

MINUTES OF THE HOUSE COMMITTEE ON TAXATION..

The meeting was called to order by Chairperson Phill Kline at 9:00 a.m. on March 12, 1998 in Room 519-S of the Capitol.

All members were present except:

Committee staff present: Chris Courtwright, Legislative Research Department
Don Hayward, Revisor of Statutes
Ann McMorris, Committee Secretary

Conferees appearing before the committee:

Julia Francisco, Cancer program director, Kansas Health & Environment
Shirley Sicilian, Department of Revenue
Curt Wright, Taylor Oil, Inc., Wellsville
Reed Davis, Asst to Director, Division of Administration, KDOT
Joe Lieber, Kansas Cooperative Council
Tom Palace, Kansas Oil Marketers Assn.

Others attending: See attached list

Chair continued hearing on:

HB 2994 - Cigarette tax rate increase, disposition of revenues, children's health care programs fund.

Proponent:

Julia Francisco, Cancer program director, Kansas Health & Environment (Attachment 1)

Written testimony from:

Karl Peterjohn, Kansas Taxpayers Network (Attachment 2)
Del Meier, RN, Saline County Health Department (Attachment 3)

Chair closed hearing on **HB 2994**

Chair opened hearing on:

SB 418 - Taxation of motor vehicle fuels, electronic filing, tax credit

Proponents:

Shirley Sicilian, Department of Revenue (Attachment 4)
Curt Wright, Taylor Oil, Inc., Wellsville (Attachment 5)
Reed Davis, Asst to Director, Division of Administration, KDOT (Attachment 6)
Joe Lieber, Kansas Cooperative Council (Attachment 7)
Tom Palace, Kansas Oil Marketers Assn. (Attachment 8)

Closed hearing on SB 418.

Chair opened hearing on:

SB 421 - Taxation of motor vehicle fuels, incidence of tax on distributor

Proponent:

Shirley Sicilian, Department of Revenue (Attachment 9)

Closed hearing on **SB 421.**

Moved by Representative Gregory, seconded by Representative Larkin, minutes for meetings of Taxation Committee held from January 15, 1998 through February 11, 1998 be approved. Motion carried.

The next meeting is scheduled for March 16, 1998.

Adjournment.

Attachments - 9

TAXATION COMMITTEE GUEST LIST

DATE: MARCH 12, 1998

NAME	REPRESENTING
Josie Stramberg	Jo Co.
Paul Welton	Jo Co.
Michelle Miller	Johnson County
Greg Tugman	Budget
Don Schnack	KCOGA
MARK DECK	KDOT
George Eisen	Ks Taxpayers Network
Karl Petrojohn	Ks Taxpayers Network
Dawn Reid	KSWA
Bill Watts	KDOT
Ken Travis	KDOT
John P. Smith	Ks Smokeless Kids Initiative
Judy Keller	American Lung Assn/Ks.
Shirley Ann Smith	KMHA
Dave Holman	Western Resource
Wendy M. Burns	Ks Aggregate Producers' Assn.
Woodlymas	Ks Aggregate Producers' Assn.



KANSAS
DEPARTMENT OF HEALTH & ENVIRONMENT
BILL GRAVES, GOVERNOR
Gary R. Mitchell, Secretary

Testimony presented to
House Taxation Committee
March 11, 1998
by
Julia Francisco
Cancer Program Director
House Bill 2994

Chairman Kline and members of the committee, thank you for the opportunity to appear before you today in support of House Bill 2994. My name is Julia Francisco and I am Director of the Cancer Program in the Kansas Department of Health and Environment's Bureau of Disease Prevention and Health Promotion.

Although HB 2994 contains language dedicating funds for children's health and services, including prevention and cessation, Kansas Department of Health and Environment neither supports nor opposes an increase in tobacco excise tax for the sake of creating a new source of revenue. The mission of KDHE, however is to promote and protect the health of all Kansans. It is the agency's role to address issues that contribute to disease and disability in the state. There can be no mistaking that tobacco use contributes to the disease and disability of Kansans. In fact, tobacco use is the number one preventable cause of death in our nation and state. Every year more than 4,000 Kansans die from tobacco related diseases, costing our citizens more that \$200 million in direct medical costs. To my knowledge, tobacco is the only product that when used as directed can kill its user.

Kansas youth have high rates of cigarette addiction. The 1997 Kansas Communities That Care Youth Survey found that out of 10 eighth grade students (average age of 13 years), two smoked at least one cigarette in the 30 days prior to the survey, and one considers himself/herself to be a regular smoker. The number increases to more than 3 out of every 10 students by the time they are seniors in high school, with two saying they are regular cigarette smokers.

In 1992, the Centers for Disease Control and Prevention in Atlanta developed a computer software system which predicts the future cost of tobacco use based on current rates of smoking and projected trends. Smoking Attributable Morbidity and Mortality Economic Costs (SAMMEC) estimates that nearly 154,000 Kansas children currently under the age of 17 will become smokers during their lifetime, and nearly 50,000 of this group will die 12 to 21 years prematurely because of tobacco-related diseases, incurring future health care costs of \$1.8 billion (\$12,000 per individual).

Kansas Legislators are to be commended for recognizing the significant impact tobacco use is having on our youth and addressing it through such legislation as the stricter youth access bill of 1996. Other Kansas leaders taking a stand for our youth are Governor Graves through his participation in the Kansas Health Foundation's "Take It Outside" PSA campaign, and the Attorney General's litigation on behalf of Medicaid victims. Because of actions such as these, Kansas Alcoholic Beverage Commission compliance buy rates have dropped from 67% non compliance in January, 1997 to an unofficial 43% non compliance rate in February, 1998. Even with these actions being initiated in Kansas, surveys show the rate of cigarette use is increasing among our youth, indicating that more preventive actions must be undertaken.

To decrease the sale of tobacco products, and thus the initiation of tobacco use among our youngest population, HB 2994 proposes to increase the price of a pack of tobacco product by 50 cents. In states where an increase in excise tax has occurred a decline in sales to youth has followed. In December, 1997, KDHE developed scenarios of the decrease in sales that could be expected as a result of varying amounts of increase in tobacco prices. These figures predict through the use of observed data the effect of different levels of tax increases on the overall rate of sales to youth (See attached). According to these findings, a 50 cent per pack increase in Kansas would produce an estimated 21.3% decrease in youth tobacco consumption.

A study published by the Institute of Medicine, Growing Up Tobacco Free: Preventing Nicotine Addiction in Children and Youth, pricing policy is the single most important element of an overall comprehensive strategy to reduce tobacco use, and particularly to reduce tobacco use among children. Cigarette price increases impact youth cigarette purchasing patterns about three times more than they affect the purchases of adults. For every 10 percent increase in cigarette prices, studies find a 12-14 percent decrease in youth consumption, resulting in an increase in both the number of youth who quit smoking and those who never start. These studies suggest that nearly two-thirds of the decrease in smoking resulting from excise tax increases is the result of people choosing to not smoke.

If the legislature should enact into law HB 2994, it would provide funds for a children's health services fund, including cessation and prevention of tobacco use. Youth who are addicted at a very young age have characteristics unique to them when they desire to quit smoking, requiring unique programs to address their addiction. Funds created by increasing the per pack cost of cigarettes could be used for that purpose, as well as launching a multi-media public education campaign to prevent young people from starting.

States that have recently enacted tobacco tax increases have created a source of tremendous ability to attack the problem of youth tobacco. Massachusetts, Oregon, Michigan, Minnesota, Alaska, and California by increasing the price of tobacco within their states have been able to launch all out counter advertising war on the tobacco industry's wooing of new smokers to replace their dying customers. According to the U.S. Department of Health and Human Services (CDC) the tobacco industry spends \$6.03 billion every year on promotion and advertising of cigarettes--- that's more than \$16.5 million every single day. In addition, the industry spends more than \$119.1 million each year on advertising and promoting spit tobacco products. In contrast, KDHE's federally funded IMPACT program is currently funded at

approximately \$300,000 per year to educate the public about the health risks associated with tobacco use. The Kansas Department of Health and Environment would be remiss if we did not point out that the increased revenue from HB 2994 would help level the playing field for public education campaigns.

As the state health agency, the Kansas Department of Health and Environment has the responsibility to address the leading causes of death and disability in our state. Tobacco use is the leading preventable cause, and it is affecting more and more of our greatest natural resource, our youth, every hour, every day, every week, every month, and each year. Today 30 more young people will experiment with cigarette smoking in Kansas. In one year over 11,000 of those young people will have started an addiction which will eventually cause them to suffer severely from emphysema, heart attack, stroke, and lung cancer. KDHE urges each committee member to take any action that you can as a state legislator to reduce the number of our youth to suffer these consequences.

Thank you again for your time today.



KANSAS
DEPARTMENT OF HEALTH & ENVIRONMENT
BILL GRAVES, GOVERNOR
Gary R. Mitchell, Secretary

January 15, 1998

Terri Roberts JD, RN
Executive Director
Kansas State Nurses Association
700 SW Jackson, Suite 601
Topeka, KS 66603-3731

Dear Ms. Roberts:

I am writing to respond to your letter of 1/15/98 requesting 1) a calculation of the expected change in cigarette usage among Kansas adolescents and adults following changes in the Kansas excise tax on cigarettes which you submitted to us, and 2) a calculation of the expected changes in cigarette tax receipts in Kansas from the sale of cigarettes following a change in the excise tax. I asked Dr. Stephen Pickard in the Bureau for Disease Prevention and Health Promotion to prepare the information for you. Tables 1A and 1B outline the analysis of cigarette usage change for adults and adolescents respectively, and Table 2 gives the expected change in tax receipts. However, please note the following issues in interpreting the data.

Published data from the scientific literature have consistently found that an increase in the sale price for tobacco is associated with a decrease in consumption. However, the size of that decrease depends on the "elasticity" (defined as the percent change in tobacco consumption associated with a 1% change in sale price). Two-thirds of this change in consumption is expected to be due to either quitting or not starting, and the other one-third due to a decrease in the number of cigarettes used by those who continue to smoke. Many factors are expected to affect the elasticity following a tax increase including the following: size of any single tax increase, age of the smoker, cost of other tobacco products used as replacement (e.g., oral tobacco), cost of cigarettes in neighboring states, and income of the population. Published articles which have examined changes in cigarette usage following a price increase report a range of elasticity values for both adults and youth.

Because of the number of different factors which effect change in consumption following a price increase, no single value for elasticity can be assumed. The expected decrease in cigarette usage in Kansas presented in the Tables 1A and 1B are calculated using three elasticity values derived from the literature (a typical value, as well as high and low estimates). A review of the available research regarding tobacco price elasticity can be

found in the Surgeon General's report "Strategies to Control Tobacco Use in the United States: A Blueprint for Public Health Action in the 1990's". Additional references from recent analyses are listed following Table 2. The fourth column of Table 1A and Table 1B give the most likely estimate for the percent decrease in use following a tax increase, based on a typical value for elasticity for adults and adolescents. The expected change has been calculated separately for tax increases of \$0.25, \$0.50, \$0.75, and \$1.0.

TABLE 1A

Expected Change in Kansas Tobacco Usage associated with a Variable Increase in Per Pack Cigarette Tax, Adults

Tax Increase	% change in price*	Expected Elasticity‡ (E)	Expected % ↓ in use	Min % ↓ (E=-0.2)	Max % ↓ (E=-0.5)
\$0.25	14%	-0.4	5.6	2.8	7.0
\$0.50	28%	-0.4	11.2	5.6	14.0
\$0.75	42%	-0.4	16.9	8.4	21.0
\$1.00	56%	-0.4	22.4	11.2	28.0

* Assumes a price per package of 20 cigarettes=\$1.79

‡ Percent change in tobacco consumption associated with a 1% change in sale price

TABLE 1B

Expected Change in Kansas Tobacco Usage associated with a Variable Increase in Per Pack Cigarette Tax, Adolescents

Tax Increase	% change in price*	Expected Elasticity‡ (E)	Expected % ↓ in use	Min % ↓ (E=-0.4)	Max % ↓ (E=-1.4)
\$0.25	14%	-0.76	10.6	5.6	19.6
\$0.50	28%	-0.76	21.3	11.2	39.2
\$0.75	42%	-0.76	31.9	16.8	58.8
\$1.00	56%	-0.76	42.6	22.4	78.4

* Assumes a price per package of 20 cigarettes=\$1.79

‡ Percent change in tobacco consumption associated with a 1% change in sale price

Table 2 demonstrates the expected tax revenue arising from an increase in the tax on a pack of cigarettes. Although an excise tax increase of between \$0.25 to \$1.0 per pack is expected to result in increased revenue collection, the increase due to the rise in price per pack is partially offset by the expected decrease in consumption. The first row of Table 2 represents the current revenue collection at \$0.24 per pack. The minimum and maximum values for revenue collection were calculated using the minimum and maximum decreases in consumption reported in Table 1.

TABLE 2

Actual or Expected Tax Receipts on Cigarette Sales by Change in Sales Tax, Kansas ~

Change in Tax (\$/pack)	Total Tax (\$/pack)	Actual or Expected Total Revenue in \$*	Minimum Exp Revenue in \$**	Maximum Exp Revenue in \$***
0.0	0.24	53,000,000	53,000,000	53,000,000
0.25	0.49	99,000,000	96,000,000	103,000,000
0.50	0.74	140,000,000	129,000,000	150,000,000
0.75	0.99	173,000,000	153,000,000	194,000,000
1.00	1.24	199,000,000	163,000,000	233,000,000

~ Current tax collection estimates sales of 170 million packs to adults and 48 million packs to children

* Assumes Elasticity of -0.4 for adults and -0.76 for children

** Assumes Elasticity of -0.5 for adults and -1.4 for children

*** Assumes Elasticity of -0.2 for adults and -0.4 for children

References reviewed included the following:

Becker GS, Grossman M, Murphy KM. *An Empirical Analysis of Cigarette Addiction*. National Bureau of Economic Research, Working Paper No 3322. Cambridge, MA: 1992.

Centers for Disease Control and Prevention. *Cigarette Smoking Before and After an Excise Tax Increase and an Antismoking Campaign*. MMWR 45(44): 1996.

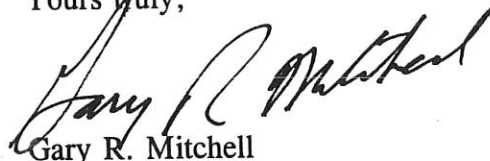
HHS. *Strategies to Control Tobacco Use in the United States: A Blueprint for Public Health Action in the 1990's*. National Institutes of Health Publication 92-3316: October, 1991.

Institute of Medicine. *Growing Up Tobacco Free: Preventing Nicotine Addiction in Children and Youth*. Lynch BS, Bonnie RJ (eds.). National Academy Press, Washington. 1994.

Keeler TE, Hut, Barnett PG, Manning WG. *Taxation, Regulation and Addiction: A Demand Function for Cigarettes Based on Time-Series Evidence*. University of California at Berkeley, Working Paper No. 91-173: 1992.

Lewit EM, Coate D. *The Potential for Using Excise Taxes to Reduce Smoking*. Journal of Health Economics. 1: 1982.

Yours truly,



Gary R. Mitchell

Secretary

Kansas Department of Health and Environment

pc: Senator Sandy Praeger
Representative Carlos Mayans
Dan Hermes, Office of the Governor
Don Brown, KDHE

1-7

KANSAS TAXPAYERS NETWORK

**P.O. Box 20050
Wichita, KS 67208
316-684-0082**

www2.southwind.net/~ktn

March 12, 1998

Testimony to House Taxation Committee on H.B. 2994

By Karl Peterjohn, Exec. Dir.

The Kansas Taxpayers Network (KTN) believes that Kansas government is already large enough. KTN created the Taxpayer Protection Pledge which many legislators signed during the 1994 and 1996 elections. This pledge is a promise not to raise taxes.

KTN urges this committee not to raise taxes and rejected HB 2994. This is not a tobacco issue, this is a tax issue. Kansans do not need or want a tax hike. Kansans need and want tax cuts.

This issue is raised as part of the on going tobacco controversy and the growing unpopularity of tobacco. However, raising the tobacco tax 50 cents a pack can have unintended and negative consequences. Here is the current level of state taxes per package in Kansas and surrounding states:

Kansas	24 cents
Nebraska	34 cents
Colorado	20 cents
Oklahoma	23 cents
Missouri	17 cents

The problems with this proposal to increase the size of state government beyond the governor's recommendation of the first \$4 billion GF budget and total spending which exceeds not only \$8 billion but \$8.5 billion are:

- 1) Revenue estimates from a 50 cent increase will fall short due to out-of-state sales east of Stateline Road, American Indian reservation sales, and tax free sales increasing at Ft. Leavenworth, Riley, and McConnell AFB. A black market could occur as smugglers purchase cigarettes from low tax states like Kentucky with only a 3 cent per pack tax and bring them into Kansas. The bigger the disparity between Kansas cigarette taxes and other jurisdictions the worse the problem gets as Canada found out after passing a large cigarette tax hike. Canada recently repealed this hike largely because it led to rampant smuggling and this law was widely ignored by smoking citizens.
- 2) A higher percentage of low income Kansans smoke. Hence, this will be a regressive tax hike on low-income Kansans who smoke.
- 3) Currently there are laws in place prohibiting teen-age smoking yet the advocates for this legislation claim that stopping illegal teen-age smoking is their goal. An unintended but likely consequence of a dramatic increase in tobacco prices is a rise in shoplifting and petty larceny.
- 4) This places Kansas businesses at a competitive disadvantage for selling this currently legal product with their out-of-state or tax exempt competitors.
- 5) Teen age smoking is a cultural problem which can better be addressed through ideas like Rep. Howell's suggestion of bundling cigarette sales which would not raise taxes. For these reasons KTN urges this committee to reject HB 2994.



Salina - Saline County Health Department
125 West Elm
Salina, Kansas 67401

WRITTEN TESTIMONY

TO THE HOUSE ASSESSMENT AND TAXATION COMMITTEE IN SUPPORT OF HB 2994

March 11, 1998

Administration
785-826-6600

Animal Shelter
785-826-6535

Clinic Services
785-826-6602

Environmental Health
785-826-6604

Home Health Agency
785-826-6606

FAX
785-826-6605

I am a Registered Nurse and Health Educator at our local city-county Health Department. A great deal of my time is spent trying to convince young people in our community not to smoke. The average age that kids in our county (and our state) start smoking is 12 years old. I think that's shameful!

Our resources can not begin to compare with the billions of dollars that the tobacco industry spends each year to convince the public that there is no need for immediate concern, and to try to convince legislators such as yourselves not to pass laws making it harder for children to start smoking. We have to work smarter, and use a variety of approaches in addition to education, to help prevent the loss of more lives. Raising the excise tax by 50 cents per pack has been shown to be extremely effective in other states, and is projected to decrease youth tobacco use by over 21%. That could have a huge impact on the health of Kansans for years to come.

I have talked to a number of students who are addicted to tobacco. They started smoking at a very young age, and purchased their own cigarettes, or paid someone older to buy them. These children have said that if cigarettes were more costly, they probably wouldn't be smoking. They have better things to spend their allowances on.

Will businesses and the tobacco industry be hurt? Put out of business? Only if they sell exclusively to children, which has been illegal for years. Retailers in our community have expressed a real desire to comply with the law, and to keep tobacco out of the hands of children. This will just be one more tool that we can all to help kids from starting, becoming addicted, and dying--as one-third of them will eventually die from tobacco-related illnesses.

Please support this very important public health effort to protect our children.

Sincerely,

Del Meier, RN, B.S.N.
Health Educator
Salina-Saline County Health Department

House Taxation
3-12-98
Attachment 3-1

Shirley K. Sicilian, Director
 Office of Policy & Research
 Kansas Department of Revenue
 915 SW Harrison St.
 Topeka, KS 66612-1588



(913) 296-3081
 FAX (913) 296-7928

Office of Policy & Research

MEMORANDUM

TO: Representative Phill Kline
 Chair, House Taxation Committee

FROM: Shirley Klenda Sicilian
 Director, Policy & Research; Kansas Department of Revenue

RE: **Senate Bill 418 - Creating a motor fuel tax credit for distributors that file returns electronically.**

DATE: March 12, 1998

Chairman Kline and members of House Taxation Committee, thank you for the opportunity to testify today regarding the Department's proposed motor fuel tax credit.

In 1995, legislation was passed which allows the director of taxation to require a distributor who receives more than 50,000 gallons of motor fuel a month to file its motor fuel tax returns electronically. This legislation is a critical part of the State's comprehensive effort to reduce the potential for motor fuel tax evasion in Kansas. In 1994, legislative post audit estimated potential revenue losses of between \$50 and \$60 million dollars. Electronic filing enables the department to track the motor fuel through each stage of the distribution chain and ensure appropriate taxes are paid. The information collected electronically is the same as what had been collected on paper. The form is identical. Electronic filing simply allows us to use that information more effectively.

While electronic filing is critical for tax collection, the department realizes it may require additional capital expenditures for some distributors who don't yet have full computer and electronic filing capability. For this reason, we've worked closely with industry and vendors in developing this tax credit proposal. The credit would be \$8,000 if the distributor files electronically on or before July 1, 1999; \$6,400 if the distributor files after July 1, 1999 and before July 1, 2000; and \$4,000 if the distributor files after July 1, 2000 and before June 30, 2001. The credit phases out over these three years to encourage early compliance. If a distributor claims the credit but ceases to file electronically within ten years of claiming the credit, the distributor must reimburse the state for the amount of the credit claimed.

Currently four motor fuel distributors are filing electronic returns. There are approximately 450 licensed distributors receiving 50,000 gallons of motor fuel each month. Should each distributor elect to file by electronic means between July 1, 1998 and June 31, 1999, the fiscal year 1999 impact would be \$3.6 million (450 x \$8,000). If all distributors elect to file during fiscal year 2000, the credit would be about \$2.9 million (450 x \$6,400). If all distributors elect to file during fiscal year 2001, the credit would be about \$1.8 million (450 x \$4,000).

House Taxation
 3-12-98
 Attachment 4-1

Taylor Oil, Inc.
Specializing in Gasoline and Diesel Fuel Supply

My name is Curt Wright. I am Vice President of Operations for Taylor Oil, Inc. located in Wellsville, KS. Taylor Oil is a family owned and operated business delivering gasoline and diesel fuel to our eastern Kansas customers for over 25 years. I am also a member of the executive board of the Kansas Oil Marketers Association.

My company and our Association fully support the idea of reducing and even eliminating excise tax evasion. In 1995, we backed the changes in fuel tax legislation because they were designed to do so. Tax evasion creates an uneven playing field for the marketer who plays by the rules as well as depriving the state of highway funds. EDI is the next step to reducing tax evasion. However, it will be an expensive endeavor for the members of the industry.

Many small marketers will be forced to either automate their business or pay a service bureau to file their taxes electronically for them. The cost of automation is not merely the cost of computer hardware and software. You must include the productivity lost to the company due to training and the additional time required to complete the new procedures. There are also on-going maintenance costs to maintain the computer system and update the software whenever a law changes in the future. The larger members of the industry already have computer systems in place to handle their accounting functions. Many of these systems do print the required paper fuel tax reports now. Due to the specialized nature of excise taxes, we simply can not run down to the local computer store and pick up a \$150 software package to run our business. In fact, our company updated our computer system two years ago at a cost of \$85,000, and our company is just a little larger than the average distributorship. We will be forced to purchase EDI software and pay for the software modifications to integrate the EDI software with our

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3-12-98
Attachment 5-1



**KANSAS DEPARTMENT OF TRANSPORTATION
OFFICE OF THE SECRETARY OF TRANSPORTATION**

E. Dean Carlson
SECRETARY OF TRANSPORTATION

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Bill Graves
GOVERNOR

**TESTIMONY BEFORE THE
HOUSE TAXATION COMMITTEE**

**Regarding Senate Bill 418 As Amended
An Act Relation To The Taxation Of Motor Vehicle Fuels;
Concerning The Filing Of Certain Reports;
Providing For A Motor Fuel Tax Credit
March 12, 1998**

Mr. Chairman, members of the Committee, thank you for the opportunity to testify today on Senate Bill 418. I am Reed Davis, Assistant to the Director of Administration.

Senate Bill 418 provides a motor fuel tax credit for those who file their reports with the Department of Revenue electronically while still maintaining current statutory requirements in all other areas related to the taxation of motor vehicle fuels.

In 1994, Legislative Post Audit suggested that there potentially was a significant underreporting of motor fuel revenues between \$50 and \$60 million dollars annually. In 1995, legislation passed which permitted the Director of Taxation to require the electronic filing of motor fuel tax returns. Last year the Department of Revenue proposed providing some financial assistance to those who began to file electronically. The Department of Transportation concurred in that proposal. The department feels that electronic filing will permit the Department of Revenue to more efficiently and effectively administer the motor fuel statutes and will provide equitable enforcement for all filers. Electronic filing also permits Kansas to more fully cooperate with ongoing federal efforts to eliminate tax fraud. We agree that it is reasonable to provide some assistance to encourage and promote electronic filing, and the Department of Transportation supports the credits proposed in Senate Bill 418.

The efforts of the Department of Revenue to improve the administration of the motor fuel statutes have improved collections, which, in turn, provides increased receipts to the State Highway Fund.

I hope that the committee will take favorable action on this bill. I will be happy to answer any questions that the committee might have.

Testimony on SB418
House Taxation Committee
March 12, 1998
Prepared by Joe Lieber
Kansas Cooperative Council

Mr. Chairman, and members of the Committee, I'm Joe Lieber, Executive Vice President of the Kansas Cooperative Council. The Council has a membership of nearly 200 cooperative businesses, which have a combined membership of 200,000 Kansans. Approximately 130 of our members are farm supply cooperatives, and most of them sell motor fuel.

The Kansas Cooperative Council supports the concept of SB418 but some of our members have expressed concerns about the mandatory requirement of electronic filing. They don't have the equipment and some feel it would require a change in paperwork.

Thank you for your time. I will be happy to attempt to answer any questions.

House Taxation
3-12-98
Attachment 7-1



KANSAS OIL MARKETERS ASSOCIATION

Convenience Store Association of Kansas

Testimony on Senate Bill 418
Submitted by the Kansas Oil Marketers Association/
Convenience Store Association of Kansas
To The House Taxation Committee

Mr. Chairman and members of the House Taxation Committee:
My name is Tom Palace. I am Executive Director of the Kansas Oil Marketers Association, a statewide trade association representing over 350 independent Kansas petroleum companies which distribute petroleum products at the wholesale and/or retail level. KOMA is also the flagship organization for the Convenience Store Association of Kansas, and as such, represents the interests of the owners and operators of convenience stores across the state.

We appreciate the opportunity to appear before you to provide testimony on S.B. 418.

In 1994, The Kansas Department of Revenue was requested by the Legislative Post Audit Committee to thoroughly investigate options for improving controls over the collection of motor fuel taxes and report their findings to the 1995 legislature. Best guess estimates were that the state could be losing up to \$66 million in combined gasoline and diesel fuel taxes. Fuel taxes were being evaded due to the fact that the state could not track fuel sales and deliveries to their final destination. Additionally, the Kansas Department of Revenue could not verify whether or not fuels sold as non-taxable, were truly tax-exempt sales under the motor fuel tax laws. Tax exempt sales are: fuel sold to the Federal Government, fuel sold to a contractor performing work for the Federal Government, fuel exported to another state, fuel sold on Indian reservations, aviation fuel, the first sale of fuel to a distributor and dyed diesel fuel. Basically, tax exempt sales constitute fuel sold for NON-highway purposes.

A coordinated effort by the petroleum industry and representatives from 6 state agencies formed the Motor Fuels Advisory Committee in 1994 to develop a solution to the problem of fuel tax evasion. The committee agreed that the key to resolving fuel tax evasion would require a complete fuel tracking system along with visible enforcement.

In 1995, HB 2161 was passed. The bill included a comprehensive package aimed at improving the fuel tracking system and combating fuel tax evasion in Kansas. The law increased penalties for violators; diesel fuel that is sold for tax-exempt purposes was required to be dyed red so that when inspected, it could be easily ascertained that the fuel was not taxable; bills of lading were required to show complete addresses so that fuel could be tracked from the terminal to the ultimate destination; licensed retailers were required to complete fuel reports so that the state could better track fuel they received from distributors, and a phase in period for electronic filing of monthly fuel tax returns **may** be required.

House Taxation
3-12-98
Attachment 8-1

This final phase of the 1995 legislation provides for Electronic Data Interchange (EDI), a method by which fuel tax returns would be transmitted to the state on a monthly basis. Currently, the state reviews monthly fuel tax returns from over 900 distributors and twice that many retailer reports, manually. According to the 1994 Post Audit Report, the revenue department was running six months behind in processing motor fuel returns. I don't know what the backlog is today, but I would anticipate that they are not running six months behind in the audit process.

In an attempt to become more modernized and efficient, the Department of Revenue wants to mandate EDI, and require any licensed distributor that receives 50,000 gallons of fuel or more per month, to file with the state electronically. KOMA supports the idea of electronically filing monthly fuel tax returns and has worked closely with the Department in efforts to educate distributors throughout the state about the benefits of EDI. However, EDI is a method of filing that will first and foremost serve the Department of Revenue. It will allow for more definitive tracking returns. That is its sole purpose. It has never been viewed as a method of making the job of tax filing easier for the filer.

With all the benefits that the Department receives from EDI, licensed distributors affected by EDI will not only be required to comply with this new record keeping measure, but will also be required to pay for this new record keeping measure. For years, licensed motor fuel distributors in Kansas have served the state well by the timely filing of monthly motor fuel tax returns. No matter what system of filing is in place, they will continue to be reliable tax collectors for Kansas. Some distributors welcome EDI; quite clearly others do not. There are many smaller operations in Kansas which are not computer-based and are angered for having to change their way of doing business. That message was made loud and clear as KOMA and KDOR held meetings last summer throughout the state explaining EDI. There are two areas of concerns that the distributors have; being forced to implement EDI and the cost. Fortunately the Department, in an attempt to soften the blow of EDI, has suggested an \$8,000 one time tax credit for distributors affected by the implementation of EDI, which is included in SB 418.

SB 418 requires the use of EDI and provides a tax credit to distributors that are affected by EDI. KOMA supports the amended version of SB 418.

We appreciate the opportunity to appear before you today and will stand for any questions you may have.

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MEMORANDUM

TO: Representative Phill Kline
Chair, House Taxation Committee

FROM: Shirley Klenda Sicilian
Director, Policy & Research; Kansas Department of Revenue

RE: **Senate Bill 421 - Amendments clarifying motor fuel tax is imposed on the distributor**

DATE: March 12, 1998

Representative Kline and members of the House Taxation Committee, thank you for the opportunity to testify today regarding the Department's proposed clarifications to the motor fuel tax act.

I. Background

This bill is intended to clarify that the legal incidence of the motor fuel tax is on motor fuel distributors, not retailers, and not customers. Prior to 1995, some distributors claimed an exemption for the fuel they sold to retailers on Indian reservations, under the theory that that fuel was delivered to an "agency" of the United States, which would be exempt from taxation. In 1995, the legislature amended the motor fuel tax act to create an exception to that exemption. The exception stated that fuel delivered to a reservation retailer would not be exempt if that retailer sold or delivered to non-tribal members. The purpose of the 1995 legislation was to level the competitive playing field between retailers on the reservation and near-by off-reservation retailers.

Objections were raised as to whether the department could actually enforce collection and the secretary of revenue requested an Attorney General's opinion. The AG upheld the state. In so doing, the AG explained that if the legal incidence of the tax fell on the tribe or its members, the state could not collect. However, "if the legal incidence of the tax rests on non-tribal members, the state may impose the tax and require the tribe to perform functions to assist in collection of the tax..."¹ The Attorney General found the legal incidence of the motor fuel tax to be on the distributor; not the tribal retailer or the ultimate, tribal and non-tribal, consumers.

¹ Attorney General Opinion No. 95-80.

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In September of 1995, the department began enforcement of the new law. That same month, two lawsuits were filed contending, contrary to the AG's opinion, that the legal incidence of the motor fuel tax falls on the retailer, and thus cannot be collected from tribal retailers. In one of those cases, the Jackson County court has ruled that the department may continue collecting motor fuel taxes from distributors that sell to non-tribal retailers on the Potawatomi reservation. That case is being appealed, but in the meantime, the department is enforcing collection. In the other case, the U.S. district court judge has issued a temporary restraining order preventing the department from collecting taxes from the tribal retailers on the Iowa, Kickapoo and Sac and Fox reservations.

The department believes the legislative intent of the motor fuel tax act is to levy a tax on the distributor. The act, on the whole, is actually quite clear about that. Our bill contains amendments that clean up individual portions of the act which lack clarity and could possibly be construed to the contrary. Some of the proposed changes are prompted by how courts in other states have interpreted similar language.

II. Summary of proposed amendments.

Section one clarifies the wording on causes for motor fuel license revocation, to clearly differentiate between making *payment* of tax, penalty or interest which is only required of distributors, from making a *report* which is required of both distributors and retailers.

Section two states that the incidence of this tax is imposed on the distributor of first receipt of the motor fuel. The proposed language in Section two, subsection (c) clarifies that the 2.5% deduction afforded to distributors is for physical loss of fuel due to causes such as evaporation and thermal contraction, and not for any administrative costs incurred by a distributor in remitting the fuel tax.

Section three new subsection (c) comports with Attorney General opinion 95-80 that tribal retailers cannot be held liable for the inventory tax that occurs from time to time when fuel tax rates increase.

Section four allows the distributor's cost of doing business, as well as the tax paid, to be included in the selling price of fuel; and clarifies that when the posted price of the fuel does not include the state and federal tax, the tax referred to is the tax that the dealer's distributor paid, or for which the distributor was liable.

Section five changes language from "delinquent distributor, manufacturer, importer or retailer" and "taxpayer" to "person."

Section six repeals a section that disallows the tax-free sales of gasoline and special fuels to retail dealers located on an Indian reservation in Kansas, if the fuel is sold and delivered to a nonmember of the reservation. Retailers don't pay the tax, so there is no need for the disallowance of a tax free sale, regardless of who the retailers' customers are.