to include other types of machinery, equipment and property which wears out or cannot be reused and recovered. In this case, the fiscal impact is well beyond that envisioned here.

3. At the very least, it opens a path for owners and users of other types of property to claim that their property also falls within the meaning of "consumed" as rewritten in SB 75. Again, the fiscal and policy impact far exceeds that envisioned in SB 75.

Conclusion

In short, we fear that rewriting the definition of consumed property creates a situation in which a number of unintended consequences could result. The actual determination of what is consumed and what is not is a factual question and a function of the courts applying tests and case law developed over time. The current definition has served well in accomplishing its intended purpose for about 20 years. We would urge you not to amend KSA 79-3602(m). If the Legislature desires to exempt drill bits, casing and cement used in oil exploration and production, we would recommend that KSA 79-3606, the normal sales tax exemption statute, be amended by adding a new subsection (gg) to cover the desired property.

Thank you for the opportunity to appear on this matter. I would be glad to answer any questions

SUBSTITUTE FOR SENATE BILL NO. 491

By Committee on Assessment and Taxation

AN ACT relating to property taxation; concerning the exemption of certain property therefrom and providing a procedure therefor.

Be it enacted by the Legislature of the State of Kansas:

Section 1. Any group, association, corporation or individual who has not been assessed or levied a tax on its personal or real property prior to July 1, 1985, and who has applied for exemption from ad valorem taxation on such property premised upon use for purposes described in K.S.A. 79-201 Second between July 1, 1986, and January 1, 1990, shall not be liable for any taxes prior to January 1, 1986, if such group, association, corporation or individual had a reasonable basis to believe that it would not be assessed or taxed under the laws of the state of Kansas, and did not deceive or otherwise mislead, by affirmative misrepresentation, the county appraiser or other taxing authority in relationship to the use or ownership of such property. The burden of proof shall rest with the party claiming exemption. Relief may be granted under this section by a court in any pending tax appeal, by remand to the state board of tax appeals or upon the filing of an initial application pursuant to K.S.A. 79-213, and amendments thereto.

Sec. 2. This act shall take effect and be in force from and after its publication in the Kansas register.

ASSESSMENT & TAXATION
SUB-COMMITTEE MEETING
February 15, 1988

Present: Senator Salisbury
Senator Frey
Senator Parrish
Senator Hoferer, YMCA representative
Bob O'Connor, YMCA representative
Bill Perdue, YMCA representative
Sue Pettet, Secretary

Senator Alicia Salisbury, Chairperson for the Sub-Committee on SB 491, called the meeting to order and announced that the purpose of the meeting was to address four issues which were outlined by Bob O'Connor, attorney for the YMCA:

1 - The mootness issue
2 - Constitutional issues
3 - State policies supporting the bill
4 - Corrections to the Board of Tax Appeals' presentation to the committee

Mootness issue: He explained that if SB 491 were passed while the YMCA was still in judicial proceedings in Shawnee County District Court, and if the YMCA wins the 1986 issue in court, then it should win the back tax issue also. The reason for that would be that under the statute, exemption relates back to the first exempt use and that the first exempt use predates 1978 which is the back tax period. He stated that contrary to the representation that Mr. Davidson made, the YMCA's record before the Board was loaded with testimony, documented and oral, that the way the YMCA used its property in 1986 was the way it had always used its property.

Mr. O'Connor stated that if the YMCA loses the 1986 issue in court, then SB 491 would give the YMCA a fighting chance economically. It would remove approximately $500,000 debt. Otherwise, the YMCA would have to close its doors.

If the bill were passed and the YMCA is still in court, legal counsel for the YMCA would seek to have the cases consolidated.

Mr. George Scobas, Director of the Topeka YMCA, polled the YMCA and found that the YMCA would appeal a court loss of the 1986 exemption issue even if SB 491 is passed.

He stated that there were two areas they felt the Board of Tax Appeals was wrong. (1) The concept of what is an investment: The Board of Tax Appeals has decided that investment income is realized when an exempt organization is conducting the very activities that make it exempt and realizes any income above actual direct cost from program participants or members. Mr. O'Connor felt this was definitely a conflict of terms. (2) He felt the Board of Tax Appeals also looked at investment on a program by program basis. Instead of looking at a year-end balance sheet to see how the organization survived over-all, the Board of Tax Appeals is looking at the YMCA program by program

which he feels is unfair. The YMCA lost money every year for the last several years on an overall basis. The adult membership program is the only program out of 25 or 26 showing any profit, but that revenue was used to subsidize scholarships for youth. The Board of Tax Appeals is saying that if you make revenue over cost in any exempt program you have investment income. They are also saying that if you fund the activities with United Way money, that is not your money in the first place, so you don't get any credit for charitable activity.

Senator Bob Frey asked if there were two cases and for an explanation of each. Mr. O'Connor responded that there were two fundamental issues before the Board of Tax Appeals. (See attached titled "Corrections to the Board of Tax Appeal's Presentation on February 10, 1988) The first was if the Y were entitled to exemptions for 1986 and future years. The first year that was taxed was 1986, along with back tax bills. The Board of Tax Appeals was approached with that issue.

The second issue was if the Y were liable for back taxes. In the original court order of May 4, the YMCA won the back tax issue, and the county lost. The YMCA lost the 1986 exemption. The YMCA then filed a motion for re-hearing before the Board because not only was this a statutory pre-requisite but also because of a basic sense of fairness. There was a request for a re-hearing filed addressing the 1986 issue only which the YMCA lost. So the YMCA did not ask for a re-hearing on the back tax issue. The Board of Tax Appeals then came out with its later order on the YMCA's motion for a re-hearing and reaffirmed its earlier denial of the 1986 exemption issue, but also, for the first time, imposed back taxes. The situation is that the YMCA is now at the threshold of the courthouse on the 1986 issue because of a request for re-hearing. The YMCA then did file an application for judicial review in the Shawnee County District Court. It's the first of the two cases in district court, but because the YMCA had never lost the back tax issue and had never sought a re-hearing before the Board of Tax Appeals on that loss, the YMCA had to file a motion for rehearing on the back tax issue with the Board of Tax Appeals. The Board of Tax Appeals subsequently ruled against the YMCA. At a later time, there was a separate judicial review proceeding in Shawnee County District Court. This is how both cases got to Shawnee County District Court. There was then a motion filed for consolidation, and they were consolidated before Judge Reagan. This is where the YMCA currently stands regarding court status. Mr. O'Connor wanted it to be clear that the YMCA did not seek and then walk away from a hearing on the back tax issue as inferred by the Board of Tax Appeals. As previously stated, the back tax issue was won, and the county did not seek re-hearing of that issue. On the 1986 exemption issue, the YMCA did not present additional evidence on re-hearing because the record was complete and none was necessary.

The YMCA's re-hearing strategy was designed to avoid being "sand-bagged" by the Board of Tax Appeals as he felt is now being done. (See briefing material, Attachment I, which is an excerpt of the brief before Judge Reagan on the back tax issue in general). Mr. O'Connor

stated that on page 81 of that exerpt it explains that in the orders that were received from the Board of Tax Appeals, starting with the original May order, it was very clear that the Board of Tax Appeals had struggled with the decision and had come up with a compromise which was to not charge the YMCA with back taxes but that they would lose their exemption and have to start paying taxes. He stated that the Board of Tax Appeals made it very clear that if the YMCA wouldn't be happy with this compromise there would be worse retributions. Knowing this, the YMCA carefully thought out the strategy of not making any further appearance before the Board of Tax Appeals for purposes of exposing themselves to having to answer questions or do anything else that would put "a new piece of evidence" into the record. This could only hurt the YMCA and relate to the back tax issue, which they had already won. The YMCA did not have a re-hearing on the back tax issue at their request. They also didn't walk off from it although the Board of Tax Appeals insinuated this. Mr. O'Connor felt that the YMCA had been falsely accused of asking for a re-hearing and them walking away from it.

Mr. O'Connor discussed another point which he felt had been misrepresented by the Board of Tax Appeals at the February 10 Senate Committee hearing. The Board of Tax Appeals said the YMCA confined their case to 1986 and did not talk about prior years. When the Board got the submission statement stating that all the years of use had been the same, it was new evidence. The YMCA felt this was false. The YMCA went to the Board of Tax Appeals with information from 1978 through 1986 documenting the history of the YMCA regarding purposes of use. He said that in the 1986 case the YMCA had the advantage of the 1986 amendments, but if they were to say they were entitled to exemptions because of these 1986 amendments, the YMCA would lose on the back tax issue. It was very important for the YMCA to show the Board of Tax Appeals that in all the years of operation it was "business as usual." Mr. O'Connor stated that the only area in which there were any changes was regarding the financial statement. There were audited statements and an independent financial analysis of the operation. The man who did this only did it in 1986 as it was expensive. He was a person who services YMCAs (doing around 400 YMCA audits) to help standardize accounting systems of YMCAs.

Senator Parish asked if the YMCA could win the back tax issue before the court and lose the 1986 issue. Mr. O'Connor said that if the court wants to make that decision and say that because of improper quorum and other technicalities that the YMCA should not have been hit with the back tax order, he would then put the 1986 issue and the back tax issue in the same boat. "Then if we lose the 1986 issue we lose the whole deal!" Mr. O'Connor stated that he felt "if we win the 1986 issue, the Y would win it all," but he didn't see that the back tax issue could be won and not win 1986.

Constitutional Issues (Attachment I, second sheet)

Mr. O'Connor stated that the argument on Separation of Powers would be that the Board of Tax Appeals is an independent agency of the Executive Branch of the State Government. SB 491 as drafted would declare null and void the Board of Tax Appeals' September 9, 1987, order. The argument would be that the legislature would void action of the

executive. The YMCA's view is that the power to levy and collect tax is a legislative function under the Separation of Powers doctrine. SB 491 relates to tax matters and there would be no significant interference of the power of the Executive under SB 491 (See Attachment A) "The power of taxation is a legislative function. It is the province of the legislature to determine the subject and extent of taxation and to provide the means and agencies for enforcing in the absence of constitutional restrictions, and the taxing power of the legislature is supreme and complete, and nothing justifies the division of that power with the judiciary."

Senator Frey asked a question regarding the "separation of powers" issue. He said that this bill does not affect the Board of Tax Appeals as much as the right of the county to collect the taxes that have been assessed.

Mr. O'Connor stated that the bill in its proper form uses the language "null and void" and the Y would not be liable as it would not be enforceable. He stated that under the Separation of Powers doctrine, the legislature cannot give away its taxation powers. He felt that it could not be said that the legislature gave away its jurisdiction to the Board of Tax Appeals, the argument would be that it was not constitutional.

Mr. O'Connor stated that he felt SB 491 needed modification. SB 491 could be modified to"suspend" the effect of the Board of Tax Appeals' order and to "prohibit" the collection of the back taxes. These changes would replace the "null and void" language currently in the bill (line 28 of the bill).

Senator Frey stated that he didn't feel the YMCA case was so special that it would merit its own bill. There was discussion on the unique position of the Topeka YMCA and the argument for special acts of the legislature.(see Attachments E and F)

Senator Frey also asked questions regarding the small businesses in town that compete with the YMCA. He also felt it would benefit the Committee to know how USD #501 and the Shawnee County Commission view this legislation.

Senator Frey stated that Keith Farrar of the Board of Tax Appeals had testified before the Senate Committee that there were many cases of back tax issues before the Board of Tax Appeals, and asked just "how many" there really were.

Senator Salisbury stated that the sub-committee would be visiting with the Board of Tax Appeals and asked Senator Parrish and Senator Frey to design questions for them.

Meeting adjourned.

ASSESSMENT AND TAXATION
SUB-COMMITTEE MEETING
On SB 491, February 22, 1988
8:30 a.m., Room 531-N

Present: Senator Alicia Salisbury, Chairman
Senator Bob Frey, Member
Senator Nancy Parrish, Member
Senator Jeanne Hoferer, Representing YMCA
Keith Farrar, Board of Tax Appeals
James Davidson, Attorney for Board of Tax Appeals
Don Hayward, Revisor's Office
Bill Perdue, Representing YMCA
George Scobas, Representing YMCA
Betty Jones, Secretary

Senator Salisbury reviewed initial meeting of sub-committee at which Bob O'Connor, attorney for Wichita YMCA, was present and assisted in outlining issues and clarifying procedures with respect to Topeka YMCA.

Mr. Davidson presented proposed language for a bill to forgive back taxes not only for the Topeka YMCA but also for all other not-for-profit organizations who may, as a result of reappraisal re-mapping, find themselves liable for back years' taxes. (See attachment) He cited as an example a Masonic organization which as a result of reappraisal will owe the tax. The proposed language would allow them to be forgiven all back taxes up to the year 1986. He stated that he foresaw other groups falling within that same category and that, at this time, it is impossible to determine how many will be affected.

Senator Salisbury asked if there were any possibility that the draft might be unconstitutional. Mr. Davidson implied that it would not be and that it simply assured that all groups would be treated the same and that 1986 taxes could still be imposed.

The question was asked that if the proposed bill passed, how would it be implemented. Mr. Davidson responded that he thought of it as an amnesty bill -- not as an exemption bill. The proposed alternative bill, he again pointed out, would forgive taxes prior to 1986 only.

Senator Salisbury questioned the meaning of the phrase "affirmative representation" and Mr. Davidson replied that it meant that a clear impression had been left that the group would be tax-exempt and that the group had understood it to mean that. Mr. Davidson repeated he considered this to be an amnesty bill, not an exemption bill.

Senator Parrish asked if those who had already paid taxes might apply for a refund under this proposed bill. Mr. Davidson said those who are added to the rolls will know in advance what their status will be. Senator Frey felt that the proposed bill would require proof that an affirmative representation had been made. He asked why it would not be simpler for the Board of Tax Appeals just to rescind its order for the YMCA to pay the back taxes, and Mr. Davidson responded that it would raise too many questions for other groups. Mr. Hayward asked why this proposed bill would not apply to individuals as well as groups, and Senator Salisbury asked if "affirmative representation" meant the same as "good faith." Mr. Davidson responded that the term is really "legalese" for "led someone to believe" but that it needs to be there in order

to provide more universal representation. Mr. Farrar said there are going to be many problems and that they felt this would take care of all of them.

Senator Frey suggested that language was going to be a real problem, and Mr. Farrar replied that they were just trying to get something down on paper; that it is inevitable that certain taxpayers are going to be hurt by reappraisal; that they felt this would help more people than SB 491; that it was better to include an entire class rather than just taking care of one taxpayer; and that this would provide a "window of opportunity" for other taxpayers.

Sen. Frey said that it bothered him that there are two actions on the Y case going on at the same time. They are now in Court and when that action is completed, this new action will have to be litigated. Sen. Salisbury asked if this new language would affect the issue now before the Court. Mr. Davidson said that this was an amnesty bill only and that the bill would affect only people who had lost on the merits, only those who have or will lose their appeal. When Senator Frey suggested that it might not apply to many taxpayers, Mr. Davidson said that they didn't know how many there would be but that all it did was to remove back taxes as present law provides no discretion for the Board of Tax Appeals to excuse back taxes. Sen. Frey asked if the Board of Tax Appeals orders the back taxes paid, and the response was that they did. Mr. Farrar repeated that they had no way of telling how many are going to be assessed back taxes.

Senator Frey suggested that at the next meeting they might wish to consider a statutory amendment that would delay everything until there is a court decision.

The next meeting will be Friday, February 26, at 11:00 a.m. in room 519-S. Meeting adjourned.

ASSESSMENT AND TAXATION
SUB-COMMITTEE MEETING
February 26, 1988

Present: Senator Alicia Salisbury, Chairman
Senator Bob Frey, Member
Senator Nancy Parrish, Member
Keith Farrar, Board of Tax Appeals
James Davidson, Attorney for Board of Tax Appeals
Bob O'Connor, YMCA Attorney
George Scobas, Representing YMCA
Don Hayward, Revisor's Office
Tom Severn, Research Dept.
Chris Courtwright, Research Dept.
Sue Pettet, Secretary

Senator Salisbury called the meeting to order and announced that the YMCA attorney, Mr. Bob O'Connor was present to offer suggested language for S.B. 491.

Mr. O'Connor stated that he had been in contact with the Board of Tax Appeals that morning and felt that the YMCA and the Board of Tax Appeals were in agreement concerning language. (See Att. 1) The attachment has language from the Board and also contains a YMCA modification language from himself.

Mr. O'Connor also stated that he would like to see an expedited effective date, which would be effective upon publication in the state register. In addition to that, he would like to see an implementation clause added.

Language to be added would read, "Relief may be granted under this section by a court in any pending proceeding, by remand to the Board of Tax Appeals or upon the filing of an initial application pursuant to K.S.A. 1987 Supp. 79-213." (See Attachment 2)

In response to a question, Senator Salisbury was assured that both parties were in agreement concerning suggested language.

Senator Parrish made a motion to amend S.B. 491 using the YMCA's modification, (Att. 1) and add to that the effective date to be in the state register. Also, the implementating language be added.

Senator Frey seconded with the suggestion that the words "any pending tax appeal" replace the words on attachment 2, "any pending proceeding".

Motion carried.

Senator Parrish moved that the sub-committee recommend sub. S.B. 491 to be passed favorably by the Assessment & Taxation committee.

Senator Frey seconded.

Meeting adjourned.