

Approved: March 6, 1996
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 22, 1996 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: John LaFaver, Secretary, Department of Revenue
Larry Clark, Kansas County Appraisers Association
Mark Beck, Director, Property Valuation Division

Others attending: See attached list

SB 448--TAXATION OF FINANCIAL INSTITUTIONS

Senator Langworthy listed the bills which will be discussed today. She then called upon Senator Bond, who chaired the subcommittee, to explain the amendments to **SB 448**. (Attachment 1)

Senator Bond said the philosophy of the subcommittee, which was unanimous, was that they were concerned about the issue of fairness, the issue of double taxation when there is a consolidation or merger, and an issue of escaping tax liability when there is a consolidation or merger. The Secretary of the Department of Revenue and the Kansas Banking Association were heavily involved in the debate and the Kansas Bankers Association did not agree with the language which appears on the last page of the balloon. This is a new section 6 and this language was drafted by the Revisor. Senator Bond suggested the committee read through this portion of the bill. Senator Bond also called attention to page 2, lines 21 through 29, which has changed the definition of business income. This was language suggested by the Department of Revenue.

Staff walked through the balloon for the committee explaining the amendments which have been made to **SB 448**.

Senator Langworthy asked Secretary LaFaver to explain (e) of the balloon. He said this is to clarify that those branches in Kansas will be taxed, they don't escape even if the home financial institution is in another state, nor will Kansas tax an operation in another state.

In the change on the definition of "business income", page 2, lines 21 through line 28 were struck, and inserted after the word "that" was inserted the words "all income to the extent that it" and continuing on the rest of the paragraph. Secretary LaFaver explained the reason for the insertion of this language is due to the change in the banking laws with branch banks being located in another state. Business income may be treated as apportionable.

Senator Ranson had several questions concerning business income being apportionable. She asked if this is the same language as was used in the *Chief* case. Secretary LaFaver said this language tends to avoid that unpleasantness. He said he did not think the Kansas Banking Association had any objection to this language. Senator Ranson then asked if this section was necessary. Secretary LaFaver said he thought there needed to be something which states what is meant by "Business income."

Senator Ranson then asked if this definition had any intent or does it in any way apply to the apportionment of the income of the corporations which were dealt with in the *Chief* case. Secretary LaFaver said this language has no bearing on the *Chief* issue. Senator Ranson then asked if he and his legal staff could assure the committee that they will not be trying to apply this definition in any way to the normal business corporations whether they are domiciled in Kansas or out of the state.

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Statehouse, at 11:00 a.m. on February 22, 1996.

Senator Bond asked the Revisor to respond to this question. Mr. Hayward said the two laws are mutually exclusive. Senator Ranson then asked staff if they thought this language was necessary and would it change the intent of the bill if this definition of business income was omitted. Staff said "no". Mr. Hayward added that his understanding of federal law is that banks cannot receive any income that is not business income and there is still the question of apportionment which he thought the Department was trying to answer by this language.

Senator Ranson asked that the minutes reflect the answer of Secretary LaFaver and the revisor that the definition of business income in **SB 448** would be applicable only for purposes of the financial institution privilege tax and would not affect the determination of business income for purposes of the corporate income tax.

Discussion was began on new Section 6 of the amendment to **SB 448**. There were questions regarding merger of banks and financial institutions. Mr. Hayward, Revisor, said if a bank ceased to do business it would not ask for the privilege to do business the next year. It would be the merged bank who would ask for the privilege to do banking in Kansas. Senator Bond gave an example: if Bank B is a \$100 million bank and in 1995 it grew to \$150 million, in 1996 the bank which grew would be taxed in relation to their income for the privilege of doing banking in Kansas. If bank B, in 1995, purchased bank A, a \$50 million bank, and by the reason of that purchase became a \$150 million bank, in 1996, the bank would be taxed based on the \$150 million worth of business income. Senator Bond said this is what this new language states. The subcommittee believes that to do less would permit part of that business income to escape taxation. The same privilege tax treatment is given to merged or consolidated banks in the event of a loss.

Senator Bond said the subcommittee on **SB 448** tried to be fair and not have a tax increase, but they also did not want any bank to escape the tax. The activity with the mergers and consolidation of banks has increased rapidly over the past three years.

There were questions on what the Department of Revenue has been doing in the past. Secretary LaFaver said the Department was looking at each case on an individual basis. Senator Lee said this puts a definite policy in place and states how the mergers and consolidations will be handled. If the law is spelled out, the banks will know what is expected.

Senator Martin made a motion to accept the amendments to **SB 448**. The motion was seconded by Senator Bond. The motion passed.

Senator Bond made a motion to pass **SB 448** favorably as amended. The motion was seconded by Senator Martin. The motion passed.

SB 430--QUALIFICATIONS OF COUNTY APPRAISERS

Senator Langworthy said there has been a great deal of discussion how necessary it is to have qualified appraisers in the field. The appraisers are saying it is very difficult under current law for them to be qualified and a request has been made from some changes.

Senator Langworthy called upon Larry Clark, representing the Kansas County Appraisers Association.

Mr. Clark said quite simply they support the Real Estate Appraisal Board in their efforts to insure that Kansas has good, competent, qualified single appraisers in Kansas. However, the County Appraisers are mass appraisers and requiring mass appraisers to have property licenses is going in the wrong direction. This is especially true when the County Appraisers have the ability to encourage, not only current appraisers, but also their staff to achieve better quality and improve their performance in mass appraisal with these designations.

Senator Langworthy asked Mr. Clark to explain how this bill was different from the bill which was proposed during the 1995 Legislative Session. Mr. Clark said toward the end of the Session, the Real Estate Appraisal Board changed the requirements for securing a license. Prior to that time, the Board accepted as credit, mass appraisal experience. The requirements were changed so that only 500 hours of the 2,000 hours required could be in mass appraisal for the general license. In response to that, the Kansas County Appraisers Association asked that the time to get the license be extended to the next reappointment cycle. Mr. Clark said the appraisers are appointed on a four year cycle. After discussion with the Executive Director of the Board, it became apparent that certain courses, which are needed by mass appraisers, will not be accepted for experience credit. Mr. Clark said they reviewed their needs and **SB 430** was proposed for county appraisers to do mass appraisals. The license does not guarantee that. He said, in the smaller counties where the budget is limited, the appraisers need to be encouraged to take appraisal courses in mass appraisal.

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MINUTES OF THE SENATE COMMITTEE ON ASSESSMENT AND TAXATION, Room 519-S
Statehouse, at 11:00 a.m. on February 22, 1996.

Senator Martin said he had asked Mr. Haynes, Executive Director of the Real Estate Board to attend this meeting, but he could not make it today. At a previous meeting with Chairman Langworthy, Mr. Clark, Mr. Haynes, Senator Martin and Mr. Beck, Mr. Haynes outlined ways in which county appraisers could fill the requirements.

Mr. Clark said Mr. Haynes did outline that appraisers could fill out forms that they do not do now and do appraisals that they do not do now.

Senator Martin then asked if the Board can look at mass appraisals. Mr. Clark said mass appraisals are in the standards and the Board is required to uphold the standards. However, he said, that is the reason the County Appraisers were so disappointed when they reduced the recognition of mass appraisals.

Senator Clark asked Mr. Clark if there were not three different ways to be licensed. Mr. Clark said there are actually five ways. Senator Clark then asked if these five ways cover all the ways necessary to become a mass appraiser. Mr. Clark replied "No". The general license under the Real Estate Appraisal Board does not provide the training to become a mass appraiser, it is directed at single appraisers. Mr. Clark said, as of now, the Board has said they will not accept a certain mass appraisal course which is the core of what mass appraisers do. He also said that his staff has taken hours and hours to fill out papers to be sent to the Board and then they are rejected. It is not as simple as what is done every day by appraisers in filling out forms. Not all of what is done by mass appraisers is recognized by the Appraisal Board.

Senator Martin said Mr. Haynes has not been directed by his Board to speak for or against this legislation.

Senator Langworthy called upon Mark Beck, Director, Property Valuation Division if he had any remarks he would like to make.

Mr. Beck said he had a comment concerning the meeting which Senator Martin mentioned. A comment was made by Mr. Haynes that with a lot of extra work nights and weekends, these county appraisers could accomplish what they needed to do. Mr. Beck said he was particularly concerned about the smaller counties. These appraisers are working full time and then are expected to do this extra work to achieve their designation.

Senator Martin made a conceptual motion to the Revisor to basically amend **SB 430** to go back to **SB 66** last year which was to just make an extension of the deadline and they would still fall under the Real Estate Appraisal Board but would be given a longer time to get their license. The amendment would give them 5 years from this day. Senator Ranson seconded the motion.

Senator Bond said he thought there was a problem in the rural counties. The Kansas County Appraisers have come to the Legislature in **SB 430** with an alternative way to get their members trained by a very simple process. He said he thought it was wrong to just extend the time limit.

Senator Martin said if a complaint was to be registered, it now goes to the Real Estate Appraisal Board. If this bill is passed, the complaint would go to the Director of the Property Valuation Division, and it might be difficult for him. The second point he made was that the County Appraisers would be treated differently than other appraisers working for banks, etc.

Senator Lee said she has 10 rural counties in her district and she would oppose this amendment.

The vote was taken on the amendment of Senator Martin's. The Chairman was undecided upon the vote by voice and asked for a show of hands. The motion to amend failed in a 5 to 5 vote.

Senator Bond made a motion to amend the bill on page 1, lines 32-33, to make it effective when published in the statute book. The motion was seconded by Senator Lee. The motion passed.

Senator Bond made a motion to pass **SB 430** favorably as amended. The motion was seconded by Senator Lee. The motion passed.

The meeting was adjourned at 12:10 p.m.

The next meeting was not scheduled at this time. The committee will meet during the week of March 4th.

SENATE ASSESSMENT AND TAXATION COMMITTEE GUEST LIST

DATE: Feb 22, 1996

NAME	REPRESENTING
Bill Jarrell	BOEING
Kathy Duffin	KBA
Darren DeVinney	INTER-SEN. LAWRENCE
TIM KENNEDY	KS TAXPAYERS NETWORK
JOHN LAFAYER	KDOR
Randy Clark	Ko County Officials
MARK HIXON	Shawnee County
DAVE HOLTHAUS	Western Resources
John Peterson	Ban 1c TV
Smalley	KBA
John Duffin	Coffman, Fej + Auther
Alan Steppat	PETER MCCOILL + ASSOCIATES
JASON PISENPOPER	BRAD SMOOT
Anne Spiess	KS. Assoc of Counties

SENATE BILL No. 448

By Committee on Assessment and Taxation

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9 AN ACT concerning taxation; relating to the apportionment and alloca-
10 tion of income of financial institutions; amending K.S.A. 79-1107 and
11 repealing the existing section.
12

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

14 New Section 1. (a) Except as otherwise specifically provided, a fi-
15 nancial institution whose business activity is taxable both within and with-
16 out this state shall allocate and apportion its net income as provided in
17 this act. All items of nonbusiness income, income which is not includable
18 in the apportionable income tax base, shall be allocated pursuant to the
19 provisions of K.S.A. 79-3274 through 79-3278 and amendments thereto.
20 A financial institution organized under the laws of a foreign country, the
21 commonwealth of Puerto Rico, or a territory or possession of the United
22 States whose effectively connected income, as defined under the federal
23 internal revenue code, is taxable both within this state and within another
24 state, other than the state in which it is organized, shall allocate and
25 apportion its net income as provided in this act and its apportionment
26 factors shall include the part of its property, payroll and sales that is
27 related to its apportionable income.

receipts

28 (b) All business income, income which is includable in the appor-
29 tionable income tax base, shall be apportioned to this state by multiplying
30 such income by the apportionment percentage. The apportionment per-
31 centage is determined by adding the taxpayer's receipts factor, as de-
32 scribed in section 3 of this act, property factor, as described in section 4
33 of this act, and payroll factor, as described in section 5 of this act, together
34 and dividing the sum by three. If one of the factors is missing, the two
35 remaining factors are added and the sum is divided by two. If two of the
36 factors are missing, the remaining factor is the apportionment percentage.
37 A factor is missing if both its numerator and denominator are zero, but
38 it is not missing merely because its numerator is zero.

39 (c) Each factor shall be computed according to the method of ac-
40 counting, cash or accrual basis, used by the taxpayer for the taxable year.

41 (d) If the allocation and apportionment provisions of this act do not
fairly represent the extent of the taxpayer's business activity in this state,
the taxpayer may petition for or the secretary of revenue may require, in

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1 respect to all or any part of the taxpayer's business activity, if reasonable:

- 2 (1) Separate accounting;
- 3 (2) the exclusion of any one or more of the factors,
- 4 (3) the inclusion of one or more additional factors which will fairly
- 5 represent the taxpayer's business activity in this state; or
- 6 (4) the employment of any other method to effectuate an equitable
- 7 allocation and apportionment of the taxpayer's income.

8 New Sec. 2. As used in sections 1 through 5, unless the context oth-

9 erwise requires:
10 (a) "Billing address" means the location indicated in the books and
11 records of the taxpayer on the first day of the taxable year, or on such
12 later date in the taxable year when the customer relationship began, as
13 the address where any notice, statement or bill relating to a customer's
14 account is mailed.

15 (b) "Borrower or credit card holder located in this state" means:
16 (1) A borrower, other than a credit card holder, that is engaged in a
17 trade or business which maintains its commercial domicile in this state;
18 or
19 (2) a borrower that is not engaged in a trade or business or a credit
20 card holder whose billing address is in this state.

21 (c) "Business income" means income that is operationally related to
22 the taxpayer's trade or business. Income is operationally related if it arose
23 from activity or property that served an operational function. Income is
24 not operationally related if it is derived from an unrelated business activity
25 which constitutes a discrete business enterprise. Income that a taxpayer
26 demonstrates with clear and cogent evidence is not operationally related
27 is classified as nonbusiness income. It is the legislative intent to treat as
28 apportionable business income all income that may be treated as appor-
29 tionable business income under the constitution of the United States.

30 (d) "Commercial domicile" means:
31 (1) The headquarters of the trade or business, that is, the place from
32 which the trade or business is principally managed and directed; or
33 (2) if a taxpayer is organized under the laws of a foreign country, or
34 of the commonwealth of Puerto Rico, or any territory or possession of
35 the United State, such taxpayer's commercial domicile shall be deemed
36 for the purposes of this act to be the state of the United State or the
37 District of Columbia from which such taxpayer's trade or business in the
38 United States is principally managed and directed. It shall be presumed,
39 subject to rebuttal, that the location from which the taxpayer's trade or
40 business is principally managed and directed is the state of the United
41 States or the District of Columbia to which the greatest number of em-
ployees are regularly commuted or out of which they are working, irre-
spective of where the services of such employees are performed, as of

(e) In the event a combined report is utilized to determine the Kansas income attributable to a unitary group of financial institutions, the financial institutions in the combined group shall include only those institutions which have a branch or office in Kansas.

all income to the extent that it

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other state if such loan has a preponderance of substantive contact to a regular place of business there.

New Sec. 5. (a) *General.* The payroll factor is a fraction, the numerator of which is the total amount paid in this state during the taxable year by the taxpayer for compensation and the denominator of which is the total compensation paid for both within and without this state during the taxable year. The payroll factor shall include only that compensation which is included in the computation of the apportionable income tax base for the taxable year.

(b) *Compensation relating to nonbusiness income and independent contractors.* The compensation of any employee for services or activities which are connected with the production of nonbusiness income, income which is not includable in the apportionable income base, and payments made to any independent contractor or any other person not properly classifiable as an employee shall be excluded from both the numerator and denominator of the factor.

(c) *When compensation paid in this state.* Compensation is paid in this state if any one of the following tests, applied consecutively, is met:

(1) The employee's services are performed entirely within this state;

(2) the employee's services are performed both within and without the state, but the service performed without the state is incidental to the employee's service within the state. The term "incidental" means any service which is temporary or transitory in nature, or which is rendered in connection with an isolated transaction;

(3) if the employee's services are performed both within and without this state, the employee's compensation will be attributed to this state:

(A) If the employee's principal base of operations is within this state;

(B) if there is no principal base of operations in any state in which some part of the services are performed, but the place from which the services are directed or controlled is in this state; or

(C) if the principal base of operations and the place from which the services are directed or controlled are not in any state in which some part of the service is performed but the employee's residence is in this state.

New Sec. 6. *Computation of tax when business ceases.* When a privilege taxpayer ceases to do business within the state, the tax for the last taxable year in which the taxpayer does business shall be measured by the income for the next preceding taxable year plus the income for the last taxable year in which it does business. If necessary to fully report such income the taxpayer shall file an amended return and pay any tax due on or before the 15th day of the fourth month following the close of the taxable year in which business ceased. This section shall apply to all taxable years beginning on or after December 31, 1994.

The net income of any financial institution earned during the taxable year in which it is merged, consolidated or otherwise combined with another financial institution shall be attributed to the surviving or resulting financial institution in the computation of its privilege tax imposed for the year next succeeding the year of such merger, consolidation or other combination. The provisions of this section shall be applicable to all privilege tax years commencing after December 31, 1995.

1 the last day of the taxable year.

2 (e) "Compensation" means wages, salaries, commissions and any
3 other form of remuneration paid to employees for personal services that
4 are included in such employee's gross income under the federal internal
5 revenue code. In the case of employees not subject to the federal internal
6 revenue code, such as those employed in foreign countries, the deter-
7 mination of whether such payments would constitute gross income to
8 such employees under the federal internal revenue code shall be made
9 as though such employees were subject to the federal internal revenue
10 code.

11 (f) "Credit card" means credit, travel or entertainment card.

12 (g) "Credit card issuer's reimbursement fee" means the fee a taxpayer
13 receives from a merchant's bank because one of the persons to whom the
14 taxpayer has issued a credit card has charged merchandise or services to
15 the credit card.

16 (h) "Employee" means, with respect to a particular taxpayer, any in-
17 dividual who, under the usual common-law rules applicable in determin-
18 ing the employer-employee relationship, has the status of an employee of
19 that taxpayer.

20 (i) "Financial institution" means: a national banking association, state
21 bank, trust company or savings and loan association, federally chartered savings bank,

22 (j) "Gross rents" means the actual sum of money or other consider-
23 ation payable for the use or possession of property.

24 (1) "Gross rents" shall include, but not be limited to:

25 (A) Any amount payable for the use or possession of real property or
26 tangible property whether designated as a fixed sum of money or as a
27 percentage of receipts, profits or otherwise;

28 (B) any amount payable as additional rent or in lieu of rent, such as
29 interest, taxes, insurance, repairs or any other amount required to be paid
30 by the terms of a lease or other arrangement; or

31 (C) a proportionate part of the cost of any improvement to real prop-
32 erty made by or on behalf of the taxpayer which reverts to the owner or
33 lessor upon termination of a lease or other arrangement. The amount to
34 be included in gross rents is the amount of amortization or depreciation
35 allowed in computing the taxable income base for the taxable year, except
36 that, where a building is erected on leased land by or on behalf of the
37 taxpayer, the value of the land is determined by multiplying the gross rent
38 by eight and the value of the building is determined in the same manner
39 as if owned by the taxpayer.

40 (2) The following are not included in the term "gross rents":

41 (A) Reasonable amounts payable as separate charges for water and
42 electric service furnished by the lessor;

43 (B) reasonable amounts payable as service charges for janitorial ser- v-

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