Approved February 11, 1992

Minutes of the House Committee on Taxation. The meeting was called to order by Joan Wagnon, Chairperson, at 9:10 a.m. on Tuesday, JANUARY 28, 1992 in room 519-S of the Capitol.

All members were present except:

Rep. J. C. Long, excused.

Committee staff present:

Tom Severn & Chris Courtwright, Legislative Research; Bill Edds and Don Hayward, Revisors; Linda Frey, Committee Secretary; Douglas E. Johnston, Committee Assistant.

Conferees appearing before the committee:

Jim Weisgerber, Dept. of Revenue
Rep. Jess Harder
Ron Smith, Kansas Bar Association

Chairman Wagnon called the committee to order at 9:10 a.m. She distributed to the committee a Washington Post article titled "Shopping by Catalogue To Find Some Money" (Attachment 1).

Ron Smith, representing the Ks. Bar Assoc., requested the introduction of two bills regarding the interest charged by the Dept. of Revenue on delinquencies and assessments, and the time a taxpayer has to request an appeal and assessment. (Attachment 2)

Rep. Snowbarger moved and Rep. Vancrum seconded the introduction of both bills requested by Smith. The motion carried.

Hearings were opened on HB 2621, Payment of Interest on Delinquent Taxes and HB 2242, Kansas Estate Tax Act.

Jim Weisgerber, Dept. of Revenue, briefed the committee on death taxes. He said the department supports the concepts of an Estate Tax contained in HB 2242 (Attachment 3).

Rep. Keith Roe asked about the effect of proposed legislation on family farms and other property that have been passed on from generation to generation. Weisgerber said special valuation techniques could be used to soften the blow of changing the inheritance tax to an estate tax.

Rep. Shore asked about who paid inheritance taxes on inherited properties in Kansas. Weisgerber said many non-Kansas residents had to pay taxes on property in Kansas, but the burden would be greater on those people living in Kansas that inherit Kansas properties.

Unless specifically noted, the individual remarks recorded herein have not been transcribed verbatim. Individual remarks as reported herein have not been submitted to the individuals appearing before the committee for editing or corrections.

MINUTES OF THE House COMMITTEE ON Taxation, room 519-S, Statehouse, at 9:10 a.m. on Tuesday, January 28, 1992.

In reply to a question, Weisgerber said the bill was revenue neutral. He also said HB 2242 was designed to bring the state in greater conformity with federal law and to make the law more comprehensible for tax practitioners as well as the general public.

In response to a question regarding inheritance of life insurance proceeds, Weisgerber said current law exempts life insurance from the inheritance tax. HB 2242 would eliminate the exemption thereby making life insurance proceeds payable to an inheritor subject to the estate tax because the bill conforms to federal law.

Information was requested on the fiscal effect of excluding life insurance from determination of taxable estate.

Rep. Vancrum said smaller estates would receive significant advantage in HB 2242. Weisgerber estimated that if Kansas goes to an estate tax with a filing threshold of $50,000, it would eliminate approximately half of the estate filings.

Information was requested comparing Kansas system of inheritance taxation with the surrounding states, and regarding the percentages of state inheritance tax revenues that come from different classes.

Rep. Harder testified in favor of HB 2621 (Attachments 4 and 5). He said HB 2621 would give the Secretary of Revenue leeway to abate the interest rate charged on delinquencies and assessments. Rep. Harder reiterated that HB 2621 would not effect the rate of interest on due inheritance taxes.

Rep. Snowbarger voiced his concern that giving the Secretary of Revenue the power to abate the interest due on delinquent taxes could lead to greatly increased litigation.

Austin Nothern, representing the Kansas Bar Assoc., spoke in favor of HB 2621 and HB 2242. He reviewed the technical aspects of HB 2242 listing several specific technical changes favored by the Ks. Bar Assoc.:

1) Incorporating references to valuation tables and rules and regulations of the Internal Revenue Service to get some degree of conformity.
2) Adding a provision for special use valuation.
3) Redefining and working with the apportionment of property in other states.

Nothern offered to work with the committee on technical changes

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MINUTES OF THE House COMMITTEE ON Taxation, room 519-S, Statehouse, at 9:10 a.m. on Tuesday, January 28, 1992.

needed to HB 2242 if the committee was interested in considering a change in this area of taxation.

The Chair noted that she would appoint a subcommittee to work HB 2242 if there was sufficient interest in converting to an estate type tax. Committee members were encouraged to express their opinions. She said HB 2621 would be brought up for discussion soon.

The Chair closed the public hearing on HB 2621. The committee was adjourned at 10:30 a.m. The next meeting will be January 29.

Unless specifically noted, the individual remarks recorded herein have not been transcribed verbatim. Individual remarks as reported herein have not been submitted to the individuals appearing before the committee for editing or corrections.

GUEST LIST

COMMITTEE: House Taxation DATE: 1/28/92

NAME (PLEASE PRINT)	ADDRESS	COMPANY/ORGANIZATION
Alan Steppat	Topeka	Pete McGill & Associates
George Goebel	Topeka	AARP-SLC-CCTF
Jim McBride	Topeka	[illegible]
HAROLD C. PITTS	TOPEKA	AARP-CCTF
Jim Young	Topeka	AARP-CCTF
Alice Hamilton [illegible]	Topeka	KDOA
[illegible]	Emporia	Intern
WALT DARLING	TOPEKA	KS DIVISION OF BUDGET
Jeffrey R. Chenhall	Lawrence	Legislative Intern
Russell A. Frey	Topeka	Ks. Vet. Med Assoc.
Ron Smith	"	Ks Bar Assoc
John H. Wachter	Topeka	Kansas Bar Assoc.
AUSTIN NOTHERN	TOPEKA	KANS BAR ASSOC
John Parks	"	KDOR
Steven Stotts	"	"

THE WASHINGTON POST NATIONAL WEEKLY EDITION JANUARY 6-12, 1992

House Taxation
Attachment 1
01-28-92

REVENUE

Shopping by Catalogue To Find Some Money

States are fighting the mail order industry over sales taxes

By Edward Walsh
Washington Post Staff Writer

LINCOLNSHIRE, Ill.—The telephone lines and fax machines are busy inside the sprawling two-story, brick and glass headquarters of the Quill Corp. here. On an average day, about 10,000 orders pour into the nerve center of the nation's largest mail-order supplier of office supplies and furniture in this pleasant suburb northwest of Chicago.

One typical order, received recently from a customer in New Hyde Park, N.Y., was for several small items totaling $38.16. The same items, purchased from a store in New Hyde Park, would have cost an extra $3.24 because of state and local sales taxes.

But Quill does not collect sales taxes in New York or any state except the three in which it has facilities, and that has helped to put it at the center of a high-stakes confrontation between the direct-marketing industry and state governments that is to be fought out this month before the Supreme Court.

At issue is whether to overturn a 1967 Supreme Court ruling that retailers can be compelled to collect sales or use taxes only in states where they have a physical presence. Based on that decision, Quill, a family-owned company with $300 million in annual sales nationwide and in Canada, charges sales tax only to customers who live in Illinois, California or Georgia, where the firm has distribution centers.

The legal showdown, prompted by a unanimous decision last May by the North Dakota Supreme Court that Quill could be compelled to collect that state's 5 percent use tax on sales in North Dakota, comes at a critical time for revenue-starved state and local governments. Reeling from the effects of a stubbornly persistent recession, state governments are often finding that budget cuts and tax increases imposed last year will not be enough to prevent a revenue shortfall.

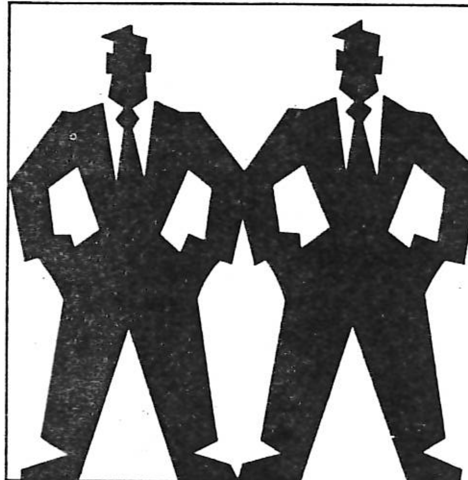
In Illinois, for example, where Quill collects the 6.25 percent state sales tax but out-of-state direct-marketing giants such as L.L. Bean do not, a bipartisan state fiscal commission has projected a $300 million gap between revenue and spending by the end of fiscal 1992 next June 30.

"Every dollar is precious," says Democratic North Dakota Gov. George A. Sinner, a leader in the effort to reverse the 1967 ruling.

The stakes are no less high for the direct-marketing industry, which has grown enormously in the 24 years since the Supreme Court ruling in *National Bellas Hess v. Illinois Department of Revenue,* which struck down taxes on mail-order goods on the grounds that they interfere with the free flow of interstate commerce. Thirty-four states have laws similar to the North Dakota use tax, which applies the state sales tax to out-of-state companies.

If the 1967 ruling is reversed, forcing firms such as Quill to collect state and local sales taxes of widely varying amounts throughout the country, "catalog production would become unbearably expensive and confusing," officials of the Direct Marketing Association warned in a Supreme Court brief.

Arnold Miller, Quill's treasurer, estimates that the company would have to pay at least $500,000 in administrative expenses to collect sales taxes nationally and return the revenue to state and local governments. Quill could handle the task, he says, but for smaller direct-marketing firms, "it's going to kill them. They won't be able to keep up with the expenses."


BY TIM CLARK FOR THE WASHINGTON POST

Each side in the dispute accuses the other of gross exaggeration. According to the National Governors' Association (NGA), the states are losing as much as $3 billion in tax revenue because of the *Bellas Hess* decision.

"We think they are exaggerating tremendously," retorts Christine Armentante, a spokeswoman for the Direct Marketing Association in New York who cited a 1988 industry-sponsored study estimating the lost tax revenue at $696 million.

"We say about $3 billion, and they say about $1 billion," says James L. Martin, the NGA's legislative counsel. "Okay, $1 billion is fine with me," he adds, ticking off a list of programs such as community health centers and education block grants for which total federal aid to the states is less than $1 billion a year.

Similarly, Martin scoffs at the industry's prediction of administrative chaos and crushing economic burdens if mail order firms are forced to collect taxes from customers nationally. The same increasingly sophisticated computer and telecommunications equipment that has helped the direct-marketing industry to expand vastly since 1967 "is readily available to collect all these taxes," he says. "It's no big deal."

In the decision that set the dispute in motion, the North Dakota Supreme Court declared that the 1967 *Bellas Hess* ruling was "an obsolescent precedent."

"The economic, social and commercial landscape upon which *Bellas Hess* was premised no longer exists, save perhaps in the fertile imaginations of attorneys representing mail-order interests," the court said. "In the quarter century which has passed in the interim, 'mail order' has grown from a relatively inconsequential market niche into a Goliath now more accurately delineated as 'direct marketing.' The burgeoning technological advances of the 1970s and 1980s have created revolutionary communications abilities and marketing methods which were undreamed of in 1967."

According to the court ruling, Quill has annual sales of almost $1 million in North Dakota, making it the state's sixth-largest seller of office supplies. Accusing Quill of attempting "to carve out a tax-free, mail-order niche and gain an unfair competitive advantage over local retailers," the North Dakota judges ruled that the firm has a "significant economic presence within the state" and said a 1990s' standard of "economic presence" should replace the 1967 "physical presence" standard in determining whether a company must collect sales or use taxes.

Dan Bucks, executive director of the Multistate Tax Commission in Washington, says the Quill case is a key test of whether the states' taxing powers will be enhanced to reflect realities of the modern "remote-control economy," of which the direct-marketing industry is a major part. "Unless state tax concepts are updated to reflect the modern economy, state revenues will continue to lag," he says.

In addition to their need for revenue, state officials argue that direct-marketing firms such as Quill undercut local merchants, who have no choice but to add sales tax to what they charge for items. "We're struggling to keep Main Street retailers in business, and they're left with a 6 to 7 percent disadvantage," Sinner says. "It's patently unfair."

But Miller and other executives of direct-marketing firms reject the fairness argument, noting that their sales include shipping charges that can exceed the amount of a state's sales tax and give them no price advantage. They also argue that, unlike local merchants, they do not benefit from state services.

"We don't use the state courts, we don't use their police and fire protection, they're not performing any services for us," Miller says. To North Dakota's argument that Quill mails more than 24 tons of material into the state that must be disposed of, Miller said, "If you accept the trash argument, you have the same problem with newspapers and other items. There's no end to it."

The Supreme Court has scheduled oral arguments in the case Jan. 22. A decision near the end of the court's term next summer could be issued just before the start of a new fiscal year for most states. But a court ruling reaffirming the 1967 decision will not end the struggle.

If Quill prevails, Miller says, the firm plans to sue North Dakota to recover its estimated $600,000 in legal fees in connection with the case. "We feel our due-process rights have been violated," he says.

At NGA headquarters in Washington, Martin says overturning the North Dakota decision would merely shift the battleground to Congress, where state governments would seek legislation empowering them to force out-of-state, direct-marketing firms to collect sales taxes.

"We will never give up until we win," Martin says. ■

STATE OF KANSAS

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Department of Revenue
Office of the Secretary

January 10, 1992

Ron Smith
General Counsel
Kansas Bar Association

Re: 1992 Kansas Tax Legislation

Dear Ron:

I wanted to confirm our conversation regarding the Department of Revenue's continued support for the Kansas Inheritance Tax reform proposal which was introduced last year in the Senate Assessment and Taxation Committee. This proposal was the subject of a summer interim study but unfortunately because of budget constraints received very little, if any, scrutiny. Jim Weisgerber of my staff has prepared a synopsis of the proposal which was presented to the Interim Committee via the Legislative research Department. If you or any of the KBA Legislative Committee would like a copy of this outline, please let me know.

I would also like to ask that the KBA introduce two pieces of legislation. The first has to do with the interest charged by the Department on delinquencies and assessments. It is my opinion, interest assessed by the Department should follow the same guidelines as used by the IRS. I have enclosed a copy of the Arizona statute which accomplishes this objective.

The second legislative proposal has to do with the time a taxpayer has to request an appeal to the Director from an assessment. I have received input from several corporate taxpayers who would like the appeal period extended from the present 30 days to a minimum of 60 days with a preference of 90 days. Ninety days may be a bit long but either time frame would be acceptable to the Department.

House Taxation
Attachment 2
01-28-92

Several years ago the KBA sponsored legislation aimed at offers in compromise. This subject does not seem to have much momentum and I suggest this initiative be put on the back burner for the time being.

If I can be of any assistance, please let me know. I am looking forward to working with you and hope we can accomplish these modest legislative goals.

Sincerely,

Mark Beshears
Secretary of Revenue

cc: Mark Burghart
Alisa Dotson
Jim Weisgerber

with whom the child is living if child support is also being enforced pursuant to an assignment or application filed under 42 United States Code § 654(6).[1]

Added by Laws 1985, Ch. 366, § 13, eff. July 1, 1986. Amended by Laws 1987, Ch. 134, § 16, eff. Aug. 18, 1987, retroactively effective to July 1, 1986.

[1] 42 U.S.C.A. § 654, par. (6).

Historical and Statutory Notes

For retroactive effective date provision of Laws 1987, Ch. 134, see Historical Note following § 42-111.

Former § 42-133 was repealed by Laws 1968, Ch. 149, § 8. See Historical and Statutory Notes following § 42-135.01.

Cross References

Political parties trust fund, voluntary contribution from income tax refund, see § 43-612.
Refunds,
  Earned credit for property taxes, residents sixty-five years of age or older, see § 43-1072.
  Excess withholding, see § 43-432.

Library References

Taxation ⇐1097, 1333.
WESTLAW Topic No. 371.
C.J.S. Licenses § 57.
C.J.S. Taxation § 1109.
Words and Phrases (Perm.Ed.)

§ 42-134. Interest

A. If it is provided by law that interest applies as determined pursuant to this section, the department shall apply the rate of interest, compounded annually, established by the director in the same manner and at the same times as prescribed by § 6621 of the United States internal revenue code, as defined in § 43-104. On January 1 of each year the department shall add any interest outstanding as of that date to the principal amount of the tax. For purposes of this section the amount added to the principal is thereafter considered a part of the principal amount of the tax and accrues interest pursuant to this section.

B. If the tax, whether determined by the department or the taxpayer, or any portion of the tax is not paid on or before the date prescribed for its payment the department shall collect, as a part of the tax, interest on the unpaid amount at the rate determined pursuant to this section from the date prescribed for its payment until it is paid.

C. Interest on the amount assessed as a deficiency shall be assessed and paid at the same time as the deficiency at the rate determined pursuant to this section from the date prescribed for the payment of the tax to the date the deficiency is assessed. If any portion of the deficiency is paid before the date it is assessed, interest shall accrue on that portion only to the date paid.

D. If the time for filing a return is extended, the department shall collect, as part of such tax, interest on any unpaid balance at the rate determined pursuant to this section from the date on which the payment should have been made if no extension had been granted until the date the tax is paid.

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E. Except in the case of a jeopardy assessment, collection of which has been stayed by the posting of a bond, if a deficiency or any interest or additional amounts imposed in connection with a deficiency under this section or § 42-136 or any addition to tax in case of delinquency provided for in § 42-136 is not paid in full within ten days from the date of notice and demand from the department, the department shall collect as a part of the tax interest on the unpaid amount at the rate determined pursuant to this section from the date of the notice and demand until it is paid.

F. If an original return filed with the department shows that the taxpayer is entitled to a refund, interest is not allowed on the amount to be refunded if the refund is paid within sixty days of the last day for filing the return or sixty days from the filing of the return, whichever is later. If the department does not pay the amount of the refund due within sixty days after the date established in this subsection, the department shall pay the interest on the amount at the rate prescribed in this section from the sixty-first day to the issued date of the refund warrant. The department's annual budget shall separately state the amount necessary to satisfy the requirements of this subsection.

G. In the case of an amended return, claim for refund or refund determined through audit, interest shall be allowed and paid, with respect to any tax, from the date prescribed for the payment of that tax to the issue date of the refund warrant, but in the case of an original return of tax which is filed after the last date prescribed for filing the return and paying such tax, determined with regard to extensions, no interest may be allowed or paid for any day before the date on which the return is filed or the tax paid, whichever is later. A payment not made incident to a bona fide and orderly discharge of an actual liability or one reasonably assumed to be imposed by law is not an overpayment for the purposes of this subsection and interest is not payable thereon.

H. If a credit or refund of any part of an overpayment would be barred under § 42-115, subsection A, except for the provisions of § 42-113, subsection B, paragraph 4, no interest shall be allowed or paid with respect to such part of the overpayment for any period beginning after the expiration of the period of limitation provided in § 42-115, subsection A for filing a claim for credit or refund of such part of the overpayment and ending at the expiration of six months after the date on which the claim was filed or, if no claim was filed and the overpayment was found by the department, ending at the time the appeal was filed with the board.

I. In any judgment of any court rendered for any overpayment, interest shall be allowed at the rate determined pursuant to this section on the amount of the overpayment from the date of the payment or collection thereof to the date of allowance of credit on account of such judgment or to a date determined by the department preceding the date of the refund warrant by not more than thirty days.

Added by Laws 1985, Ch. 366, § 13, eff. July 1, 1986. Amended by Laws 1987, Ch. 134, § 17, eff. Aug. 18, 1987, retroactively effective to July 1, 1986; Laws 1989, Ch. 132, § 8, eff. May 3, 1989.

Source:

Laws 1933, Ch. 39,
Laws 1933, 1st S.S.,
Laws 1937, Ch. 27,
Laws 1939, Ch. 10,
Code 1939, §§ 40-
Laws 1949, Ch. 16,
Laws 1953, Ch. 25,
Code 1939, Supp.1
Laws 1954, Ch. 65,
Code 1939, Supp.1
73-2286.
Laws 1955, 2nd S.
A.R.S. former §§
42-1524, 42-15
43-186, 43-621
to 43-806.
Laws 1968, Ch. 8
Laws 1971, Ch.
Laws 1971, Ch. 1
Laws 1973, Ch. 7
Laws 1973, Ch. 1
Laws 1974, Ch. 1
Laws 1978, Ch.
Laws 1979, Ch.

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(relating to floor stock refunds), 6413(d) (relating to taxes under the Federal Unemployment Tax Act), 6416 (relating to certain taxes on sales and services), 6419 (relating to the excise tax on wagering), 6420 (relating to payments in the case of gasoline used on the farm for farming purposes), and 6421 (relating to payments in the case of gasoline used for certain nonhighway purposes or by local transit systems).

Last amendment.—Sec. 6612(c) appears above as amended by Sec. 208(a)(7) of Public Law 627, June 29, 1956, effective (Sec. 208 of P.L. 627) June 29, 1956.

Prior amendment.—Sec. 6612(c) was previously amended by Sec. 4(f) of Public Law 466, Apr. 2, 1956. Sec. 6612(c) as so amended is in P-H Cumulative Changes.

SUBCHAPTER C—DETERMINATION OF INTEREST RATE; COMPOUNDING OF INTEREST

Sec. 6621. Determination of rate of interest.
Sec. 6622. Interest compounded daily.

SEC. 6621. DETERMINATION OF RATE OF INTEREST.

(a) General Rule.—

(1) Overpayment rate.—The overpayment rate established under this section shall be the sum of—

(A) the short-term Federal rate determined under subsection (b), plus
(B) 2 percentage points.

(2) Underpayment rate.—The underpayment rate established under this section shall be the sum of—

(A) the short-term Federal rate determined under subsection (b), plus
(B) 3 percentage points.

Addition.—Sec. 6621(a) was added by Sec. 1511(a) of Public Law 99-514, Oct. 22, 1986, effective (Sec. 1511(d) of P.L. 99-514) for determining interest for periods after Dec. 31, 1986.

Former (a) [Repealed]

Repealer.—Sec. 6621(a) was repealed by Sec. 1511(a) of Public Law 99-514, Oct. 22, 1986, effective (Sec. 1511(d) of P.L. 99-514) for determining interest for periods after Dec. 31, 1986. Former Sec. 6621(a) prior to this repealer read as follows:

(a) In General.—The annual rate established under this section shall be such adjusted rate as is established by the Secretary under subsection (b).

Prior amendment.—Former Sec. 6621(a) was previously amended by Sec. 4(b) of Public Law 96-167, Dec. 29, 1979, effective (Sec. 4(c)(2) of P.L. 96-167) Dec. 29, 1979. Former Sec. 6621(a) as so amended is in P-H Cumulative Changes.

Addition.—Former Sec. 6621(a) was added by Sec. 7(a)(1) of Public Law 93-625, Jan. 3, 1975, effective (Sec. 7(e) of P.L. 93-625) July 1, 1975, and for amounts outstanding on such date or arising thereafter.

(b) Short-Term Federal Rate.—For purposes of this section—

(1) General rule.—The Secretary shall determine the short-term Federal rate for the first month in each calendar quarter.

(2) Period during which rate applies.—

(A) In general.—Except as provided in subparagraph (B), the Federal short-term rate determined under paragraph (1) for any month shall apply during the first calendar quarter beginning after such month.

(B) Special rule for individual estimated tax.—In determining the addition to tax under section 6654 for failure to pay estimated tax for any taxable year, the Federal short-term rate which applies during the 3rd month following such taxable year shall also apply during the first 15 days of the 4th month folloiwing such taxable year.

(3) Federal short-term rate.—The Federal short-term rate for any month shall be the Federal short-term rate determined during shuch month by the Secretary in accordance with section 1274(d). Any such rate shall be rounded to the nearest full percent (or, if a multiple of 1/2 of 1 percent, such rate shall be increased to the next highest full percent).

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Addition.—Sec. 6621(b) was added by Sec. 1511(a) of Public Law 99-514, Oct. 22, 1986, effective (Sec. 1511(d) of P.L. 99-514) for determining interest for periods after Dec. 31, 1986.

(b) [Repealed]

Repealer.—Sec. 6621(b) was repealed by Sec. 1511(a) of Public Law 99-514, Oct. 22, 1986, effective (Sec. 1511(d) of P.L. 99-514) for determining interest for periods after Dec. 31, 1986. Former Sec. 6621(b) prior to this repealer read as follows:

(b) **Adjustment of Interest Rate.—**

(1) **Establishment of adjusted rate.**—If the adjusted prime rate charged by banks (rounded to the nearest full percent)—

(A) during the 6-month period ending on September 30 of any calendar year, or

(B) during the 6-month period ending on March 31 of any calendar year,

differs from the interest rate in effect under this section on either such date, respectively, then the Secretary shall establish, within 15 days after the close of the applicable 6-month period, an adjusted rate of interest equal to such adjusted prime rate.

(2) **Effective date of adjustment.**—Any adjusted rate of interest established under paragraph (1) shall become effective —

(A) on January 1 of the succeeding year in the case of an adjustment attributable to paragraph (1)(A), and

(B) on July 1 of the same year in the case of an adjustment attributable to paragraph (1)(B).

Prior amendments.—Former Sec. 6621(b) was previously amended by the following:

Sec. 345(a) of Public Law 97-248, Sept. 3, 1982, effective (Sec. 345(b) of P.L. 97-248, as amended by Sec. 714(m) of P.L. 98-369, July 18, 1984) for adjustments taking effect on or after Jan. 1, 1983.

*Sec. 711(a), Public Law 97-34, Aug. 13, 1981, effective (Sec. 711(d)(1), P.L. 97-34) for adjustments made after Aug. 13, 1981.**

*Sec. 711(c), Public Law 97-34, Aug 13, 1981, effective (Sec. 711(d)(2), P.L. 97-34) for adjustments made for periods after 1982.**

Addition.—Former Sec. 6621(b) was added by Sec. 7(a)(1) of Public Law 93-625, Jan. 3, 1975, effective (Sec. 7(e) of P.L. 93-625) July 1, 1975, and for amounts outstanding on such date or arising thereafter.

**Former Sec. 6621(b) as so amended is in P-H Cumulative Changes.*

Former (c) [Repealed]

Repealer.—Former Sec. 6621(c) was not reenacted by Sec. 1511(a) of Public Law 99-514, Oct. 22, 1986, effective (Sec. 1511(d) of P.L. 99-514) for determining interest for periods after Dec. 31, 1986. Former Sec. 6621(c) prior to this repealer read as follows:

(c) **Definition of Prime Rate.**—For purposes of subsection (b), the term "adjusted prime rate charged by banks" means the average predominant prime rate quoted by commercial banks to large business, as determined by the Board of Governors of the Federal Reserve System.

Prior amendment.—Former Sec. 6621(c) was previously amended by Sec. 711(b) of Public Law 97-34, Aug. 13, 1981, effective (Sec. 711(d)(1) of P.L. 97-34) for adjustments made after Aug. 13, 1981. Former Sec. 6621(c) as it read before this amendment is in P-H Cumulative Changes.

Addition.—Former Sec. 6621(c) was added by Sec. 7(a)(1) of Public Law 93-625, Jan. 3, 1975, effective (Sec. 7(e) of P.L. 93-625) July 1, 1975, and for amounts outstanding on such date or arising thereafter.

(c) Interest on Substantial Underpayments Attributable to Tax Motivated Transactions.—

(1) In general.—In the case of interest payable under section 6601 with respect to any substantial underpayment attributable to tax motivated transactions, the rate of interest established under this section shall be 120 percent of the underpayment rate established under this section.

Last amendment.—Sec. 6621(c)(1) (formerly (d)(1)) appears above as redesignated and amended by Sec. 1511(c)(1) of Public Law 99-514, Oct. 22, 1986, effective (Sec. 1511(d) of P.L. 99-514) for purpose of determining interest for periods after Dec. 31, 1986. Sec. 6621(c)(1) (formerly (d)(1)) prior to this redesignation and amendment read as follows:

(d) **Interest on Substantial Underpayments Attributable to Tax Motivated Transactions.—**

(1) **In general.**—In the case of interest payable under section 6601 with respect to any substantial underpayment attributable to tax motivated transactions, the annual rate of interest established under this section shall be 120 percent of the adjusted rate established under subsection (b).

Addition.—Sec. 6621(c)(1) (formerly (d)(1)) was added by Sec. 144(a) of Public Law 98-369, July 18, 1984, effective (Sec. 144(c) of P.L. 98-369) for interest accruing after Dec. 31, 1984.

(2) Substantial underpayment attributable to tax motivated transactions.—For purposes of this subsection, the term "substantial underpayment attributable to tax motivated transactions" means any underpayment of taxes imposed by subtitle A for any taxable year which is attributable to 1 or more tax motivated transactions if the amount of the underpayment for such year so attributable exceeds $1,000.

Last amendment.—Sec. 6621(c)(2) (formerly (d)(2)) appears above as redesignated by Sec. 1511(a) of Public Law 99-514, Oct. 22, 1986, effective (Sec. 1511(d) of P.L. 99-514) for determining interest for periods after Dec. 31, 1986. Sec. 6621(c) as it read before this amendment is in P-H Cumulative Changes.

Addition.—Sec. 6621(c)(2) (formerly (d)(2)) was added by Sec. 144(a) of Public Law 98-369, July 18, 1984, effective (Sec. 144(c) of P.L. 98-369) for interest accruing after Dec. 31, 1984.

(3) Tax motivated transactions.—

(A) In general.—For purposes of this subsection, the term "tax motivated transaction" means—

(i) any valuation overstatement (within the meaning of section 6659(c)),

(ii) any loss dissallowed by reason of section 465(a) and any credit disallowed under section 46(c)(8),

(iii) any straddle (as defined in section 1092(c) without regard to subsections (d) and (e) of section 1092),

(iv) any use of an accounting method specified in regulations prescribed by the Secretary as a use which may result in a substantial distortion of income for any period, and

(v) any sham or fraudulent transaction.

Last amendment.—Sec. 6621(c)(3)(A) (formerly (d)(3)(A)) appears above as amended and redesignated by the following:

Sec. 1535(a) of Public Law 99-514, Oct. 22, 1986, effective (Sec. 1535(b) of P.L. 99-514) for interest accruing after Dec. 31, 1984 (but not on underpayments relating to final court decision before Oct. 22, 1986). This amendment added Sec. 6621(c)(3)(A)(v).

Addition.—Sec. 6621(c)(3)(A) (formerly (d)(3)(A)) was added by Sec. 144(a) of Public Law 98-369, July 18, 1984, effective (Sec. 144(c) of P.L. 98-369) for interest accruing after Dec. 31, 1984.

(B) Regulatory authority.—The Secretary may by regulations specify other types of transactions which will be treated as tax motivated for purposes of this subsection and may by regulations provide that specified transactions being treated as tax motivated will no longer be so treated. In prescribing regulations under the preceding sentence, the Secretary shall take into account—

(i) the ratio of tax benefits to cash invested,

(ii) the methods of promoting the use of this type of transaction, and

(iii) other relevant considerations.

(C) Effective date for regulations.—Any regulations prescribed under subparagraph (A)(iv) or (B) shall apply only to interest accruing after a date (specified in such regulations) which is after the date on which such regulations are prescribed.

(4) Jurisdiction of Tax Court.—In the case of any proceeding in the Tax Court for a redetermination of deficiency, the Tax Court shall also have jurisdiction to determine the portion (if any) of such deficiency which is a substantial underpayment attributable to tax motivated transactions.

Last amendment. Sec. 6621(c)(3)(B)—(c)(4) (formerly (d)(3)(B)—(d)(4)) appears above as redesignated by Sec. 1511(c)(1)(A) of Public Law 99-514, Oct. 22, 1986, effective (Sec. 1511(d) of P.L. 99-514) for determining interest for periods after Dec. 31, 1986. Sec. 6621(c)(3)(B)—(c)(4) (formerly (d)(3)(B)—(d)(4)) as it read before this amendment is in P-H Cumulative Changes.

Addition.—Sec. 6621(c)(3)(B)—(c)(4) (formerly (d)(3)(B)—(d)(4)) was added by Sec. 144(a) of Public Law 98-369, July 18, 1984, effective (Sec. 144(c) of P.L. 98-369) for interest accruing after Dec. 31, 1984.

SEC. 6622. INTEREST COMPOUNDED DAILY.

(a) General Rule.—In computing the amount of any interest required to be paid under this title or sections 1961(c)(1) or 2411 of title 28, United States Code, by the Secretary or by the taxpayer, or any other amount determined by reference to such amount of interest, such interest and such amount shall be compounded daily.

(b) Exception for Penalty for Failure to File Estimated Tax.—Subsection (a) shall not apply for purposes of computing the amount of any addition to tax under section 6654 or 6655.

Addition.—Sec. 6622 was added by Sec. 344(a) of Public Law 97-248, Sept. 3, 1982, effective (Sec. 344(c) of P.L. 97-248) for interest accruing after Dec. 31, 1982.

[The page following this is (I.R.C.) 26,079]

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Kansas Department of Revenue
Testimony in Support of House Bill 2242
Before the Senate Assessment and Taxation Committee
Tuesday, January 28, 1992

Introduction

House Bill 2242 relates death taxes in Kansas. The proposals contained in the bill appear in the same form in Senate Bill 188.

The change proposed in House Bill 2242 was the subject of an interim report submitted by Legislative Research. The Department of Revenue is familiar with, and agrees with, the content of that report. Today's testimony summarizes some of the points made in the report (which the Committee is encouraged to review in its entirety), and adds the Department's support of the proposal.

Types of Death Taxes [See Legislative Research Report, Page 1.]

There are two basic types of death tax systems - inheritance tax and estate tax. An understanding of two major points is essential to an understanding of the similarities and differences in these systems.

> First, an inheritance tax system and an estate tax system are similar in that they include essentially the same assets in the gross estate (the starting point in determining what is subject to tax), and value these assets in essentially the same manner.
>
> Second, the principal differences between an inheritance tax system and an estate tax system are (1) the concept by which the tax is imposed, and (2) the treatment accorded a situation in which the estate contains property with a tax situs in another jurisdiction. In other words, while the same assets are subject to tax, the manner in which the tax is computed is different.

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In order to compare and contrast the inheritance tax and the estate tax it is necessary to understand the concepts under which the taxes are imposed.

An inheritance tax is imposed on the right of a beneficiary to receive property, and is levied on the value received by each beneficiary. The individual heirs and beneficiaries are responsible for the payment of tax, unless a will or trust specifically provides otherwise. Inheritance taxes may generally be structured to achieve a particular tax incidence policy in that different classes of beneficiaries may be subjected to selective tax rates and exemptions.

An estate tax is imposed on a decedent's right to transfer property, and is levied on the net value of the decedent's estate. The estate is responsible for the payment of tax. The estate tax lacks the flexibility of an inheritance tax in that selective tax rates and exemptions may not be applied to particular classes of beneficiaries, but has the advantage of ease of computation and administration.

In addition, it is necessary to consider the treatment accorded a situation in which the estate contains property with a tax situs in another jurisdiction.

Under an inheritance tax concept, assets which are beyond the jurisdiction of the taxing authority are set apart before the tax is imposed. Most deductions for debts and expenses, federal tax, and claims for exemption which are personal to the distributee, are prorated to reflect the percentage that property within the taxing jurisdiction bears to the total of all property in the estate.

Under an estate tax concept, the tax liability of the estate is determined before the tax situs of property comprising the estate is considered. After the tax liability has been determined the total liability is then prorated to reflect the percentage that property within the taxing jurisdiction bears to the total of all property in the estate.

There is also a secondary type of death tax which is frequently used in connection with either an inheritance tax or an estate tax. It is called a "pick-up" tax.

> The pick-up tax taxes the estate in an amount equal to the federal credit for state death taxes. Under federal estate tax law, each estate is allowed a 100% credit against its federal estate tax liability for a certain level of state death taxes based on the value of the decedent's estate. Under a pick-up tax system, the estate tax liability is equal to the federal credit allowed. Absent a state death tax, liability in an amount at least equal to the state death tax credit would be owed to the federal government. Stated differently, a state pick-up tax system does not increase total federal and state death tax liability, but merely causes a portion of the death tax liability to be paid to the state instead of to the federal government.

<u>How Tax Is Computed</u> [See Legislative Research Report, Page 2 & 3.]

Inheritance tax is computed in the following manner: First, a "gross estate" value is computed by adding the value of basically the same assets of the decedent's estate that comprise the gross estate for federal estate tax purposes. Second, an "adjusted gross estate" value is computed by deducting the value of certain assets that are beyond the jurisdiction of Kansas to tax (i.e., property in other states) and other exempt assets (i.e., certain life insurance proceeds, exempt government securities, unpaid mortgage indebtedness and losses during administration). Third, a "taxable" or "distributable" estate value is computed by deducting debts and expenses of the estate and federal estate taxes paid. Fourth, the value of the distributable estate is set over as "shares" to the "distributees" (heirs, beneficiaries, joint tenants, etc.). Fifth, the "class" of each distributee is determined by the nature of their relationship to the decedent. Sixth, the amount of the "personal deduction" allowed each distributee (as determined by their class and by the amount, if any, of non-Kansas property they receive) is subtracted from their share. Seventh, the tax on the net share passing to each distributee is determined by applying the rate applicable to their class and the amount they receive. Eighth, the total liability of the estate is determined by adding the liabilities of all distributees. (Note: each distributee is personally responsible for the tax on their share.)

Estate tax is computed in the following manner: First, a "gross estate" value is computed by adding the value of basically the same assets of the decedent's estate that comprise the gross estate for federal estate tax purposes. Second, a "taxable estate" value is determined by deducting the value of the marital deduction and charitable deduction, and the amount of any debts and expenses of the estate and federal estate taxes paid. Third, the tax is determined by applying the rate applicable for the size of the estate. Fourth, a "uniform credit" (which is a credit against tax which has the effect of exempting a threshold amount from tax) is subtracted from the computed tax liability. Fifth, if the estate includes property which is beyond the jurisdiction of the state, the tax is prorated between the jurisdictions.

Similarities And Differences In The "Mechanics" Of Inheritance Tax and Estate Tax [See Legislative Research Report, Page 4 - 14.]

Many aspects of an inheritance tax and an estate tax are quite similar. For example, valuation methods are often the same. In addition, the nature of property to be included in the gross estate, and the extent to which it is to be included, are often nearly identical under both systems. Most differences between an inheritance tax and an estate tax are found in the process by which the gross estate is modified and adjusted to arrive at the amount subject to tax, and in the manner in which the tax itself is computed.

For a discussion of the elements common to both inheritance tax and estate tax, the elements which are unique to each, and of how a pick-up tax is imposed, please see the Legislative Research Report, at Page 4 - 14.

Effects Of A Change From An Inheritance Tax To An Estate Tax [See Legislative Research Report, Page 14 - 16.]

A conceptual change from an inheritance tax to an estate tax would produce several effects. Among them would be: (1) a shift in the burden of death taxes, and the party responsible for paying the tax; (2) a conceptual change in the timing of the tax computation; (3) increased practitioner understanding, and; (4) a reduction in the administrative burden borne by both the estate and the Department of Revenue. These effects are discussed briefly below:

(1) Under an inheritance tax system, where the tax liability of each distributee is separately determined on the basis of the relationship between the distributee and the decedent, it is easy to "pick your victim" by assigning higher personal deductions and lower rates to one class (generally those closely related to the decedent), and lower personal deductions and higher rates to another (generally remote heirs). Under an estate tax system, where the tax liability of the estate is determined by reference to the estate in toto, it is impossible to "pick the victim." As a result, since remote heirs (as a group) generally pay more tax than immediate heirs (as a group), going from an inheritance tax to an estate tax will generally shift some of the tax burden from remote heirs to immediate heirs. [Note: This effect is not as apparent for estates which pay the pick-up tax, and can be ameliorated in many estates by effective estate planning.]

Under an inheritance tax system, each distributee is responsible for paying the tax attributable to their share. The "personal representative" (fiduciary) of the estate serves as the collection agent, and can either deduct the tax due from the distributee's share prior to distribution or collect the tax directly from the distributee. Under an estate tax system, the estate is responsible for paying the tax. Tax is paid from the "probate estate" (i.e. property for which devolution of title is not automatically determined) unless special "allocation" rules provide that tax is to be paid from the property generating the tax and give the personal representative (executor) authority to pursue the takers of the assets (such as joint tenants, designated beneficiaries, beneficiaries of trusts, etc.) to make collection.

(2) Under an inheritance tax system, assets and deductions are categorized as being within or without the taxing jurisdiction prior to the computation of tax. Under an estate tax system, all assets are included in the tax base, and the full amount of any deductions is allowed, before the tax estate is computed and then prorated, if necessary. By allocating assets and deductions prior to the imposition of tax, an inheritance tax applies a lower marginal tax rate. By prorating the total tax liability determined by including all assets and allowing all deductions in full, the estate tax applies a higher marginal tax rate. [This process is similar to that currently used in determining Kansas income tax liability.]

(3) Most practitioners consider the inheritance tax to be complicated and confusing. Many provisions are unique, complex wills and trusts must often be interpreted and applied, and a great many computations and prorations are required. Most practitioners consider the estate tax to be simple and straight forward. Most have a working knowledge of the federal estate tax and appreciate concepts, and even language, which is familiar from federal law.

(4) Under an inheritance tax system the relationships of the heirs to the decedent and the size of the shares they receive must be examined in detail in order to determine whether tax is due. This process often requires great effort just to determine no tax is due, and/or to obtain proof no tax is due (to clear title, for example.) Under an estate tax system there is a set threshold which defines the size of estate which will be subject to tax. As a result, the need to examine the estate in detail to determine whether tax will be due (to clear title, for example) is eliminated.

History [See Legislative Research Report, Page 17.]

The Kansas Inheritance Tax was first enacted in 1909, repealed in 1913, and reenacted in 1915. Since 1915, it has undergone several revisions.

The inheritance tax was the subject of major studies conducted by the 1977 Interim Committee on Assessment and Taxation, and the 1984 Kansas Tax Review Commission. As a result of the work of the 1977 Committee, the Kansas Inheritance Tax was substantially rewritten, and legislation implementing much of the 1977 Committee's recommendation was enacted by the 1978 Kansas Legislature. After studying the current system, and alternative systems, the 1984 Commission recommended that the present inheritance tax law be retained in preference to changing to an estate tax or a pick-up tax.

Present Law. [See Legislative Research Report, Page 18.]

The Kansas inheritance tax, like all inheritance tax systems, levies a tax on the beneficiary of assets from a decedent's estate. It is regarded as an excise tax on the right to receive property resulting from the decedent's death. The Kansas inheritance tax achieves a tax incident policy in that different classes of heirs are subjected to selective rates and exemptions.

The current inheritance tax system of Kansas generates approximately 35 to 40 million dollars in annual revenues. Approximately 1,000 returns are filed each month, of which approximately 40% are taxable. Ten to 15 percent of the returns which are filed involve estates large enough to be required to file federal estate tax returns.

The tax has remained relatively unchanged since 1982 when an exemption was provided for all property left to a surviving spouse, replacing the former exemption of $250,000. For other beneficiaries varying exemptions and tax rates are applied, depending upon the the relationship of the beneficiary to the decedent. A minimum tax is imposed in the form of a pick-up tax when the same exceeds the direct inheritance tax liability. The pick-up tax is the equivalent of the federal credit for state death taxes allowed in the computation of the federal estate tax under the provisions of the Internal Revenue Code.

1 rector. The application for refund shall be filed on forms prescribed
2 by the secretary within the time allowed for refunds pursuant to
3 K.S.A. 79-1574, *and amendments thereto*. Upon being satisfied that
4 the executor, administrator or deemed executor has exercised due
5 diligence in attempting to recover the taxes attributable to the dis-
6 tributive shares of the decedent's estate which were not within such
7 executor's, administrator's or deemed executor's custody or control,
8 the director shall refund the same.
9 (5) The director shall issue a receipt acknowledging payment of
10 ~~said~~ *such* taxes whenever the taxes as shown to be due on the return
11 or any additional taxes assessed by the director have been paid by
12 an executor, administrator or deemed executor and (A) such executor
13 or administrator has requested a cash receipt in order to be sub-
14 rogated to the state's right to proceed in collecting the tax against
15 a distributee; or (B) such executor or administrator has received a
16 stay of payment from the director. Such a receipt shall be issued
17 only under circumstances described in clauses (A) or (B) of this
18 subsection (5) and shall not constitute evidence that a final deter-
19 mination of taxes pursuant to K.S.A. 79-1571, *and amendments*
20 *thereto*, has been made.
21 (e) If the taxes contemplated by this act are not paid when due,
22 interest at the rate prescribed by K.S.A. 79-2968(b), *and amendments*
23 *thereto*, shall be charged and collected commencing at the time the
24 same become payable. When the filing of the return is delayed
25 beyond nine ~~(9)~~ months after the death of the decedent and the
26 director finds that such delay was due to the inability of the executor,
27 administrator or deemed executor to determine the distributive
28 shares of an estate or the proper recipients thereof, or to litigation,
29 interest shall commence at the time the return is filed. *Whenever*
30 *in the judgment of the secretary or the secretary's designee, the*
31 *failure of any executor, administrator or deemed executor to pay*
32 *any taxes hereunder was due to reasonable causes, the secretary or*
33 *the secretary's designee may waive or reduce any interest charged*
34 *upon making a record of the reasons therefor.*
35 (f) At the election of the executor, administrator or deemed ex-
36 ecutor, the taxes imposed by this act may be determined by the
37 director. Such election shall be made by filing a return disclosing
38 all information necessary for the determination of the taxes imposed
39 by this act. Upon receipt of all necessary information, the director
40 shall determine the taxes due and owing and shall notify the executor,
41 administrator or deemed executor of the tax liability by registered
42 or certified mail. Notwithstanding any election made pursuant to
43 this section,

timely

or if the charging of interest would be inequitable for any other reason,

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STATE OF KANSAS

JESSE J. HARDER
REPRESENTATIVE, ONE HUNDRED AND THIRD DISTRICT
BOX 208
BUHLER, KANSAS 67522

TOPEKA

COMMITTEE ASSIGNMENTS
MEMBER: EDUCATION
LOCAL GOVERNMENT
TAXATION
LEGISLATIVE EDUCATIONAL
PLANNING COMMISSION

HOUSE OF
REPRESENTATIVES

HB 2621

January 28, 1992

Testimony on HB 2621
before the
House Committee on Taxation
by
Rep. Jesse Harder

Madam Chairperson, members of the committee:

Thank you for scheduling a hearing on this bill.

A need for its provisions was brought to my attention by a letter from Mr. William Chalfant, an attorney who lives in my legislative district. A copy of the letter is attached and is offered as the primary evidence in support of HB 2621.

You will note from a careful reading of Mr. Chalfant's letter that his only concern is fairness in the application of the inheritance tax law. As he says in his letter, enactment of HB 2621 will not bring relief to his client but would be of benefit to subsiquent, similar cases.

A balloon copy of HB 2621 contains an amendment suggested by Mr. Chalfant.

I'm asking for your favorable consideration of the bill's amended version.

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SB 188

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HAROLD R. BRANINE (1892-1988)

TELECOPIER 316 662-2160

February 27, 1991

Rep. Jesse Harder
State Capitol
Room 284 West
Topeka, KS 66612

Dear Jesse:

I have recently had occasion to deal with an inheritance tax problem that I think needs attention by amendment of the statute. Briefly the facts are these.

Approximately twenty years ago a Kansas landowner died, owning two quarter-sections of land in the state of Kansas, both of which were owned in joint tenancy with his wife. The couple had two children, both of whom resided in the state of Arkansas. The mother was aged, and shortly after her husband's death she deeded the land to her two children, reserving a life estate. She did this so that she would no estate in Kansas. She removed from the state of Kansas to the state of Arkansas, and remains living to the present time. About eight years ago her son, who had never been married and had no children, became afflicted with what apparently was a terminal illness. He deeded his interest in the land to his sister and brother-in-law along with himself, as joint tenants. He died within a year of the conveyance, and had no other estate of any kind either in Arkansas or elsewhere. He had retired from work in a laundry some time before his death, and was cared for in his home by his mother. He had never received any income from the land, and had no possessory interest. The state of Arkansas does not have an inheritance tax, and its estate tax applies only to estates of persons who have a sufficient amount to owe a federal estate tax. They did not understand at any time that the son's interest was subject to any kind of Kansas inheritance tax. It was not until a number of years later, namely in 1991, when it became necessary to sell land to raise money to care for the mother, who is in her upper nineties and living in a care facility, that the fact there was a Kansas inheritance tax became known to them. It was filed, and a tax of some $700 was assessed. In addition, the state assessed interest on the tax in the amount of $819.18, far more than the original tax.

On behalf of the taxpayer, we requested that the interest be abated. It was pointed out that when examination of the title revealed the problem, the family filed the tax return in good faith as promptly as was possible, though the need to do so worked a financial hardship on them. It was pointed out that the children, including the deceased son, had no possessory interest as yet. It was also pointed out that K.S.A. 79-1567 would have given a representative of the decedent's estate or a "deemed executor," the right to elect to defer payment until right of possession or to enjoy the estate occurs, if a bond is given. In this instance the tax was paid, though the right of possession has not occurred. Unfortunately, although no specific reference was made to the right to give a bond, it was presumably the position of the tax authorities that no bond had been given and that the statute had not literally been complied with. At any rate, the request that the tax be abated was denied, and it was stated that K.S.A. 79-1564(e) did not provide sufficient grounds to do so under these circumstances.

I think that it is important that fairness govern all of our laws, and that is especially true with tax laws. It seems a terrible miscarriage of justice to impose a penalty on people who live in another state, and who have no way of understanding that a tax might be owing. It is quite common for people even within our own jurisdiction to assume that when there is no right of possession, and that such will not occur until the death of another party in the future, that they have nothing upon which a tax would apply. Many are heavily influenced by the circumstances within their own state boundaries. Certainly in this case the family was astounded that there was something owed in the first instance, and could hardly believe that they owed more interest that they did tax. That seems something short of equitable, and I call it to your attention with the hope that you can address a remedy to this problem, so that other persons in the future will not have to face it.

Thank you for your attention.

Very truly yours,

W. Y. CHALFANT

WYC:pm