

Approved: Feb 22, 1995
Date

MINUTES OF THE SENATE COMMITTEE ON ASSESSMENT AND TAXATION.

The meeting was called to order by Chairperson Audrey Langworthy at 11:00 a.m. on February 23, 1995 in Room 519--S of the Capitol.

Members present: Senator Langworthy, Senator Corbin, Senator Martin, Senator Bond, Senator Clark, Senator Feleciano, Jr., Senator Hardenburger, Senator Lee, Senator Ranson, Senator Sallee and Senator Wisdom.

Committee staff present: Tom Severn, Legislative Research Department
Chris Courtwright, Legislative Research Department
Don Hayward, Revisor of Statutes
Elizabeth Carlson, Secretary to the Committee

Conferees appearing before the committee: Bob Corkins, KCCI
Mark Beshears, Sprint
Secretary John LeFaver, Department of Revenue
Senator Don Sallee

Others attending: See attached list

SB 316--BUSINESS INCOME DEFINED FOR UDITPA PURPOSES

Bob Corkins, KCCI, testified in support of the objective of **SB 316** in order to clarify the meaning of "business income" in the context of state corporate income tax liability. (Attachment 1) He said he qualified the support of KCCI because there are some improvements which can be made in the bill. The main issue is the way Kansas domiciled firms are treated versus foreign domiciled firms. The apportionment formulas are used by states to determine which states get to tax what share of the taxable income of multi-state corporations. **SB 316** deals with the disposition of corporate assets. The issue has come to a head because of a Kansas Supreme Court ruling in the case of Chief Industries which held that a firm domiciled in Nebraska did not owe Kansas tax on income from the sale of one of its subsidiaries division in Russell. The ruling means that Kansas domiciled firms will pay Kansas tax on 100% of their proceeds, plus they will pay the income tax of other states in accordance with the other states' apportionment laws. Without **SB 316** there will be a powerful motive to reject Kansas as a corporate headquarters. Other proponents can attest to the strong need for this legislation.

Mark Beshears, Sprint, said he was appearing for a coalition of Kansas companies. (Attachment 2) He said **SB 316** would eliminate an unfair income tax burden imposed on only those corporations which make the state of Kansas their commercial domicile. He spoke also of the Kansas Supreme Court decision in Chief Industries. He said the result is that Kansas taxpayers are taxed by the states in which the taxpayer conducts business operations on more than 100% of its income. This multiple taxation is inconsistent with all interstate compacts which the state of Kansas has adopted. He listed 5 positive features of **SB 316**. He proposed a balloon version of this bill which strikes the words "except" on page one, line 21 through lines 26, inserting instead the words "provided, however, that if a taxpayers' commercial domicile is in the state of Kansas, the income arising from the acquisition, management, use or gain or loss from the disposition of tangible or intangible property shall constitute business income." He asked the committee to pass **SB 316** as amended.

There were questions from the committee if this bill would impact revenue and the budget for the state. They answered it would only impact it in the future. It was asked why would any major corporation or subsidiary domicile in Kansas if this is the fact, and the answer was they would not domicile here. It was also asked if the state of Kansas would see an increase in revenue and the answer was "yes".

Secretary John LaFaver, Department of Revenue, said the Department of Revenue agrees with the intent and purpose of **SB 316**. (Attachment 3) However, the results generally favor out of state firms and works against in-state firms. In attempting to remedy the problem, this bill creates even larger ones. The approach of the bill clearly violates the Commerce Clause. The prescribed treatment should apply to all corporations. He also felt that the amendment which was offered will not meet nor succeed in a challenge to the constitutionality of the law. He also said it would be unpleasant to enforce a law which he knew was unconstitutional.

CONTINUATION SHEET

MINUTES OF THE SENATE COMMITTEE ON ASSESSMENT AND TAXATION, Room 519-S
Statehouse, at 11:00 a.m. on February 23, 1995.

The committee asked what changes would be necessary. It was stated that it should be changed to make it consistent with the multi-state law. Senator Bond said he did not understand the constitutionality problem and he hoped Secretary LaFaver could make available language that he believes would correct the uniformity problem.

Senator Langworthy announced a subcommittee would meet at 5:00 p.m. today to work on this problem with **SB 316**.

The hearing was closed on **SB 316**.

SB 194--MOTOR-FUEL TAXATION, EXEMPT SALES

Senator Sallee explained **SB 194**. He said this bill passed the legislature last year but was vetoed by the Governor. In the past 10 years, many merchants have set up businesses on tribal ground and sold numerous items without collecting sales tax. It should be only tribal members who are able to do this. However, this has become common practice for non-tribal members to buy there also. This bill would eliminate that problem.

Senator Martin asked how this is going to be enforced and Senator Sallee said it would be enforced by the Attorney General's office. He said the Kansas Supreme Court has ruled that Kansas has the right to collect these taxes. The procedure will be for the tax payer to apply for a refund from the Department of Revenue if a refund is due.

Senator Bond made a motion to pass **SB 194** favorably. The motion was seconded by Senator Corbin. The motion carried.

SB 165--REDEMPTION OF REAL PROPERTY SUBJECT TO SALE FOR DELINQUENT TAXES

There was discussion by the committee if **SB 165** should be amended to counties over 300,000 population. Senator Wisdom said he would like Wyandotte County to be included so would suggest 150,000. Staff recommended the names of the counties be amended into the bill instead of using the numbers.

Senator Bond made a motion to include the three counties of Johnson, Wyandotte and Sedgwick Counties in the bill. The motion was seconded by Senator Corbin. The motion carried with Senator Feleciano voting No.

Senator Bond made a motion to pass **SB 165** favorably as amended. The motion was seconded by Senator Wisdom. The motion carried.

SB 132--TAXATION OF THE BUSINESS OF BANKING; PROHIBITING

Jim Maag, Kansas Bankers Association, said the Department of Revenue, in Order No. 94-08, has interpreted the privilege tax into a corporate income tax. This would result in a 5% to 20% increase in tax for Kansas banks. This would create a serious tax imbalance between state and national banks. He said this is an issue similar to the issue in **SB 132**.

Senator Bond asked if the banks would be paying tax upon tax and the answer was "no". There was discussion if this should be incorporated into **SB 132** or in a separate bill. Staff said it should go into a separate bill. Mr. Maag said it deals with the same philosophical issue.

SB 88--OTTAWA COUNTY JAIL FACILITY SALES TAX AUTHORIZED

Attorney General's Opinion, No. 95-22, does not prohibit the legislature from enacting curative legislation the effect of which would retroactively ratify an election wherein the voters authorized the levying of a county wide retailers' sales tax, provided the action does not impair contractual rights nor disturb vested rights.

The committee determined from the newspaper advertisements regarding the election in Ottawa County and the way the question was being asked that it was very clear it was going to take action by the legislature to validate the election.

Senator Bond made a motion to pass **SB 88** favorably. The motion was seconded by Senator Wisdom. The motion carried.

CONTINUATION SHEET

MINUTES OF THE SENATE COMMITTEE ON ASSESSMENT AND TAXATION, Room 519-S
Statehouse, at 11:00 a.m. on February 23, 1995.

SB 90--OTTAWA COUNTY JAIL FACILITY SALES TAX AUTHORIZED

Senator Bond made a motion to report **SB 90** unfavorable. The motion was seconded by Senator Wisdom.
The motion carried.

The meeting adjourned at 12:00 noon.

The next meeting is scheduled for February 24, 1995.

SENATE ASSESSMENT AND TAXATION COMMITTEE GUEST LIST

DATE: 2-23-95

NAME	REPRESENTING
Rich McKee	KS Livestock Assoc.
Catherine Holdeman	City of Wichita
Mary E. Turkington	KS MOTOR CARRIERS ASSN
MARK A. BURGHART	
Nancy Barnes	Wyandotte County Council
Trudy Perkins	CPAK
Alan Steppert	PETE MCGILL + ASSOC.
Pat Hubbell	KS Railroad Assn.
John Peterson	Pizza Hut
MICHAEL G. SMITH	Southwestern Bell Tele. Co.
Denny Koch	S W Bell
Jim Mack	KBA
Marshall Jew	KMHA
Martha Jenkins	Sprint
Jon Lewman	KS Governmental Consulting
Gudry Racine	KDOT
Bob Corkins	KCCI

SENATE ASSESSMENT AND TAXATION COMMITTEE
GUEST LIST

DATE: 2-23-95

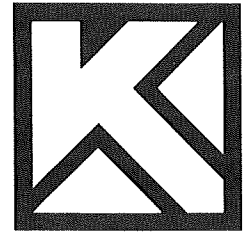
NAME	REPRESENTING
BEV BRADLEY	KS Assoc of Counties
Anne Kimmel	AARP
George Goebel	AARP
HAROLD PITTIS	AARP
David Progn	REV
Steve Spotts	Rev
MARK BISHOP	Sprint
TERRY FREDERICK	SPRINT
Shannon Peterson	KS Bar Assoc
Stew Richard	Yellow Corporation
DAVID SCHNEIDER	David Schneider
JP Small	KOCH INDUSTRIES, INC
ALAN COBB	City of Wichita
Charles Nicolay	Ks Oil Marketers Assn
Ed Schaub	Western Resources Inc
Jordan T. Hawett	CPAK
MARK CIARDULLO	KDOR
Larry Abbott	P.H.I.
Janet Stubbs	KBIA

SENATE ASSESSMENT AND TAXATION COMMITTEE GUEST LIST

DATE: Feb 23, 1995

NAME	REPRESENTING
Paul E Wold (son)	Koch Industries
David Weeks	Yellow Corporation
John Delaney	Western Resources
GAIL KLETCHER	KOCH INDUSTRIES
Gordon Hartwig	Koch Industries
JEFF SHRIVER	RUBBERMAID INC.
Bice Jurek	BOEING
JEFF RUSSELL	SPRINT
Jeri Steppat	Ks City Appraisers Assoc.
LEE DORHAM	Rep. Holman
Lena Powers	MCI
Mike Reacht	AT&T
JEFF SONNICH	KNOLSI
CJ Schwarz	Sprint
Ken Peterson	Ks Petroleum Council
Thomas Stuber	Proza Hous, Inc.
[Signature]	Pepsi Co, Inc
[Signature]	Dixie Line
Randy Clark	Ks County Appraiser

LEGISLATIVE TESTIMONY



Kansas Chamber of Commerce and Industry

835 SW Topeka Blvd. Topeka, Kansas 66612-1671 (913) 357-6321 FAX (913) 357-4732

February 23, 1995

KANSAS CHAMBER OF COMMERCE AND INDUSTRY

Testimony Before the

Senate Committee on Assessment and Taxation

by
Bob Corkins
Director of Taxation

Madam Chair and members of the Committee:

My name is Bob Corkins, director of taxation for the Kansas Chamber of Commerce and Industry. I appreciate the opportunity to testify in support of the objective of SB 316 in order to clarify the meaning of "business income" in the context of state corporate income tax liability.

The Kansas Chamber of Commerce and Industry (KCCI) is a statewide organization dedicated to the promotion of economic growth and job creation within Kansas, and to the protection and support of the private competitive enterprise system.

KCCI is comprised of more than 3,000 businesses which includes 200 local and regional chambers of commerce and trade organizations which represent over 161,000 business men and women. The organization represents both large and small employers in Kansas, with 55% of KCCI's members having less than 25 employees, and 86% having less than 100 employees. KCCI receives no government funding.

The KCCI Board of Directors establishes policies through the work of hundreds of the organization's members who make up its various committees. These policies are the guiding principles of the organization and translate into views such as those expressed here.

I qualify KCCI's support only because there are improvements to the bill which you will hear recommended by an upcoming proponent. Our Chamber is aware of these modifications and will fully support SB 316 with those changes included.

The heart of the issue concerns corporate income tax apportionment and the way Kansas domiciled firms are treated versus foreign domiciled firms. Apportionment formulas are the methods used by states to determine *which states* get to tax *what share* of the taxable income of

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even multi-state corporation. Kansas enforces its tax upon corporate income derived from business activity that may occur wholly outside Kansas, wholly within Kansas, or some combination thereof.

But SB 316 does not address all corporate income which is taxable by Kansas. Instead, the bill deals with the disposition of corporate assets -- such as the sale of a subsidiary company of a corporation -- and what, if any, of those proceeds Kansas may tax. This bill would say that for firms having a commercial domicile in Kansas, such transactions would be considered "business income" and therefore subject to Kansas tax to the extent of the share our apportionment formula computes.

This issue has come to a head recently because of a Kansas Supreme Court ruling. The court's decision in the case of Chief Industries held that a firm domiciled in Nebraska did not owe Kansas tax on income from the sale of one of its subsidiaries. Because the sale was not an ordinary transaction of Chief Industry's normal operation, it was not "business income" and thus not taxable to Chief's Kansas division in Russell.

Extending this rationale to Kansas domiciled firms does not achieve the same rosy results from the taxpayer's perspective. Chief Industries concluded that proceeds from such transactions are non-business income. Current statutes provide that all non-business income of firms having their commercial domicile here is subject to Kansas corporate income tax. Business income is apportioned by our formula while non-business income is not.

That means Kansas domiciled firms will pay Kansas tax on 100% of their proceeds, plus they will pay the income tax of other states in accordance with the other states' apportionment laws.

Without SB 316 (as we hope you will see fit to amend as we request), there will be a powerful motive to reject Kansas as a corporate headquarters. Especially in light of the growing fluidity of business associations -- mergers, downsizing, spin-off firms, etc. -- corrective action needs to be taken soon. Our subsequent proponent and the other affected Kansas firms can attest to the strong need for this legislation and the valuable contributions they have made to the Kansas economy. I'll defer to Mr. Beshears' more elaborate experience and expertise and simply ask your support on this issue. Thank you for your time and consideration.

TO: The Honorable Audrey Langworthy, Chairperson
Senate Committee on Assessment and Taxation

FR: Mark V. Beshears, Assistant Vice President
State and Local Tax, Sprint

RE: Senate Bill 316

DATE: February 23, 1995

Thank you for the opportunity to appear in support of Senate Bill 316. I am appearing as a spokesperson for a coalition of Kansas companies including Sprint, Koch Industries, Yellow Freight, National Pizza, Western Resources, Southwestern Bell, KIOGA, Kansas Chamber of Commerce and Industry, Kansas Petroleum Association, Cargill, Phillips Petroleum, Southwestern Bell, Boeing, Arco, Amoco, Texaco, Mobil Oil, Marathon Oil, ConAgra, Inc., Fourth Financial Corp. The bill eliminates an unfair income tax burden imposed only on those corporations which have chosen to make the state of Kansas their commercial domicile. The specific problem which is addressed by this bill arose during the summer of 1994 after the Kansas Supreme Court rendered its decision in Chief Industries, Inc. That case invalidated an administrative regulation promulgated by the Kansas Director of Revenue in 1979 and held that income derived from the sale of stock in a subsidiary corporation is nonbusiness income allocable in its entirety to the state of commercial domicile.

The Court's ruling results in double taxation for certain income earned by companies domiciled in Kansas. For example, under the Chief Industries decision, gain from the sale of stock would be allocated in its entirety to Kansas and would be taxed 100% by Kansas. In states where the taxpayer does business other than Kansas, the states would define such income not as nonbusiness income, but as business income a portion of which would be apportioned to and taxed by these other states. The result is that Kansas taxpayers are taxed by the states in which the taxpayer conducts business operations on more than 100% of its income. This multiple taxation of the same income is inconsistent with all of the interstate compacts which the state of Kansas has adopted.

Senate Bill 316 addresses the problem created by the Chief Industries decision by amending the definition of business income in K.S.A. 79-3271. The amended definition would allow Kansas taxpayers to apportion such income to Kansas. This was the position of the Department of Revenue regarding the treatment of such income prior to the release of the Chief

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Industries decision. The bill codifies for Kansas taxpayers the Kansas Department of Revenue regulation which had been in effect for 15 years. Kansas taxpayers have structured their affairs and made business decisions based upon this regulation. Passage of Senate Bill 316 will allow Kansas taxpayers to be treated under the rules which they believe were in effect at all times.

The positive features of Senate Bill 316 may be summarized as follows:

1. The bill eliminates the threat of multiple taxation for companies which are commercially domiciled in Kansas. Strong arguments may be advanced that such multiple taxation of the same income is, in fact, unconstitutional.
2. The proposal is consistent with and a natural extension of other incentive legislation specifically targeted to companies headquartered in Kansas which have been passed by the Kansas Legislature in recent years.
3. The bill does not provide a complete exemption for Kansas domiciled companies from taxation -- it only taxes income to the extent of the taxpayer's activity in the state of Kansas.
4. The amount of tax paid by companies domiciled in Kansas would not be less than that amount which the companies would have paid prior to the Chief Industries decision based upon the then Department policy. The state would not receive a windfall at the expense of a few corporations which are domiciled in this state.
5. Corporations domiciled in Kansas would be placed on a level playing field with taxpayers from outside the state of Kansas who do business in the state. Such companies would not be penalized for having made the decision to invest in Kansas.

We would respectfully request that the balloon version of Senate Bill 316 which is attached be recommended for passage by the Senate Committee.

Thank you for your consideration of this important legislation. I would be happy to respond to any questions you might have.

SENATE BILL No. 316

By Committee on Assessment and Taxation

2-14

9 AN ACT relating to income taxation; concerning the definition of business
10 income for uniform division of income for tax purposes act purposes;
11 amending K.S.A. 1994 Supp. 79-3271 and repealing the existing
12 section.

13
14 *Be it enacted by the Legislature of the State of Kansas:*

15 Section 1. K.S.A. 1994 Supp. 79-3271 is hereby amended to read as
16 follows: 79-3271. As used in this act, unless the context otherwise re-
17 quires: (a) "Business income" means income arising from transactions and
18 activity in the regular course of the taxpayer's trade or business and in-
19 cludes income from tangible and intangible property if the acquisition,
20 management, and disposition of the property constitute integral parts of
21 the taxpayer's regular trade or business operations, ~~except that, if a tax-~~
22 ~~payer's commercial domicile is in the state of Kansas, the income arising~~
23 ~~from the acquisition, management, gain or loss from sale, exchange or~~
24 ~~other disposition of tangible or intangible property constitutes income if~~
25 ~~the property while owned by the taxpayer was used in the taxpayer's trade~~
26 ~~or business.~~

Provided, however, that if a taxpayer's commercial domicile is in the state of Kansas, the income arising from the acquisition, management, use or gain or loss from the disposition of tangible or intangible property shall constitute business income.

27 (b) "Commercial domicile" means the principal place from which the
28 trade or business of the taxpayer is directed or managed.

29 (c) "Compensation" means wages, salaries, commissions and any
30 other form of remuneration paid to employees for personal services.

31 (d) "Financial organization" means any bank, trust company, savings
32 bank, industrial bank, land bank, safe deposit company, private banker,
33 savings and loan association, credit union, cooperative bank, investment
34 company, or any type of insurance company, but such term shall not be
35 deemed to include any business entity, other than those hereinbefore
36 enumerated, whose primary business activity is making consumer loans
37 or purchasing retail installment contracts from one or more sellers.

38 (e) "Nonbusiness income" means all income other than business in-
39 come.

40 (f) "Public utility" means any business entity which owns or operates
41 for public use any plant, equipment, property, franchise, or license for
42 the transmission of communications, transportation of goods or persons,
43 or the production, storage, transmission, sale, delivery, or furnishing of

2-3

STATE OF KANSAS

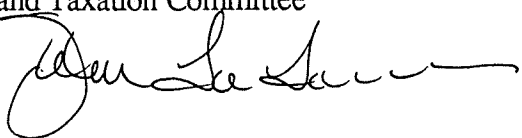
John D. LaFaver
Secretary of Revenue
Robert B. Docking State Office Building
915 S.W. Harrison St.
Topeka, Kansas 66612-1588



(913) 296-3041
FAX (913) 296-7928

Department of Revenue

TO: Senator Audrey Langworthy, Chairperson
Senate Assessment and Taxation Committee

FROM: John D. LaFaver 

DATE: February 23, 1995

SUBJECT: SB 316

The Department is in accord with the intent and purpose of SB316: to correct the unfortunate result of a recent Kansas Supreme Court case, *Chief Industries*. The effect of that case creates an "all or nothing" rule for allocating or apportioning certain income of interstate firms to Kansas. The result generally favors out of state firms which may allocate primarily capital gains income away from taxation in Kansas. It works against in-state firms which would allocate all of this income to Kansas but would remain taxable on this same income in other states. Accordingly, firms domiciled in Kansas would be subject to double taxation. This unfortunate result is due to the Court requiring Kansas to allocate income of interstate firms operating in Kansas by a methods used in few other states. Since the treatment is not uniform, other states will tax the same income Kansas is taxing under *Chief*. Clearly, this should be corrected.

Unfortunately this bill, in attempting to remedy the problem, creates even larger ones. The remedy proposed in this legislation would apportion the income from in-state firms (those domiciled in Kansas) one way and the income from out of state firms another way. These two methods will serve to impose different taxes on the same transaction depending on the domicile of a firm. This approach clearly violates the Commerce Clause.

I am sure there are alternatives to resolving this issue in a uniform, non-discriminatory manner. Whatever way is chosen, the prescribed treatment should apply to all corporations.

The Department is prepared to work with the Committee and industry to fashion a true solution -- one that passes constitutional muster, that taxes all firms uniformly, and that minimizes adverse fiscal impacts on all parties including the State.

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