Approved: January 15, 1997
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 January 14, 1997, in Room 519--S of the Capitol.

Members present: Senator Langworthy, Chairman, Senator Corbin, Vice-Chairman, Senator Bond, Senator Goodwin, Senator Hardenburger, Senator Harris, Senator Karr, Senator Lee, Senator Praeger, and Senator Steineger

Others attending: See attached list

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

Conferees appearing before the committee: Senator Tim Emert
Don Schnacke, Kansas Independent Oil & Gas Association

Senator Langworthy welcomed the committee for the 1997 legislative session. She noted the committee would meet on January 15 and 16 for briefings and hearings on **SB 6** and **SB 7**, both introduced as a result of interim studies.

Senator Tim Emert requested the introduction of a bill allowing a property tax exemption for industrial training centers located on community college campuses.

Senator Bond moved to introduce the bill, seconded by Senator Hardenburger. Motion carried.

Don Schnacke requested the introduction of two bills. The first bill would allow income tax credit for plugging orphan wells. (Attachment 1)

Senator Hardenburger moved to introduce the bill, seconded by Senator Karr. Motion carried.

The second bill requested for introduction by Mr. Schnacke regarded tax reduction incentives to protect marginal oil wells. (Attachment 2)

Senator Corbin moved to introduce the bill, seconded by Senator Bond. Motion carried.

Senator Langworthy called on Chris Courtright, Legislative Research, to review the report by the interim Special Committee on Property Taxation (Attachment 3) and the report of the Task Force on Uniformity and Equality of Property Tax Appraisals (Attachment 4).

Senator Corbin moved to introduce legislation recommended by the Task Force, seconded by Senator Lee. Motion carried.

The meeting was adjourned at 11:55 a.m.

The next meeting is scheduled for January 15, 1997.

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.

SENATE ASSESSMENT & TAXATION COMMITTEE
GUEST LIST

DATE: January 14, 1997

NAME	REPRESENTING
Grant Denny	Sen. Goodwin's Office
Kelly Kultala	City of Overland Park
Robin Lehman	Olathe USD 233
Pat Lehman	Olathe USD 233
Joleene M. Isabell	Girl Scout Councils of Ks
Sarah Davis	Girl Scout Council
JASON PITSENBERGER	BRAD SMOOT
John Peterson	Raytheon Aircraft
Bernie Koch	Wichita Area Chamber
Jim Yonally	Jo. Co. Comm. Coll.
Tom Bruno	Allen & Assoc.
Ashley Sherard	Overland Park Chamber of Commerce
Harriet Lange	Ks Assn Broadcasters
DAVE HOLTHAUS	Western Resources
Bob Corkins	KCCI
Don Schnacke	KIOGA
Bill Fance	BOEING
Shirley Sicilian	KDOR

KIOGA

KANSAS INDEPENDENT OIL & GAS ASSOCIATION

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Introduction of Income Tax Credit for Plugging Orphan Wells

SB 566 (1996 Session) was introduced to stimulate the plugging of orphan wells throughout Kansas.

SB 566 was drafted by Arden Ensley and Bill Eads of the Revisor's staff. A hearing was held and Chairman Langworthy indicated that the state policy had not yet been established concerning the plugging of orphan oil wells and asked that the bill be deferred until the 1997 session.

Late in the 1996 session, the legislative policy for plugging orphan wells was established and funds were appropriated. The State of Kansas has embarked on a long-range effort to plug wells and authorized $1.6 million to undertake this effort (H. Subs. for SB 755).

Chairman Langworthy will recall that this subject was presented to the Special Interim Committee this summer.

In order to stimulate more plugging of orphan wells, we recommend the reintroduction of SB 566 and that this effort be seriously considered during this session.

Donald P. Schnacke
Executive Vice President
Kansas Independent Oil & Gas Assn.

DPS:pp

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KIOGA

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Introduction of Tax Reduction Incentives to Protect Marginal Oil Wells

The State of Kansas is an active charter member of the Interstate Oil and Gas Compact Commission (IOGCC) and participates regularly. Governor Graves accepted an appointment by Oklahoma Governor Frank Keating to work on the subject of the *conservation of crude oil* as a part of a national energy policy.

The IOGCC recently released a study of the importance of marginal oil wells in the old producing states like Kansas. Marginal oil wells contribute greatly to the economy of Kansas and need to be protected.

This fall Governor Graves issued a public statement about the importance of protecting producing wells in Kansas. Following the Governor's public position on this subject, we communicated with Chairperson Langworthy indicating the best approach to protect marginal production.

Marginal oil production in Kansas is far below that recognized by the IOGCC at 10 BOD and the federal government has recognized marginal production at 15 BOD.

Crude oil production in Kansas is currently declining 7% per year and is at a 63-year low, about what it was in 1933. The best way to protect this production is to relieve it from severance and property taxes.

KSA 79-201t exempts two barrel wells and three barrel oil wells below 2,000 feet from ad valorem taxes. To assure that Kansas marginal production is relieved of property taxes, the limitation should be raised from two to three barrels; and production below 2,000 feet should be raised from three to five barrels.

KSA 79-4217 exempts two barrel oil wells from the state severance tax. To be consistent and to fully protect marginal oil production in Kansas, the exemption should be raised to five barrels. This statute does provide for exemptions above five barrels based on price fluctuations. We continue to believe that exemption approach is realistic and should not be disturbed.

Donald P. Schnacke
Executive Vice President
Kansas Independent Oil & Gas Assn.

DPS:pp

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STUDY TOPIC: Comprehensive Study of Property Tax System*

SUMMARY: The Special Committee on Property Taxation recommends a four-year extension of the property tax lid and further recommends that certain fund levy limits be abolished. The Committee recommends legislation be passed to assure the preservation of property tax exemptions for churches and governmental buildings to which cellular phone relay equipment has been attached. The Committee recommends a substantial expansion of the Homestead Property Tax Relief program, with the maximum refund entitlement increasing from $600 to $950 and the total household income eligibility ceiling increasing from $17,200 to $25,000. The Committee recommends that property tax refund interest be paid prospectively beginning with tax year 1997 to taxpayers who have had their valuations reduced through the appeals or payment-under-protest procedures. The Committee also recommends that the interest rate for delinquent property taxes be changed to the market-driven underpayment rate established for other taxes in K.S.A. 79-2968. The Committee asks the Department of Revenue to present a proposal to enhance substantially the public information efforts associated with the Homestead program. The Committee also recommends that the 1997 Legislature consider possible changes in the inheritance tax, including indexation of exemption amounts, as part of the overall tax relief discussion.

BACKGROUND

Following the deliberations by the 1996 Legislature on property taxation and school finance, the Legislative Coordinating Council (LCC) established two special Committees to study the issues indepth—the Special Committee on Property Taxation and the Special Committee on School Finance.

The Special Committee on Property Taxation was directed to conduct a comprehensive study of the state's property tax system and recommend any changes deemed appropriate with respect to a number of issues, including the property tax lid, property tax exemptions and abatements, and the property tax refund interest topic. As part of the comprehensive overview of property taxation, the Special Committee was charged with reviewing the property tax recommendations of the 1995 Governor's Tax Equity Task Force; the requirements imposed on county and district appraisers by law and by directives of the Property Valuation Division (PVD); efforts by PVD to implement changes in the use-valuation formula for agricultural land; and Shawnee County District Court Order No. 92-CV-796 regarding the property tax system.

Finally, the Special Committee was asked to review inheritance tax issues before the Legislature in recent years.

COMMITTEE ACTIVITIES

At the July meeting, staff briefed the Committee on the property tax recommendations of the 1995 Governor's Tax Equity Task Force and on the 1991 through 1995 county-by-county assessed valuation data. Legislative Post Audit reviewed Post Audit 93-39 regarding selected uniform and equal appraisal issues.

Mark Beck, Director of PVD and M. J. Willoughby, Assistant Attorney General, outlined the status of Judge Bullock's court order regarding the property tax system (Shawnee County District Court Order No. 92-CV-796). They said they had been meeting with Judge Bullock on a regular basis regarding the implementation of the plan for corrective action that is embodied in the court order. Commercial and industrial real property, especially in Sedgwick and Shawnee Counties, was identified as one of the more pressing problems at the April 1996 status meeting. The PVD Director told the Committee that any attempt to decelerate annual reappraisal could cause the sales ratio study to look worse than it does now and, therefore, have implications with respect to the court order.

Staff from PVD explained how the sales ratio study is conducted. PVD staff also presented a comprehensive report on the use valuation of agricultural land. The report listed the 1996 procedures used to estimate net income for each

* S.B. 6, S.B. 7, H.B. 2005, and H.B. 2006 accommpany the Committee's reports.

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of the land classes (grassland, dryland, and irrigated land). Agricultural land values had been frozen in 1994 and 1995. A number of changes have been implemented in 1996, including the development of the county average agricultural tax rate (which more accurately reflects each taxpayer's actual tax expenses) to replace the statewide median county agricultural tax rate. The Committee also reviewed the Kansas property tax calendar, analyzed property tax relief for the elderly in Kansas and other states, and received data on property tax delinquency.

Staff reviewed the 1995 interim proposal regarding the inheritance tax. Enacting H.B. 2150 as amended by the House Committee of the Whole—replacing the Kansas Inheritance Tax Act with the Kansas Estate Tax Act and implementing a pure "pick-up" tax—would reduce State General Fund (SGF) receipts by over $40 million per year. The original H.B. 2150 would simply have increased exemption amounts for Class A and Class B distributees within the existing inheritance tax structure and would have had a smaller fiscal note—about $13 million.

The Special Committee in August received from staff a flow chart outlining how property tax appeals are handled. Staff then reviewed the 1996 preliminary assessed valuation data and noted that the preliminary statewide growth rate of 2.4 percent was less than the 3.15 percent growth rate that had been forecast. PVD provided additional data on the use valuation of agricultural land and on the valuation of exempt property. The Committee also held public hearings on the property tax refund interest and tax lid issues.

The Department of Revenue provided a number of tables with inheritance and estate tax information, including the estimated impact of moving from the inheritance tax system to a variety of estate tax systems.

Staff told the Committee that the tax mix was now much closer to the "public policy ideal" of one-third property, one-third income, and one-third sales than it had been prior to the 1992 school finance law.

The Committee also received a memorandum on the policy implications of various plans to abolish property taxes in Kansas. One issue that would arise would involve the contract rights of persons owning property-tax backed bonds. Another issue would concern "local control." If a local cemetery board lacked property tax authority and wanted to mow the grass once a week rather than once a month, would they have to come to Topeka to request a legislative appropriation?

Staff presented data on the administrative costs of the property tax, which were estimated to be at less than 3 percent of the amount collected.

The Committee held public hearings on a use-value "recapture" proposal suggested by the city of Olathe in both August and September.

Also at the September meeting, the Committee received a report from Budget Director Gloria Timmer on the multi-year profile of the SGF. Shelby Smith, former chair of the House Assessment and Taxation Committee, advocated making changes to the school finance law such that the school district general fund property tax levy would no longer be considered a statewide levy. The Committee received a report from the Citizens for Tax Justice on the tax burden in Kansas. Paul Welcome, Johnson County Appraiser, also suggested a number of changes in property tax appraisal and local budget statutes, including a "truth in millage" concept. Proponents appeared in support of 1996 S.C.R. 1616 regarding a Kansas property tax cap and 1996 H.C.R. 5031 regarding economic development exemptions for oil and gas property.

PVD presented testimony regarding the impact of deregulation on utilities. PVD said that because of growing competition, utilities are arguing that Kansas property tax assessment practices for state-assessed properties are detrimental to the companies. PVD outlined the property tax appraisal directives currently in effect.

At the conclusion of the September meeting, the Committee asked the League of Kansas Municipalities to develop for further consideration a smorgasbord of revenue options for local units that could be utilized as alternatives to additional property taxes. The Committee also asked for a bill draft on extending the property tax lid for an additional four years, abolishing certain fund levy limits, and adding an additional tax lid exemption for criminal justice system information improvements.

In October, the Department of Revenue responded to some requests by presenting data on the fiscal notes associated with a number of different plans to expand the Homestead Property Tax Refund Program. The fiscal impact of increasing the total household income threshold from $17,200 to $25,000 was estimated at $2.4 million

.o $2.6 million. The fiscal impact of eliminating the age, dependency, or disability requirements was estimated at $2.1 million. The fiscal impact of increasing the threshold to $25,000 and simultaneously eliminating the other requirements was estimated at $4.8 million to $5.0 million.

Mr. Welcome said that in the wake of some recent court decisions, a number of issues had arisen with respect to locally-appraised telecommunications equipment on tax-exempt properties. He said that in order to prevent the imperilment of the exemption for churches and government buildings, the Legislature could have a taxable "possessory interest" created by a lease, and the commercial equipment would be placed on the personal property tax roll. Taxes would be assessed directly to the telecommunications company.

PVD presented a report on the taxation of "farm" pickups under (1) the motor vehicle tax; and (2) the personal property tax.

The Committee held a public hearing on the tax lid bill draft requested in September and discussed the tax lid issue. The Committee rejected a proposed plan that would have eliminated the tax lid altogether, eliminated certain fund levy limits, and eliminated all state aid to local units.

The Committee also rejected a plan that would have eliminated the sunset provision in the tax lid bill requested in September.

The Committee took no action on the alternative revenue sources recommended by the League of Kansas Municipalities.

Staff discussed eight different school finance simulations based on the concept of eliminating the uniform school district general fund mill rate.

Conclusions and Recommendations

The Special Committee on Property Taxation finds that extending the current property tax lid for four years and adding an exemption for criminal justice system information improvements would be the wisest course of action at this time with respect to the tax lid issue. But the Committee also recommends that certain fund levy limits, which have been suspended statutorily since 1989, be abolished altogether.

The Committee does not wish for the property tax exemption for various churches, governmental buildings, and other tax-exempt properties to be endangered because cellular phone relay equipment has been attached to the property pursuant to lease agreements. The Committee, therefore, recommends that the "possessory interest" created by the lease be deemed to be personal property and that such property be taxable directly to the owners of the equipment.

In order to provide additional property tax relief for Kansans, the Committee recommends that the Homestead Property Tax Relief program be expanded by increasing the maximum refund from $600 to $950 (which also has the effect of increasing the total household income ceiling from $17,200 to $25,000).

The Committee also recommends that the Department of Revenue present to the standing Tax Committees in 1997 a proposal to enhance substantially the public information efforts associated with the Homestead program. Such proposal should contain recommendations for any administrative and statutory changes necessary to make all Kansans aware of the program.

The Committee recommends that interest be paid on property taxes refunded to taxpayers who under certain circumstances have had their valuations reduced through the appeal or payment-under-protest procedures. The Committee recommends 1995 S.B. 41 as amended by the Senate Assessment and Taxation Committee, with the following changes:

1. Interest refund entitlements would begin starting with tax year 1997.
2. Taxpayers who appealed values in the spring would have their interest refund computed from December 20 (or, if later, the date of payment). Taxpayers protesting values in the fall would not have their interest computation begin until June 20 of the following year (or, if later, the date of final payment).
3. The interest rate for delinquent property taxes would be changed to the underpayment rate established by K.S.A. 79-2968. The Committee notes that this interest rate will always be greater than the time value of money and will discourage taxpayers from using the state and local governments "as a bank."
4. The interest rate for property tax refunds would be the interest rate for delinquent property taxes computed as described above, minus 4 percent. The Committee chooses this methodology in the belief that this interest rate should appropriately reflect the time value of money.

5. The State Board of Tax Appeals (SBOTA) would have the power to dismiss all cases in which taxpayers had not presented "good faith" estimates of their valuation. County officials still would be required to "initiate the production of evidence," but taxpayers not presenting relevant information (to establish good faith estimates) at each step of the process would be subject to having their cases dismissed by SBOTA. SBOTA also could dismiss cases when taxpayers missed a hearing at the local level without providing 48 hours' notice. Taxpayers would have to provide "substantial and compelling" reasons for missing a local hearing to prevent SBOTA from dismissing the cases.
6. SBOTA would have the power to waive interest attributable to time periods when delays had been caused by actions of the taxpayer or taxpayers' representative.

The Committee finds that a number of inequities may exist within the existing inheritance structure, and that the 1997 Legislature should consider the issue as part of the overall tax relief discussion and continue to study options based on additional information provided by the Department of Revenue. That information should include the fiscal impact of increasing and indexing for inflation the exemption thresholds for Classes A and B distributees. ■

Task Force on Uniformity and Equality of Property Tax Appraisals

Study Topic: Review the status of Shawnee County District Court Order No. 92-CV-796 and study whether the legislature has taken adequate steps to ensure that all property within each subclass is appraised and taxed on a uniform and equal basis. Analyze issues and concerns raised by Judge Bullock with respect to the court order, including the definition of fair market value, the accuracy and efficacy of the sales ratio study as a monitoring device, and the intent of language in K.S.A. 1996 Supp. 79-503a with respect to a variance of 10 percent in any single appraisal's not being demonstrative of "willful neglect" by a county or district appraiser.

Summary: The Task Force recommends that the annual reappraisal valuation cycle be retained for a number of reasons, including fairness to taxpayers and compliance with the court order. The Task Force notes with approval the recommendation of the Special Committee on Property Taxation with respect to expansion of the Homestead Property Tax Relief program.

Background

Following a meeting involving the Governor, the Attorney General, the President of the Senate, the Speaker of the House, and Judge Bullock, the Legislative Coordinating Council (LCC) appointed the Task Force to review a number of issues and concerns raised by Judge Bullock in connection with the court order embodied in the April 12, 1996, amended journal entry in *State of Kansas, ex rel., Carla J. Stovall, Attorney General v. Kansas Department of Revenue, John D. LaFaver, Secretary, Kansas Department of Revenue, and Mark S. Beck, Director, Division of Property Valuation, Kansas Department of Revenue, and the Honorable Sally Thompson, State Treasurer* (Shawnee County District Court Order 92-CV-796).

The LCC on November 20 directed that representatives of the Department of Revenue, State Board of Tax Appeals, the Kansas Association of Counties, and the Kansas County Appraisers Association join certain legislative tax committee members or their designees to comprise the Task Force. The LCC authorized the Task Force to conduct three one-day meetings prior to the start of the 1997 Session on January 13.

Committee Activities

At the initial meeting on December 9, staff provided the Task Force with flow charts on the current property-tax-appeals and payment-under-protest procedures.

PVD presented information on the way the Kansas sales-ratio study is conducted. Addressing the technical reliability of the sales-ratio study, Dr. Ronald L. Wasserstein, Washburn University, told the Task Force that he had concluded that the study "is a valid and reasonable method for monitoring appraisal uniformity, and is being conducted in Kansas in a manner consistent with industry standards and with statistical standards of good practice."

PVD and the Attorney General's office briefed the Task Force extensively on the status of the court order and on the issues and concerns raised by Judge Bullock. PVD also provided information on the number of counties in "substantial" compliance as of January 1, 1996.

At the December 17 meeting, the Attorney General's office responded to a number of questions raised by Task Force members with respect to the status of the case and what

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.he court order actually requires. The Task Force asked the Attorney General's staff and PVD to seek clarification from the court with respect to the date of compliance determination in the court order. The Attorney General filed such a motion on December 31 and scheduled a meeting with Judge Bullock to discuss the motion on January 14, 1997.

PVD provided information indicating that as of January 1, 1996, 26 counties were not in "statistical" compliance outlined in the court order for one or both of the residential and/or commercial subclasses of real property. PVD also provided a partial year-to-date report for calendar year 1996.

The Task Force discussed policy options with respect to seeking an additional evaluation of the accuracy and efficacy of the sales-ratio study as a measuring tool. The Task Force learned at its January 8 meeting that the Division of Legislative Post Audit had been directed to perform such an evaluation.

The Task Force also extensively discussed the tax implications of allowing land owners to continue to acquire use valuation tax treatment on commercially zoned parcels by planting crops. The Chairman of the State Board of Tax Appeals said that this tactic was occurring far more often than the Legislature realized.

The Task Force discussed the possibility of eliminating the "laundry list" in K.S.A. 1996 Supp. 79-503a of additional factors (besides sales, cost, and income) which need to be taken into consideration by appraisers in the determination of fair market value. The Task Force asked the representative of the Kansas County Appraisers' Association to provide the "USPAP" market value definition for consideration.

In terms of other potential amendments to K.S.A. 1996 Supp. 79-503a, the Task Force decided to take up at its final meeting the possibility of eliminating the 10 percent variance language.

The Task Force asked PVD to conduct a comparison between their budget requests over the last four years and the final legislative appropriations results.

After a discussion of taxpayer frustration with respect to the short amount of time available at the hearing officer/hearing panel level in the appeals process, the Task Force agreed to consider recommending changing certain dates within the appeals process.

Conclusions and Recommendations

The Task Force strongly recommends that Kansas retain the annual reappraisal valuation cycle for a number of reasons.

- Decelerating the reappraisal cycle would increase the number of counties not in statistical compliance as measured by the court order.
- A multi-year cyclical approach within which new property and improvements come on line at fair market value in the first year could tend to shift the property tax burden more heavily toward fast-growing counties.
- A multi-year cyclical approach also could seem unfair to rural counties where values are declining. Owners of a grocery store on Main Street in a small town—where the market value declines by $5,000 per year—could be taxed based on a valuation that is too high.
- Even if a multi-year cyclical reappraisal were somehow to be crafted to allow the grocery store described above to have its valuation go down every year but NOT ALLOW property with increasing values to be adjusted for several years at a time, the Task Force would have serious concerns about the constitutionality of such a system. How could "fair market value" mean something different for two different parcels depending solely on where the appraiser felt the valuations were relative to last year's valuations?
- Freezing values for the residential and commercial subclasses of real property without freezing values for other classes

and subclasses of property could raise serious constitutional concerns, as well.

- With the exception of the 1.5 mill levy for state building funds and the mandatory 33 mill school district general fund levy, "freezing" values would in no way guarantee lower taxes. If values are normally increasing and are not allowed to increase, county clerks would simply set higher levies based on local units' legally adopted budgets, everything else being equal.
- Assuming county clerks would be required to automatically set higher levies, motor vehicle taxes would simply increase that much faster beginning two years in the future.
- Reducing somewhat the annual growth in the tax base would have implications with respect to mandating increased spending to continue to fully fund school finance relative to the Governor's Budget and current estimates. The statewide property tax base is projected currently to grow by 3 percent per year.
- A taxpayer with a $100,000 house whose valuation is increasing by $4,000 per year may not be terribly happy under current law when he receives his valuation notice. But he is likely to be even more upset if he received a valuation notice every third year indicating an increase of $12,000.

In order to facilitate the aim of achieving uniformity and equality, the Task Force recommends that the 1997 Legislature thoroughly analyze resource issues associated with PVD's budget and the requirements of the court order.

The Task Force recommends that the standing tax committees study further the notion of replacing the definition of fair market value in K.S.A. 1996 Supp. 79-503a with the definition provided by "USPAP" standards. (The chairpersons of the standing committees agreed to hold hearings should such legislation be introduced.)

While there was no consensus on the Task Force for a specific legislative solution, the Task Force encourages the standing tax committees to study legislation designed to clarify what the statutory definition of "agricultural land" for property tax purposes should be in order to combat some of the perceived abuses described by the Chairman of the State Board of Tax Appeals.

The Task Force recommends the introduction of legislation to delete the 10 percent variance language from K.S.A. 1996 Supp. 79-503a to clear up any confusion such language may have caused. The Task Force notes that K.S. A. 79-1426 provides that a 10 percent variance shall not be considered violative of that statute, which provides for county appraisers to be removed from office and charged with a misdemeanor for willfully failing to properly appraise and list property.

The Task Force recommends the introduction of legislation to change the initial property tax appeals deadline from April 1 to "within 30 days of the mailing" of the valuation notices. The Task Force notes that this should encourage counties to mail valuation notices earlier than the current March 1 mailing deadline and could allow taxpayers more time to present their cases at the hearing panel level.

The Task Force also notes with approval the recommendation of the Special Committee on Property Taxation with respect to expanding the Homestead Property Tax Refund program by raising the total household income eligibility ceiling from $17,200 to $25,000. Kansas property tax expert Dr. Glenn W. Fisher has said that expansion of the Homestead program is the best targeted method of alleviating some of the property tax burden on certain elderly, disabled, and poor Kansans. ■