

Approved: February 23, 1999  
Date

## MINUTES OF THE HOUSE COMMITTEE ON TAXATION.

The meeting was called to order by Chairperson Adkins at 9:00 a.m. on January 14, 1999 in Room 519-S of the Capitol.

All members were present except: All present

Committee staff present: Chris Courtwright, Legislative Research Department  
April Holman, Legislative Research Department  
Don Hayward, Revisor of Statutes  
Shirley Sicilian, Department of Revenue  
Mary Shaw, Committee Secretary

Conferees appearing before the committee:

Dan Hermes, Director of Governmental Affairs, Governor's Office  
Chris Courtwright, Legislative Research Department  
April Holman, Legislative Research Department

Others attending: See attached list.

The Chairman opened the meeting with a brief orientation with committee members and staff introducing themselves. Since there were some new committee members, the Chairman asked for the committee members to give their names, where they were from, how many years they have been in the Legislature and whether or not they are new to the Taxation Committee.

The Chairman introduced Dan Hermes, Director of Governmental Affairs for the Governor. Mr. Hermes gave a briefing regarding the Governor's Tax Relief Proposals (Attachment 1). .

The Chairman opened the meeting to bill introductions.

The Chairman recognized Representative Wilk who made a motion, and seconded by Representative Johnston, to introduce the Governor's car tax proposal in a committee bill. Motion carried.

The Chairman recognized Representative Aurand who made a motion, and seconded by Representative Minor, to introduce the Governor's sales tax exemption proposal for grain storage and transportation in a committee bill. Motion carried.

Chairman Adkins introduced April Holman and Chris Courtwright of the Kansas Legislative Research Department who gave briefings to the Committee on the Interim Committee Reports of the Special Committee on Assessment and Taxation (Attachment 2).

Committee Rules (Attachment 3) and Conferee Rules (Attachment 4) were distributed.

The meeting adjourned at 10:10 a.m.

The next meeting is scheduled for January 19, 1999.

HOUSE TAXATION COMMITTEE

GUEST LIST

DATE: Jan. 14, 1999

Kich McKee	Kansas Livestock Assoc
Kelly Kuitala	City of Overland Park
Debbie Glenn	Volunteer Assistant - Johnson
Ann Dukes	DOB
Clay Johnson	Ks Taxpayers Network
Whitney Dameron	KS Gas Service
Bruce Janese	BOEING
Doug Smith	SWKROA
Nanci Xerox	Sedgwick County
Bill Fuller	Kansas Farm Bureau
Jim Allen	Seaboard
RICHARD BODEWALD	TAXPAYERS
Tom Tunnell	KGFA/KFCA
Dag Wareham	KGFA/KFCA
Don Schnack	KIOGA
SCOTT SCHNEIDER	McGILL, GRACHER & ASSOC.
Alan Steppat	KLPG

# STATE OF KANSAS

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## OFFICE OF THE GOVERNOR

### LEGISLATIVE TESTIMONY

TO: Chairman David Adkins and Members of the House Committee on Taxation

FROM: Dan Hermes, <sup>DWH</sup> Director of Governmental Affairs

DATE: January 14, 1999

SUBJECTS: Governor's Tax Relief Proposals

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Mr. Chairman and members of the committee, thank you for the opportunity to appear today to discuss the Governor's tax relief proposals. My name is Dan Hermes and I am the Director of Governmental Affairs for the Governor.

The tax relief proposals the Governor has included in his budget recommendations to you cannot be adequately explained outside the context of the overall budget he recommended from the State General Fund and the impact of several tax reduction measures enacted last session.

His budget recommends increased spending from the State General Fund for FY 2000 that is 2.6 percent above the revised FY 1999 amount. This is equal to expected inflation for this year. Included in this recommendation is \$41 million to increase the demand transfer to the State Highway Fund. By any standard, this is a conservative budget.

Additionally, the "first" dollars that had to be accounted for in the spending plan were additional dollars for last year's tax cuts. This includes \$83.5 million in additional spending for property and car tax cuts, as well as an additional reduction in receipts of \$35 million to move to an estate tax.

When we view the \$15.1 million cost of the new tax reductions in this light – combined with the new dollars committed to financing last year's package – we see a spending package that commits an additional \$133.6 to our ongoing tax relief efforts. Put in perspective, that amount committed to spending would allow increased State General Fund expenditures of about three percent. Total reductions for taxpayers in FY 2001, based on our combined efforts the last four years, will total \$898.1 million.

House Taxation  
1-14-99  
Attachment 1

## Motor Vehicle Tax Elimination

Although it does not reduce receipts in FY 2000, by far the most significant of the Governor's recommendations is the elimination of taxes on "tax and tag" vehicles. This plan piggy-backs on the reduction plan passed in 1995. The final tax cut in the previous plan is a reduction from a 22.5 percent to 20 percent assessment rate for cars in 2000. The Governor's proposal reduces this assessment rate to 15 percent in 2001, to 10 percent in 2002 and to five percent in 2003. The tax would not exist in following years. As a reminder, the assessment rate is the percent applied to the car's value that is multiplied by the mill levy to determine the tax.

Before visiting about the details of how local government would be reimbursed for the reduced receipts, it is important to explain: why eliminate the car tax -- why not reduce income taxes or eliminate another tax, such as the tax on food.

I served with two of your colleagues and several university economists on the Governor's Tax Review Commission this fall. I believe that our major finding related to state tax policy is that the state lacks adequate information on the impact of state and local tax policy on our families. In other words, how much tax do Kansans at different income levels, with different family situations pay in total and by tax.

The review commission provided the Department of Revenue resources to begin to develop a tax incidence model to provide this information and we have some preliminary results. Of our major taxes, the property taxes on cars and trucks is our most regressive tax. It hits working Kansans harder than the sales tax, the general property tax and the individual income tax. The following table presents some of these results.

1996 Adjusted Gross Income Level	Individual Income Tax (Percent of Tax Paid)	Sales and Use Tax (Percent of Tax Paid)	Vehicle Property Tax (Percent of Tax Paid)
\$1 - \$10,000	0.6	3.0	10.0
\$10,001 - \$20,000	3.5	9.3	12.4
\$20,001 - \$30,000	6.5	11.3	12.9
\$30,001 - \$40,000	8.0	10.8	12.0
\$40,001 - \$50,000	8.8	12.0	11.3
\$50,001 - \$60,000	9.4	11.0	10.1
\$60,001 - \$70,000	6.7	9.1	7.9
\$70,001 - \$80,000	7.2	6.0	5.8
\$80,001 - \$90,000	5.6	4.4	4.0
\$90,001 - \$100,000	4.3	3.2	2.7
\$101,000 - \$250,000	19.2	12.0	8.5
More than \$250,000	17.9	8.1	2.0

As you can see from the table, people with lower incomes pay a higher percent of the vehicle tax than either the income tax or the sales tax. Conversely, our wealthiest Kansans pay a far greater share of the income and sales tax than they pay in vehicle taxes. The assertion by advocates that an elimination of the tax on food is the most effective way to help working class taxpayers is simply not the case. The evidence is clear -- an elimination of the car tax is far more helpful to low and middle income taxpayers.



Local governments are understandably concerned when we discuss elimination of one of their more important and elastic tax sources. Much effort was made in designing this plan to assure that local governments will experience no impact from this proposal. The state will reimburse each county based on the law in effect in 2000. Monthly distributions will be made in the transition years of the difference in the amount taxpayer's pay and the amount they would have paid under existing law. In future years, the entire amount would be provided to counties to distribute based on the current distribution arrangement with cities and other government units. Changes in car values in each county and the applicable mill levy will continue to drive their receipts.

### Business Machinery and Equipment

The Governor recommends an increase from 15 to 20 percent in the refundable income tax credit businesses receive for property taxes paid on machinery and equipment. Kansas business continues to be taxed on their productive capital at a level higher than surrounding states. This recommendation continues progress toward eliminating this competitive disadvantage.

### Oil Severance Tax

The oil industry has played an integral role in the Kansas economy for many years. To help relieve the effect of declining oil prices, the Governor recommends the elimination of this tax, as well as the tax on coal. Although, the state cannot influence the international oil market, we must do what we can to reduce the tax burden on this industry – a tax burden that is higher than in other states that also produce a significant amount of oil.

### Adoption Tax Credit

Two years ago, the legislature approved a \$1,250 income tax credit for families that adopt. This was half of the amount recommended at that time by the Governor. In order to provide additional assistance to Kansas citizens who provide homes through both private adoptions and adopting children in the custody of SRS, the Governor recommends the credit be doubled to the amount of his original recommendation.

### Sales Tax Exemption for Grain Storage and Transportation

Grain storage capacity during the last two harvests has been inadequate, resulting in the storage of grain on the ground. The first component of the recommendation provides a sales tax exemption of labor and materials used for the construction or refurbishment of commercial grain elevators. The exemption should provide an incentive to expand available storage space. This exemption sunsets in five years.

Reliable rail service is another variable that determines when grain must be stored on the ground. The second part of this recommendation provides sales tax exemptions on materials and

labor for enhancement of shortline railroad infrastructure. The exemptions will serve as an incentive for maintenance and use of rail lines vital to moving agricultural products produced in Kansas to market. This, coupled with the Governor's recommendation for low-interest loans of \$4.0 million per year for shortline track rehabilitation in the transportation bill will provide significant assistance to maintain this critical infrastructure.

Thank you for your time and assistance. I look forward to working with your committee this session to improve tax policy in our state and would answer any questions you may have.

Reports of the  
Special Committee on Assessment  
and Taxation  
to the  
1999 Kansas Legislature

**CHAIRPERSON:** Senator Audrey Langworthy

**VICE-CHAIRPERSON:** Representative Tony Powell

**OTHER MEMBERS:** Senators David Corbin, Les Donovan, Jerry Karr, and Janis Lee, (Jim Barone, special designee for Retail Wheeling); Representatives Troy Findley, Dave Gregory, Annie Kuether, Bruce Larkin, Gayle Mollenkamp, Vern Osborne, and Jene Vickrey

**STUDY TOPICS**

- Education savings accounts
- Expansion of sales tax exemption for manufacturing machinery and equipment in connection with the integrated production theory
- Private property rights as affected by tax increment financing and eminent domain laws
- Taxing municipal and rural water districts—sales tax
- Board of Tax Appeals
- Local county appraisers issues
- Oil and gas industry issues, including consideration of repeal of the severance tax on the production of oil and gas
- Proposed constitutional amendments—H.C.R. 5034, boats and airplanes, and H.C.R. 5004, oil and gas
- Retail wheeling—tax implications

December 1998

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HOUSE TAXATION  
1-14-99  
Attachment 2

# SPECIAL COMMITTEE ON ASSESSMENT AND TAXATION

## EDUCATION SAVINGS PLAN

### CONCLUSIONS AND RECOMMENDATIONS

The Committee recognizes the importance of the extensive study of education savings account issues performed by the Kansas College Savings Plan Task Force. The Committee believes that the Task Force report will serve as a valuable resource document as the 1999 Legislature again considers education savings account tax issues. The Committee further encourages the House Taxation and Senate Assessment and Taxation Committees to develop legislation in 1999, perhaps considering the recommendations outlined in the Task Force report.

### BACKGROUND

During the 1998 Legislative Session, legislation was passed directing the Treasurer's office to conduct a feasibility study concerning college savings plans. The Special Committee on Assessment and Taxation was given the charge of monitoring the progress of the Task Force which was created for this purpose. Under the provisions of the legislation, the Treasurer formed the Kansas College Task Force to study and develop possible criteria for a postsecondary education savings plan. The study included a review of the following:

- an examination of existing state-sponsored postsecondary education savings plans;
- determination of participation guidelines;
- maximization of participant's state and federal tax benefits under the current tax codes;
- consideration of the range of coverage of savings programs in terms of restricting them to tuition and fees or also including additional postsecondary education costs;
- examination of investment procedures and regulations including programs managed by the private sector; and
- consideration of establishing an oversight committee or an appointed board of directors, including the State Treasurer or other

representatives affiliated with higher education and the investment community.

Due to the concerns raised by members of the Legislature and the academic community regarding the level of the financial commitment occasioned by prepaid college savings plans which guarantee future educational costs, the Task Force focused its inquiry on college savings account plans.

The Task Force report noted that a key underpinning of any successful college savings plan would be making full use of the federal tax code to achieve the most favorable tax treatment for the plan beneficiaries. At the current time, this requires that a plan achieve "qualified status" which defers the federal tax owed until the funds are disbursed for educational purposes. The disbursements are then treated by the Internal Revenue Service as the beneficiary's assets, and a lower tax rate is applied. The federal requirements for a qualified college savings plan are as follows:

- contributions must be in cash;
- neither the contributor, nor the beneficiary may exercise any investment control over the plan account;

- a separate accounting should be required for each designated beneficiary;
- a specific beneficiary must be named when the account is established;
- the transfer of funds to another account, or a change of beneficiary is an immediate family member as defined for Internal Revenue Code purposes;
- more than a *de minimus* penalty should be required on earnings withdrawn not used for qualified educational expenses unless the disbursement is on account of death or disability, or is made on account of a scholarship awarded the beneficiary to the extent that the sum does not exceed the scholarship amount used for qualified educational expenses;
- the account interest may not be used to secure a loan; and
- the plan should contain safeguards to prevent accumulating contributions more than necessary to cover the beneficiary's qualified educational expenses.

The Task Force determined that Kansas can maximize the savings advantage and the attractiveness of its college savings plan program by making annual contributions deductible from the contributor's Kansas gross income. The state should allow beneficiaries to take full advantage of compound interest by exempting account earnings on distributions provided that the funds are used to pay qualified education expenses.

In recognizing that the availability of federal student grant aid has decreased over the last ten years while the use and availability of student loans has increased, the Task Force noted that a prime goal of a Kansas college savings plan must be to encourage savings thereby reducing the future "debt load" on students and their families, which should then lower the loan default rate.

Therefore, the Task Force recommends that the state adopt a savings plan to encourage any Kansas family with some income apportionable for savings to do so. Any individual with a valid Social Security number should be eligible to open an account for any beneficiary who is a Kansas resident when the account is established. As an incentive to participate, the beneficiary should

remain eligible to receive benefits from the account without penalty after relocation to another state.

The Task Force stated that the benefits of a qualified college savings plan should be made available to the greatest number of Kansans seeking a postsecondary education. Under a qualified plan, the institutions of higher learning eligible for disbursements from a beneficiary's savings account would include any that meet the participation requirements for federal student aid programs. Those institutions include the following:

- any two-year and four-year public or regionally accredited private not-for-profit college or university,
- community colleges, or
- an accredited or certified technical training school.

Federal law defines those expenses payable from a qualified savings plan account as tuition, fees, books, supplies, or equipment required for enrollment or attendance, and reasonable room and board for a beneficiary enrolled on at least a half-time basis.

Account assets not to be used for educational purposes, or in the event of the death, mental incapacity, or permanent disability of the beneficiary should be transferable to the college savings account of a "member of the same family" as defined by the United States Department of Education.

The Task Force concluded by saying that the Legislature will have to determine the amount of Kansas taxable income it can afford to exempt as an incentive to invest in educational savings accounts, as well as the annual specific maximum tax exempt contribution per account. To this end, the Task Force included the following graph which shows the fiscal impact of a savings plan under various scenarios.



## COMMITTEE ACTIVITIES

At the July meeting the Treasurer briefed the Committee on the creation of the College Savings Plans Task Force to study and develop possible criteria for a postsecondary education savings plan.

At the August meeting, the Assistant State Treasurer presented an update on the feasibility study conducted by the Task Force. She discussed the list of questions being addressed by the group and distributed copies of the minutes of the first meeting of the Task Force. Following the update from the Treasurer's office, the Department of Revenue presented a report which included an education profile for Kansas, information on federal assistance programs for higher education, information on state education/tuition plans, and an analysis of the interaction between state and federal plans.

At the October meeting, the Treasurer once again updated the Committee on the progress of the Task Force. He reported that, due to scheduling conflicts, the final report of the Task Force would not be available to the Committee until the November meeting.

At the November meeting, the Treasurer presented the Task Force report and recommendations.

## CONCLUSIONS AND RECOMMENDATIONS

The Committee recognizes the importance of the extensive study of education savings account issues performed by the Kansas College Savings Plan Task Force. The Committee believes that the Task Force report will serve as a valuable resource document as the 1999 Legislature again considers education savings account tax issues. The Committee further encourages the House Taxation and Senate Assessment and Taxation Committees to develop legislation in 1999, perhaps considering

the recommendations outlined in the Task Force report. Some of those recommendations are as follows:

- make full use of the federal tax code to achieve the most favorable tax treatment for the plan beneficiaries;
- maximize the savings advantage and the attractiveness of the college savings plan program by making annual contributions deductible from the contributor's Kansas gross income;
- allow beneficiaries to take full advantage of compound interest by exempting account earnings on distributions provided that the funds are used to pay qualified education expenses;
- encourage savings thereby reducing the future "debt load" on students and their families, which should then lower the loan default rate;
- any individual with a valid Social Security number should be eligible to open an account for any beneficiary who is a Kansas resident when the account is established;
- beneficiaries should remain eligible to receive benefits from the account without penalty after relocation to another state;
- include any institutions that meet the participation requirements for federal student aid programs in the list of institutions of higher learning eligible for disbursements from a beneficiary's savings account;
- account assets not to be used for educational purposes, or in the event of the death, mental incapacity, or permanent disability of the beneficiary should be transferable to the college savings account of a "member of the same family" as defined by the United States Department of Education; and
- the Legislature should determine the amount of Kansas taxable income the state can afford to exempt as an incentive to invest in educational savings accounts as well as the annual specific maximum tax exempt contributions per account.

# EXPANSION OF SALES TAX EXEMPTION FOR MANUFACTURING MACHINERY AND EQUIPMENT IN CONNECTION WITH THE INTEGRATED PRODUCTION THEORY\*

## CONCLUSIONS AND RECOMMENDATIONS

The Committee recommends that the Kansas law exempting certain manufacturing machinery and equipment from sales tax be clarified and modified to reflect the integrated plant theory. Additionally, the Committee recommends that the exemption be extended to include oil and gas drilling services and supplies as well as drilling, pumping, and monitoring equipment used at a well site or in oil and gas exploration.

## BACKGROUND

The Committee was given the task of reviewing the Governor's proposal for manufacturing machinery and equipment in its entirety, along with the related proposals to expand the consumed in production exemption.

Almost all states have some form of sales tax exemption for manufacturing machinery and equipment. In some states the manufacturing exemption is tied to economic development criteria, such as new jobs. Kansas has both an economic development related exemption and a straight manufacturing machinery and equipment exemption. K.S.A. 79-3606(kk) is an exemption for manufacturing or processing machinery and equipment, and it has no employment criteria. The proposed legislation to expand the exemption for manufacturing machinery and equipment would amend K.S.A. 79-3606(kk).

There are two basic standards for exemption of manufacturing machinery and equipment. One standard, usually called the physical transformation or Ohio rule, requires that exempt machinery and equipment have a "direct and immediate effect" on the physical transformation of raw materials into new products. The other standard is the integrated plant rule. The inte-

grated plant rule only requires that exempt machinery and equipment constitute an "integral or essential part of the manufacturer's production process." As initially proposed in 1988, K.S.A. 79-3606(kk) would have limited the scope of the exemption to production line machinery and equipment following the Ohio rule. Before being enacted the bill was amended to specifically include a few other types of machinery and equipment. The result is a combination of the two different theories which has been difficult to interpret and administer consistently over the years. Furthermore, as recently as July 10, 1998, the Kansas Supreme Court upheld the Department of Revenue's understanding of the statute and explicitly rejected the Board of Tax Appeals application of the integrated plant theory to the "major component" determination of K.S.A. 79-3606(kk)2.

In 1996, the Department of Revenue surveyed its auditors and asked them to identify the statutes which created the most controversy or confusion. Two of the top problem areas were the consumed in production exemption and the manufacturing machinery and equipment exemption. Last session, the Governor proposed H.B. 2643 which would have, among other things, clarified and expanded these two statutes. The clarifications would have shown that Kansas was

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\* H.B. 2009 was recommended by the Committee.

adopting a broadly defined integrated plant theory; however, those provisions did not pass.

The Department of Revenue, along with industry groups, developed proposed legislation which they presented to the Committee. There are three major points and objectives of the proposed legislation. The first is to expand the exemption for property which is "immediately" consumed to property which is consumed within one year. This eliminates confusion over what is meant by "immediately" consumed. The proposed legislation also clarified that the exemption applies to certain lubricants and catalysts.

The second major point and objective of the proposed legislation is to expand the manufacturing machinery and equipment exemption from just that machinery which has a direct physical effect on the property being produced, to all machinery which is part of a broadly defined integrated production process. The expansion would explicitly pick up the following:

- pre-production machinery and equipment (e.g., raw material storage equipment, raw material handling equipment, etc.);
- machinery that services the production line (e.g., machinery that purifies water, cleans oil, screens chemicals, etc.);
- machinery that deals with by-products of production (e.g., pollution control equipment, waste handling equipment, etc.); and
- ancillary property that might otherwise not be viewed as "machinery or equipment" (e.g., gas pipes, electric wiring, special foundations, clean rooms, etc.)

The proposed legislation would exempt labor services for installation and repair of qualified machinery, expanding the exemption, and eliminating the requirement that taxpayers separate out installation costs from equipment costs. The proposed legislation would clarify, without narrowing, the types of firms eligible to receive the exemption.

The third major objective addressed by the proposed legislation is to extend the exemption beyond manufacturing or processing machinery

and equipment to add oil and gas extraction related machinery and equipment which is part of a broadly defined integrated production process. Machinery and equipment involved in the extraction process has not been exempt in the past.

According to the Department of Revenue, the fiscal year 2000 impact of this proposed legislation would be \$5 million for the manufacturing machinery and equipment and the consumed in production expansion. The addition of oil and gas exploration and extraction adds another \$7.1 million. The total fiscal impact would be \$12.1 million, while the State General Fund impact would be \$11.5 million and the State Highway Fund impact would be \$0.66 million.

## COMMITTEE ACTIVITIES

At the July meeting, the Director of the Office of Policy and Research of the Department of Revenue briefed the Committee on the background of Kansas' treatment of the manufacturing machinery and equipment sales tax exemption. At that time, she also provided the Committee with copies of a recent *Washburn Law Journal* article on the integrated plant theory, as well as the Governor's Tax Simplicity and Fairness Proposal and the 1988 *Kansas Retailers' Sales Tax Information Guide* which the Department issued after the sales tax exemption for manufacturing machinery and equipment was enacted. Conferees advocating clarification and expansion of the current law at the July meeting included representatives of the Boeing Company, the Kansas Independent Oil and Gas Association, the Kansas Chamber of Commerce and Industry (KCCI) and the Wichita Area Chamber of Commerce.

At the September meeting, the Committee heard an update from the Department of Revenue, including the fiscal note on extending the sales tax exemption to oil and gas machinery. Conferees testifying in favor of the integrated plant approach included representatives of the Boeing Company, KCCI, the Kansas Corporation Commission, and Custom Metal Fabricators, Inc. The Committee passed a motion for a bill

draft to be prepared with the basic concept of the integrated plant proposal, including the oil and gas provisions.

At the October meeting, the Department of Revenue presented the Committee with a bill draft of legislation which would adopt an integrated plant approach, expanding the exemption for manufacturing machinery and equipment. The Department of Revenue also provided an updated fiscal note on the proposed legislation in the amount of \$12.1 million including the oil and gas portion. The Committee approved a motion recommending introduction of the legislation in the 1999 Legislative Session.

## CONCLUSIONS AND RECOMMENDATIONS

The Committee concludes that the benefits of the proposal to expand the sales tax exemption for manufacturing machinery and equipment outweigh the cost of providing such an expansion, noting the importance of the manufacturing sector because of the number of jobs that it creates.

The Committee recommends that the Kansas law exempting certain manufacturing machinery and equipment from sales tax be clarified and modified to reflect the integrated plant theory. Additionally, the Committee recommends that exemption be extended to include oil and gas drilling services and supplies as well as drilling, pumping, and monitoring equipment used at a well site or in oil and gas exploration.

## PRIVATE PROPERTY RIGHTS AS AFFECTED BY TAX INCREMENT FINANCING AND EMINENT DOMAIN LAWS

### CONCLUSIONS AND RECOMMENDATIONS

The Committee recommends that the issues of eminent domain usage and private property rights as they relate to Tax Increment Financing (TIF) be further studied by the standing committees of both houses during the 1999 Legislative Session.

### BACKGROUND

Under Kansas law, cities have the authority to exercise the power of eminent domain to acquire property in connection with a redevelopment district established under the Tax Increment Financing (TIF) Act, K.S.A. 12-1770, *et seq.* This act is one of hundreds of state statutes authorizing cities and other local units to acquire property through the exercise of the power of eminent domain.

The use of the power of eminent domain is conditioned, however, on the requirement of the Fifth Amendment to the *United States Constitution* that just compensation be paid and that it be for a valid public use.

Although the Kansas Supreme Court has held that what constitutes a valid public use or purpose cannot be precisely defined and it changes over time (*Ulrich v. Board of Thomas County Commissioners*, 234 Kan. 782, 789 (1984)) the threshold question is whether the use of the public funds or the exercise of eminent domain served a "public" rather than a "private" purpose.



The TIF Act was enacted in 1976 to stimulate and develop the general and economic welfare of the state and its communities. Specifically, the statute states its purpose to assist in the development and redevelopment of the following areas and thus promote the general welfare of the citizens of the state by authorizing cities to acquire certain property and to issue special obligation bonds for the financing of redevelopment projects. Projects located in one of the following areas may qualify for TIF financing:

- blighted areas;
- deteriorating areas within cities which are not yet blighted, but which may be so in the future;
- environmentally contaminated areas located within and without cities;
- enterprise zones within cities; and
- major tourism areas.

The statute goes on to state that the powers conferred by the TIF Act are for public uses and purposes for which public money may be expended and the power of eminent domain exercised.

The TIF Act allows the use of eminent domain in three types of instances. They are as follows:

- in the case of an area within a city which is deemed to be blighted by substantial deterioration or dilapidation that substantially impairs the sound development or growth of the city, is an economic or social liability, or is a menace to the public health, safety, morals, or welfare;
- in the case of an area within a city which is deemed to be blighted by virtue of having been identified by any state or federal environmental agency as being environmentally contaminated; or
- in the case of an area within a city which was designated prior to 1992 as an enterprise zone and the city deems the conservation, development, or redevelopment of the area is necessary to promote the general economic welfare of the city.

There is a list of steps which a city must follow to establish a TIF district in order to complete the financing and improvement of the area. This process has procedural safeguards, including the requirements that a super-majority vote of the governing body (two-thirds) is required before eminent domain is used, and that relocation assistance payments must be paid including compensation of any retailer for losses due to the liquidation of inventories.

## COMMITTEE ACTIVITIES

It was announced at the September meeting that the Legislative Coordinating Council had assigned the topic of private property rights as affected by tax increment financing and eminent domain laws to the Special Committee on Assessment and Taxation.

At the November meeting, the League of Kansas Municipalities briefed the Committee on the history of TIF laws in Kansas. Also in November, a public hearing was held on the topic. Conferees at the public hearing included State Representative Cliff Franklin; property owner, Lavern Gross; the Merriam City Attorney; and the Community Development Director for the City of Merriam. State Representative Phill Kline provided written testimony to the Committee.

Testimony at the public hearing centered around an ongoing dispute between one property owner and the City of Merriam. In this case, the city was able to exercise eminent domain because the property in question is located in an area which was designated an enterprise zone prior to 1992. Representative Franklin urged the Committee to develop a clearer definition of "public good" as used in the TIF Act, and to develop better guidelines for the use of eminent domain.

## CONCLUSIONS AND RECOMMENDATIONS

Some members of the Committee expressed concern as to whether the proper balance between private property rights of existing property owners in re-development districts and economic



development interests exists under the TIF and eminent domain laws. The Committee recommends that the issues of eminent domain usage

and private property rights as they relate to TIF be further studied by the standing committees of both houses during the 1999 Legislative Session.

## TAXING MUNICIPAL AND RURAL WATER DISTRICTS—SALES TAX\*

### CONCLUSIONS AND RECOMMENDATIONS

The Committee recommends that purchases of tangible personal property and services made by municipalities and certain rural water districts for use in the operation or maintenance of the district be exempt from sales tax.

### BACKGROUND

Legislation was originally introduced in 1996 and later reintroduced in 1997 as H.B. 2107 to exempt all purchases of rural water districts organized or operated under the authority of K.S.A. 82a-612, provided the tangible personal property and services purchased are used in the operation or maintenance of the district. The legislation would also have exempted all similar purchases of public water supply districts organized or operated pursuant to K.S.A. 19-3501 or K.S.A. 19-3522 as well as expanded the sales tax exemption for groundwater management districts, rural water districts, and public water supply districts to include certain purchases made indirectly through contractors.

While the House passed the water district legislation, the Senate did not act on it. The issue was referred for study to the 1998 interim committee.

### COMMITTEE ACTIVITIES

A public hearing on the topic was held at the July meeting. Conferees included representatives of the League of Kansas Municipalities, the Kansas Rural Water Association, Johnson County Water District No. 1, the City of Wichita, the City of Olathe and the law offices of Stumbo, Hanson and Hendricks, LLP on behalf of five small cities and approximately 25 water districts.

An updated fiscal note was presented at the September meeting. The Department of Revenue used data from a 1995 survey by the Kansas Rural Water Association as well as data compiled from the largest cities in Kansas, determining that this change in the law on July 1 would reduce state sales tax collections by \$4.4 million in FY 2000. Of this amount, \$4.2 million would be attributable to a reduction in State General Fund (SGF) receipts, and \$0.2 million to a reduction in State Highway Fund (SHF) receipts. The SGF fiscal note would be \$4.8 million in FY 2001 and \$4.9 million in FY 2002, while the SHF fiscal note would be \$0.3 million in both years.

Also in September, the Committee voted to introduce a bill identical to 1997 H.B. 2107 which would amend K.S.A. 79-3606(b) by striking the

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\* H.B. 2011 was recommended by the Committee.

word "water" as one of the utility services that is taxable when operated by a political subdivision and also would amend K.S.A. 79-3606(s) to include rural water districts as exempt. The effect of these changes would be to exempt from sales tax those purchases made by city and county public works/water departments and rural water districts for tangible personal property and services used in providing water.

In October, the Committee voted to approve a draft Committee report.

## CONCLUSIONS AND RECOMMENDATIONS

The Committee finds that provision of water is a basic governmental service, and the public-at-large therefore would benefit from reduced operating costs and simplified administration associated with exempting water district purchases from the sales tax. The Committee recommends the introduction of legislation to provide such an exemption and strongly encourages its enactment by the 1999 Legislature.

## BOARD OF TAX APPEALS

### CONCLUSIONS AND RECOMMENDATIONS

The Committee does not at this time recommend any further changes in statutes relating to the State Board of Tax Appeals (SBOTA) or the property tax appeals process. The Committee does note that the Legislature may need to review the hearing officer step in the appeals process to the extent that county-appointed hearing officers may provide a duplicative step in the process, given the new hearing officers appointed by SBOTA.

### BACKGROUND

The Legislature, in 1998, enacted H.B. 2684, which made a number of changes in statutory requirements relating to the powers, duties, and functions of SBOTA. The Legislative Coordinating Council requested that the Special Committee monitor the implementation of the new law and make any additional recommendations deemed appropriate.

After January 15, 1999, three of the five members will be required to have been "actively practicing" law in Kansas for at least five years. (Prior law required members to be selected with special reference to training and experience for duties imposed by the SBOTA statutes.) All members will be made subject to the Supreme Court Rules of Judicial Conduct applicable to all district court judges. SBOTA will be bound by the doctrine of *stare decisis* to adhere to published decisions of the appellate courts other than district courts. Decisions of SBOTA deemed to be

of sufficient importance also are required to be published. Members are required to complete various courses to assure familiarity with property appraisal theory.

SBOTA is required to appoint, subject to approval by the Governor, an executive director. The executive director, who is required to have familiarity with the tax appeals process, will perform such duties as directed by SBOTA.

All appeals of final actions of SBOTA on property tax exemption cases will move directly to the Court of Appeals. Under prior law, all property tax cases not involving state-assessed valuation issues were appealed to district court.

The Department of Commerce and Housing is required to provide property owners information and assistance sufficient to allow the preparation of proper requests for exemption.

The bill establishes one division within

SBOTA as the Small Claims Division (SCD) as of January 1, 1999. Hearing officers appointed by the executive director will have authority to hear and decide SCD cases. Taxpayers may elect to appeal decisions, findings, orders, or rulings of the Kansas Director of Taxation to the SCD when the amount of tax in controversy does not exceed \$15,000, or, in the case of property tax valuation disputes, when the property in question is single-family residential property or the appraised valuation of the property in question is less than \$2,000,000, except that no cases involving agricultural use value may be considered in the SCD. Taxpayers may elect to skip the local hearing officer step in the appeals process and move directly to the SCD. (The legislation does let counties retain local hearing officers, a provision supported by Sedgwick County.) SCD hearings will be required to be conducted within 60 days after appeals are filed, and hearing officers will be required to render decisions within 30 days of the hearings. Such hearings also will be required to be held in the counties where the property is located or in adjacent counties. Documents provided by taxpayers and county or district attorneys for SCD hearings must be returned and will be considered confidential. Taxpayers appealing to the SCD are not be precluded from appealing subsequently to SBOTA, and all such appeals will be *de novo*. The requirement under prior law that counties with 10,000 or more parcels of real estate appoint local hearing officers also will be repealed. A current requirement that county appraisers during SBOTA hearings are responsible for initiating the production of evidence and demonstrating by a preponderance of evidence the validity of appraisals for certain kinds of property also will be extended to hearings within the SCD.

With respect to locally-granted IRB and EDX property tax exemptions, all such exemptions will be deemed approved unless a hearing will be scheduled by SBOTA within 30 days, and any such hearing is required to be held within 90 days. The amount of time parties seeking exemption have to file motions for SBOTA reconsideration is extended from 15 to 30 days.

To fund the changes imposed by the bill, the

Legislature appropriated an additional \$700,000 to SBOTA for FY 1999 and added 7.0 FTE new positions. The positions consist of an executive director, who is funded for the entire year, and six positions associated with the Small Claims Division, which would begin the second half of the fiscal year (three hearing officers, one computer technician, and two support staff). The appropriation includes start-up costs for the division, funds for computer programming and equipment, and money for other on-going costs.

The requirement that three of the five SBOTA members be "active-practice" attorneys is effective after January 15. The SCD is established as of January 1. All other provisions of the bill were effective July 1.

#### COMMITTEE ACTIVITIES

At the July meeting, the SBOTA Chairman presented a comprehensive review of the features of the new law which were effective July 1 and outlined the timetable for implementation of the other provisions of H.B. 2684. He said that a number of counties had decided to retain hearing officers, and that such a decision meant that there could be a duplicative step in the appeals process which could cause confusion for taxpayers and time problems for county appraisers.

At the September meeting, staff reported that as many as 24 of the 37 counties which had hearing officers in 1998 planned on retaining them in 1999. Also in September, a conferee representing Kansas Chamber of Commerce and Industry testified that the Kansas Tax Coalition, a group which was a proponent of H.B. 2684, wanted to see how the new law would work in 1999 and did not advocate any additional changes involving SBOTA at this time.

#### CONCLUSIONS AND RECOMMENDATIONS

The Committee does not at this time recommend any further changes in statutes relating to SBOTA or the property tax appeals process. The Committee does note that the Legislature may

need to review how the appeals process works in 1999, given the surprising number of counties which have decided to retain locally-appointed hearing officers. Taxpayers in those counties could face a potentially confusing and duplicative

step in the valuation-appeals process (given the new hearing officers appointed by SBOTA pursuant to H.B. 2684), and county appraisers could face significant obstacles in getting the hearings completed within the allotted time.

## LOCAL COUNTY APPRAISERS ISSUES\*

### CONCLUSIONS AND RECOMMENDATIONS

The Committee supports the efforts of the Kansas County Appraisers' Association (KCAA) to clean up and modernize Kansas statutes relating to property tax administration. The Committee therefore recommends introduction of a number of the legislative proposals advocated by the KCAA.

### BACKGROUND

Several property tax administrative issues which were supported by the KCAA were contained in the House-passed version of Board of Tax Appeals' reform legislation during the 1998 Legislature but were not included in the final conference committee version. The Senate Assessment and Taxation Committee recommended those issues for interim study. The broad Legislative Coordinating Council charge to the Committee included those property tax issues as well as any other issues the KCAA wished to bring up for legislative consideration.

### COMMITTEE ACTIVITIES

At the July meeting, the Committee received preliminary testimony from Johnson County Appraiser Paul Welcome representing the KCAA. He indicated that the KCAA would be bringing bill drafts in for the Committee's review in September on a number of topics.

In September, Mr. Welcome returned with ten different proposals. The Committee recommended:

- the introduction of the extension of the physical reinspection cycle for real estate from four to six years;
- allowing counties to place certain comparable sales information on property tax valuation notices;
- a property tax exemption for pickup shells and sailboards;
- returning motor vehicles weighing between 16,000 and 20,000 pounds to the staggered vehicle registration and taxation system pursuant to K.S.A. 79-5101 *et seq.*; and
- allowing counties to file paper plats electronically with registers of deeds.

The Committee postponed consideration of several other topics until the November meeting, including a proposed change in the property tax "grievance" law. The Committee also scheduled follow-up information at the October meeting on proposals relating to watercraft and motorized bicycle registration and taxation.

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\* S.B. 9, S.B. 10, S.B. 11, S.B. 12, S.B. 13, and H.B. 2010 were recommended by the Committee.

After the September meeting, the Kansas Association of Counties (KAC) sent a letter to the Committee indicating that both KAC and KCAA wished to add consideration of a proposal to repeal the sunset on state funding for the "VIPS" system.

In October, the Committee received information from the Property Valuation Division (PVD) on tax and registration laws relating to motorized bicycles. The Committee asked the KCAA to work with PVD and provide additional information in November regarding sample moped taxes in certain counties. Also in October, the Secretary of Wildlife and Parks briefed the Committee on Kansas boat registration laws and statistics.

At the November meeting, Mr. Welcome returned to address the remaining issues. The Committee introduced a bill to make several changes in the property tax grievance statute and

a bill to move motorized bicycles to the motor vehicle tax system with a minimum tax of \$6.

#### CONCLUSIONS AND RECOMMENDATIONS

The Committee recommends the introduction of a number of legislative initiatives advocated by the KCAA, including extension of the physical reinspection cycle for real estate from four to six years; allowing counties to place certain comparable sales information on property tax valuation notices; a property tax exemption for pickup shells and sailboards; clarifying the property tax grievance law; changing the tax treatment of motorized bicycles such that the provisions of the motor vehicle tax statutes would apply (with a minimum tax of \$6); and returning motor vehicles weighing between 16,000 and 20,000 pounds to the staggered vehicle registration and taxation system pursuant to K.S.A. 79-5101 *et seq.*

## OIL AND GAS TAXATION

#### CONCLUSIONS AND RECOMMENDATIONS

The Committee strongly believes the 1999 Legislature needs to provide tax relief for the industry and recommends that the highest priority be given to a proposal to repeal the severance tax on oil and gas. The Committee notes, however, that the entire benefit of such a repeal in the tax on oil would be provided to wells producing more than ten barrels per day. As such, the Legislature is further encouraged to consider the enactment of refundable income tax credits for property taxes paid on certain low-producing oil wells.



## BACKGROUND

The 1998 Legislature enacted a number of changes in tax policy at the request of the oil and gas industry, including enhancement of the severance tax exemption for low-producing wells, elimination of the severance tax on all "incremental production" resulting from certain production enhancement projects, expansion of the property tax exemptions for low producing oil wells, and implementation of income tax credits for costs associated with plugging abandoned wells. But the continuing collapse in the price of oil throughout 1998 began causing severe distress for Kansas oil producers and prompted the Legislative Coordinating Council (LCC) to approve a broad study of oil and gas taxation. Governor Graves in August told the annual convention of the Kansas Independent Oil and Gas Association (KIOGA) that he was pleased the LCC had assigned the topic for study.

## COMMITTEE ACTIVITIES

The Committee held public hearings on oil and gas taxation at the August and September meetings, and heard from KIOGA and a number of industry conferees, as well as the Kansas Corporation Commission. In October, the Committee viewed a short film about the industry and received preliminary information from staff regarding severance tax fiscal notes. In November, staff reviewed the impact of the new revenue estimates and provided additional information about the cost of further increasing the low-production exemption for oil and of totally repealing the severance tax on oil. Staff also provided information about the history of the 1957 severance tax law. The following information about the evolution of oil and gas taxation was provided at the request of the Chair.

### Sales Tax Exemptions (date enacted)

Under K.S.A. 79-3603(a), a retailer's sales tax is imposed on the gross receipts received from the sale of tangible personal property at retail in the state. The following is a list of exempt items relating to oil and gas:

- K.S.A. 79-3606 (w) exempts all sales of natural gas, electricity, heat, and water delivered through mains, lines or pipes for use in the severing of oil (1994).
- K.S.A. 79-3606 (pp) exempts all sales of drill bits and explosives actually utilized in the exploration and production of oil or gas (1988).
- K.S.A. 79-3602 (m) exempts property which is consumed (and not subject to sales tax), including tangible personal property which is essential and necessary to, and which is used in, the actual process of and immediately consumed or dissipated in the mining or drilling of tangible personal property (1971). This exemption would be expanded substantially under the interim committee bill to change "immediately" to "within one year." (Expansion proposed for 1999.)
- Additional proposed exemption in interim sales tax bill for "oil and gas drilling services and supplies, and drilling, pumping, and monitoring equipment, used at a well site or in oil and gas exploration." (Proposed for 1999.)

### Severance Tax Exemptions

Under K.S.A. 79-4217, an excise tax is imposed on the severance and production of coal, oil, and gas in Kansas. The modern severance tax has been in place since 1983. (Note: The severance tax on salt was in effect from 1983-87. The tax on coal still in effect, but exemption expansion in 1987 has substantially reduced revenue.)

### Gas Severance Tax Exemptions (date enacted)

The following are exemptions from the severance tax on gas:

- injected into the earth for the purpose of lifting oil, recycling, or repressuring (1983);
- used for fuel in connection with the operation and development for, or production of, oil or gas in the lease or production unit where severed (1983);
- lawfully vented or flared (1983);

- average daily production during a calendar month having gross value of \$87 or less (1983: \$81; 1998: \$87);
- inadvertently lost due to leaks, blowouts or other accidental losses (1983; clarified in 1992);
- used or consumed for domestic agricultural purposes on the lease or production unit from which it is severed (1983);
- placed in underground storage for recovery at a later date after having been taxed originally in Kansas or originally severed in another state (1983);
- new pool exemption for two years (1983);
- all production from a three-year inactive well for the next ten years (1994); and
- incremental production resulting from certain production enhancement projects (1998).

(Note: Effective gas severance tax rate reduced from 7 percent to 4.33 percent over three years (1994 veto override).)

### Oil Severance Tax Exemptions (date enacted)

The following are the exemptions from the severance tax on oil:

- severed as a result of tertiary recovery process (1983);
- test, frac, or swab oil which is sold or exchanged for value (1983);
- inadvertently lost due to leaks, blowouts, or other accidental losses (1983; clarified in 1992);
- new pool exemption for two years (1983);
- low production exemption: 3 bbls per day or less and 4 or less for water flood (1983-1988);
- all production from a three-year inactive well for the next ten years (1994);
- incremental production resulting from certain production enhancement projects (1998).

#### Oil Low Production Severance Tax Exemptions—1988-1998

<u>Price</u>	<u>Normal Exemption Threshold</u>	<u>Water-Flood Exemption Threshold</u>
Over \$30	3 bbls per day or less	4 bbls per day or less
\$24.01 to \$30	4 bbls per day or less	5 bbls per day or less
\$16.01 to \$24	5 bbls per day or less	6 bbls per day or less
\$10.01 to \$16	6 bbls per day or less	7 bbls per day or less
\$10 or less	7 bbls per day or less	8 bbls per day or less

#### Oil Low Production Several Tax Exemptions (1998)

<u>Price</u>	<u>Normal Exemption Threshold</u>	<u>Water-Flood Exemption Threshold</u>
Over \$16	6 bbls per day or less	7 bbls per day or less
\$15.01 to \$16	7 bbls per day or less	8 bbls per day or less
\$14.01 to \$15	8 bbls per day or less	9 bbls per day or less
\$13.01 to \$14	9 bbls per day or less	10 bbls per day or less
\$13 or less	10 bbls per day or less	10 bbls per day or less

**Property Tax Exemptions and Reduced Assessment Level**

K.S.A. 79-201t (1992, expanded in 1998) exempts low-production oil leases (other than royalty interests) as follows, based on depth:

	<u>1992-1997</u>	<u>1998 Law</u>
Less than 2,000 feet	2 bbls per day or less	3 bbls per day or less
2,000 feet or less	3 bbls per day or less	5 bbls per day or less

Reduced Assessment Level Authorized by Voters in New Classification Amendment, Effective for Tax Year 1993 (all mineral leaseholds had been taxable at 30 percent of fair market value up to that time).

Oil: 5 bbls per day or less—25 percent (other taxable oil property still assessed at 30 percent)

Gas: 100 mcf per day or less—25 percent (other gas property still assessed at 30 percent)

**Income Tax Credit**

In addition to other income tax credits available to the oil and gas industry (job expansion and investment credits), the 1998 Legislature enacted a measure advocated by the oil and gas which allows for certain costs associated with plugging abandoned wells to be claimed as income tax credits.

**CONCLUSIONS AND RECOMMENDATIONS**

The Committee’s concerns about the long-run prospects of the Kansas oil and gas industry have become magnified, especially given the

collapse in the price of oil throughout 1998. The Committee has approved several recommendations (as part of other interim study topics) supported by the industry, including a proposed extension of the sales tax exemption for manufacturing machinery and equipment to include certain oil and gas machinery and equipment; and a proposed constitutional amendment which would allow cities and counties to promote economic development by granting tax abatements to certain oil and gas property.

But the Committee strongly believes that the 1999 Legislature needs to enact additional tax relief to help the beleaguered industry. While the 1999 Legislature is encouraged to consider a broad spectrum of tax policy options which could benefit the industry—including potential severance, property, sales, and income tax reductions. The Committee recommends that the highest priority be given to a proposal to repeal the severance tax on both oil and gas.

The Committee does note that while the severance tax traditionally has been mentioned most often by industry conferees as the best candidate for tax relief, an estimated 70 percent of Kansas oil production will be exempt in FY 2000 pursuant to the low price of oil and the 1998 legislative enhancement of the low-production exemption. As such, the entire benefit of a proposed repeal of the severance tax on oil would be provided to wells producing more than 10 barrels per day. Since the Committee believes that tax relief needs to be targeted to the low-producing wells, the 1999 Legislature is further encouraged to consider as one policy option the enactment of refundable income tax credits for property taxes paid on certain low-producing oil wells.

**PROPOSED CONSTITUTIONAL AMENDMENTS—H.C.R. 5034,  
BOATS AND AIRPLANES, AND H.C.R. 5004,  
OIL AND GAS\***

**CONCLUSIONS AND RECOMMENDATIONS**

The Committee recommends introduction of a constitutional amendment allowing cities and counties to grant economic development property tax exemptions for certain oil and gas property. The Committee makes no recommendation regarding changes in boat taxation.

**BACKGROUND**

During the 1997 Legislature, the House approved H.C.R. 5004 which would expand the purposes for which cities and counties may grant economic development property tax abatements. The House in 1998 also approved H.C.R. 5034 which would authorize the Legislature to provide tax systems for watercraft and aircraft based on something other than fair market value. The Senate did not act on either amendment, and the Legislative Coordinating Council referred both to the Committee for interim study.

**H.C.R. 5004—Economic Development Property Tax Abatements for Oil and Gas.** Article 11, Section 13 of the *Kansas Constitution*, allows cities and counties to exempt from ad valorem taxation for up to ten years all or any portion of the appraised value of buildings, land, and tangible personal property used exclusively by businesses commencing operations for the purposes of manufacturing, research and development, or storing goods sold in interstate commerce. The exemptions or abatements may be granted for similar purposes to facilitate the expansion of existing businesses, provided new employment is created as a result of such expansion.

H.C.R. 5004 would have amended the Constitution to allow the governing body of a city or county to exempt from all or any portion of its

valuation property actually and regularly used in conjunction with the development, exploration, and production of oil and gas.

**H.C.R. 5034—Taxation of Watercraft.** Watercraft (and certain privately-owned aircraft) are assessed as "all other" personal property at 30 percent of fair market value. During public hearings in the House Taxation Committee on H.C.R. 5034 in the 1998 Session, the vast majority of all conferees advocated the proposed constitutional change relative to watercraft and did not address the aircraft issue. Many aircraft are exempt from property taxation because they are antique aircraft (at least 30 years old) or are used exclusively for business purposes.

H.C.R. 5034 would have amended the property tax classification amendment (Article 11, Section 1, of the *Kansas Constitution*) to authorize the Legislature to separately classify and tax aircraft and watercraft on a different basis from other property.

The resolution is not self-executing, and subsequent legislation would have been needed before the taxation of aircraft or watercraft would have been changed.

After a similar legislative authorization for "recreational vehicles" was adopted as part of a constitutional amendment in 1992, the Legislature in 1994 enacted a new tax system (which was

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\* H.C. R. 5002 was recommended by the Committee.

effective January 1, 1995) for such vehicles under which liability is based on the weight and the age of the vehicles (rather than on fair market value).

#### COMMITTEE ACTIVITIES

At the August meeting, staff presented a background memorandum on economic development property tax exemptions. At public hearings in August and September, conferees representing local units of government and the oil and gas industry urged the Committee to introduce a new proposed constitutional amendment to the 1999 Legislature identical to 1997 H.C.R. 5004.

At the September meeting, staff presented data from the Department of Revenue survey regarding county boat and aircraft tax information. In the 85 counties responding to the survey, there is about \$48.6 million of assessed valuation attributable to watercraft and \$5.5 million of property tax liability. Data from 22 of the most populous counties showed about \$8.2 million of assessed valuation for aircraft and \$0.9 million in property taxes.

During the public hearing, also conducted in September, conferees said that Kansas boat taxes were higher than those imposed by surrounding

states. No conferees appeared in support of changing the taxation of aircraft.

In October, the Secretary of Wildlife and Parks presented information regarding Kansas boat registration laws and said that over 100,000 watercraft were registered in Kansas in 1997. Advocates for changing the system of taxation regarding boats told the Committee they were planning on meeting with officials at the Department of Revenue and indicated they hoped to have a proposal for consideration at the November meeting.

In November, proponents said the computer and administrative issues associated with a new boat tax system would be minor.

#### CONCLUSIONS AND RECOMMENDATIONS

The Committee recommends introduction of a new constitutional amendment identical to H.C.R. 5004 and notes that local units of government could encourage additional oil and gas exploration by granting the EDXs.

The Committee makes no recommendation regarding constitutional or statutory changes in boat taxation.

### RETAIL WHEELING—TAX IMPLICATIONS

#### CONCLUSIONS AND RECOMMENDATIONS

The Committee recommends that the 1999 Legislature use the "policy options checklist" developed in this study to help decide how Kansas should best address taxation issues if the state decides to proceed with retail wheeling. The Committee further recommends that the standing tax committees be briefed with these options during the first week of the 1999 Session to determine if any legislation needs to be developed. When tax issues are addressed, the Committee recommends that a flexible tax policy be developed with the potential to be proactive and provide economic development incentives for electricity generation.



## BACKGROUND

The Legislative Coordinating Council (LCC) charged the Special Committee on Assessment and Taxation with investigating the tax implications associated with "retail wheeling"—the direct sale of electricity from a power producer to a retail consumer—believing that potential deregulation of the industry could unleash competitive forces which would demand major changes in state and local tax policy.

### I. Summary Explanation of "Retail Wheeling"

Electric utilities have historically operated as vertically integrated companies that provide "bundled" generation, transmission, and distribution services to their customers. Because electricity is most efficiently produced in very large quantities which can supply a broad geographic area, and because it takes such a huge investment to achieve this scale of production, electric utilities are granted monopoly territories by the state. The prices utilities can charge their customers in these monopoly territories are controlled by state regulators. Regulators have traditionally employed a "cost-of-service" approach to pricing, which allows tax expenses, along with all other reasonable utility costs, to be recovered from "captive" customers in rates.

Over the years, advances in technology have changed the economics of providing electricity, to the point where some believe generation could be competitive. Most continue to believe the "delivery" of electricity, *i.e.*, transmission and distribution, should remain a monopoly. The thinking is that it makes little sense to have more than one wire strung through the neighborhoods and to the home, but it might make sense to allow consumers a choice as to what company will supply them electricity over that wire. "Wheeling" is the term utilities use to describe one utility's transfer over its wires of another utility's power. Wheeling currently occurs every day as utilities buy and sell power among themselves. "Retail wheeling" would occur if the recipient of the "wheeled" power is a retail customer, as opposed to another utility. However, "retail wheeling" could not occur until the Legis-

lature revokes the grant of monopoly territory for the generation portion of utility service. Thus, "retail wheeling" effectively means deregulation of electricity generation. Specifically, deregulation of generation would allow consumers and power marketers to purchase electricity from anyone willing to sell it, including out-of-state generators.

### II. Summary of Main Concerns for Key Stakeholders

A move to competition in electric generation will create numerous tax issues. The issues are highly complex and their resolution will have significant implications for three sets of stakeholders: electricity generators; electricity consumers; and governments, both state and local. Minimizing the tax burden on Kansans and avoiding large tax shifts are among the most important tax policy goals the Legislature must consider before drafting any retail wheeling tax legislation.

**A. Electricity Generators.** The key tax issue for Kansas utilities is a level playing field. Kansas utilities will want to avoid any uniquely high property taxes, franchise fees, and sales tax collection responsibilities, if their out-of-state counterparts will be free from such burdens. Traditionally, utilities have been able to pass any additional tax burden to captive consumers through the ratemaking process, but such costs are likely to drive up the price of electricity and create a competitive disadvantage in an unregulated market.

**B. Electricity Consumers.** Electricity consumers have a stake in clarifying whether the sales tax exemptions for "electricity" will continue to apply to all three services: generation, transmission, and distribution; if these are unbundled. Perhaps more importantly, electricity consumers will want to avoid any tax shifts that may result from deregulation. Any property tax relief for electric generators has the potential to affect all other property tax payments if local jurisdictions raise the mill levy to make up for significant reductions in the electric generation property tax base.

**C. State and Local Government.** State and local governments, in addition to wanting to protect taxpayers from unintended or unreasonable tax shifts, must also be aware of any significant revenue changes that could result from retail wheeling.

### III. Income Tax

**A. General Administration.** K.S.A. 79-32,110 (c) imposes a tax on "every corporation doing business within the state or deriving income from sources within the state." Electric cooperatives and municipal electric companies are not subject to income tax (K.S.A. 79-32,113). If a corporation is doing business solely within Kansas, it will report all of its Kansas-modified federal taxable income on its Kansas return. A multistate corporation must allocate or apportion its income among the states in which it has a sufficient level of business activity or "nexus."

**1. Nexus.** Normally, sufficient nexus for income tax purposes is established when a corporation derives income from sources within the state, owns or leases property located or stored in the state, employs personnel in the state, or has other capital in the state. Nexus can be defined by state statute, but is subject to limitations imposed by the *U.S. Constitution's* due process and commerce clauses, and Public Law No. 86-272. For example, a state is prohibited from taxing a business when the only connection with the state is the solicitation of orders that are sent outside the state for approval or rejection and, if approved, are filled and shipped by the business from a point outside the state (Public Law No. 86-272).

**2. Business vs. Non-Business Income.** To make this allocation or apportionment of income among states in which it has nexus, a multistate corporation must first separate its income into "business" and "non-business" income. "Business" income is defined by K.S.A. 79-3271 as "income arising from transactions and activity in the regular course of the taxpayer's trade or

business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitute integral parts of the taxpayer's regular trade or business operations." A taxpayer may elect to have all income which derives from the acquisition, management, use, or disposition of tangible and intangible property treated as business income. Non-business income is generally allocated 100 percent to the state, while business income is apportioned among the states in which the firm does business and has nexus. (See K.S.A. 79-3275 through 3278 for the determinants of 100 percent allocation.)

**3. Apportionment of Business Income.** K.S.A. 79-3279(b)(1) sets out an equally weighted, three-factor apportionment formula. The three factors are property, payroll and sales. A ratio for each of the three factors is calculated by comparing the level of that factor in Kansas to the level in all states in which that corporation has nexus. If a corporation is doing business in a state, but does not have nexus in that state, that state is not included in the apportionment. When the seller is immune from tax in the destination state, sales of tangible property are considered to be sales of the origination state under a "throwback" provision. Furthermore, K.S.A. 79-3286 treats the sale of tangible personal property as taking place in the state in which the property is delivered, *i.e.*, the destination state. However, K.S.A. 79-3287 treats a service as occurring where the performance of the service, or "the greater proportion of the income producing activity" took place.

The three ratios are then added together and divided by three to determine the percentage of the multistate corporation's income that will be apportioned to Kansas. Railroads, interstate motor carriers, and qualifying telecommunications companies and other qualifying taxpayers have special apportionment rules or options (K.S.A. 79-3279(a), (b)(2) and (b)(3)).

The three-factor formula was adopted in 1963 when, along with 25 other states, Kansas adopted the federal Uniform Division of Income for Tax Purposes Act (UDITPA) which defines business income and establishes a basic methodology of

apportionment. The purpose of UDITPA is to create uniformity among the states in order to avoid either double taxation or less than full taxation of multistate corporations.

As of July 1995, some form of the UDITPA three-factor apportionment formula was in place in more than one-third of the states imposing a corporate income tax. However, approximately a third of those states had adopted a modified three-factor formula under which the sales factor is assigned a greater weight than the payroll or property factors. For example, Iowa, Nebraska, Texas, Colorado, and Missouri all provide a sales factor emphasis in their apportionment formulas (1995 *Multistate Corporate Tax Guide*, Vol. I, Corporate Income Tax, William A. Raabe and Karen J. Boucher (1995) p. I367-I368). Emphasizing the sales factor causes state tax liability to depend less on the relative amount of property and payroll in the state, and more on the relative amount of sales in the state. It thereby reduces the tax liability of export-oriented firms located in the state, and increases the liability of importing firms located outside the state.

**4. Rate.** After Kansas taxable income has been determined through allocation of non-business income and apportionment of business income, a rate is applied. The Kansas corporate tax rate is 4 percent of Kansas taxable income, plus a surcharge of 3.35 percent on income in excess of \$50,000.

**B. Receipts.** In tax year 1996, which is the 1997 processing year, electric utilities paid approximately \$5 million in corporate income tax. This amount is about 2 percent of fiscal year 1997 corporate tax receipts after refunds. The amount does include tax received on nonutility income as well as utility income. Corporate tax receipts are traditionally volatile. For example, electric utilities remitted approximately \$30 million for tax year 1995, and Western Resources announced that during tax year 1997 they would remit, alone, \$60 million.

**C. Issues. 1. Nexus—Effect on State Revenues and Competition.** Retail wheeling could have an indirect effect on state revenues if it

causes significant change in the profitability of utilities with nexus in Kansas or realignment of market share between utilities with Kansas nexus and those without Kansas nexus.

The income tax nexus issue could also affect competition. A direct marketer with no presence in Kansas, who merely solicits sales from outside the state could avoid incurring a Kansas income tax liability. A marketer may sell electricity, solicit business via the U.S. mail, telephone, broadcast advertising, or even the Internet and avoid income tax by delivering the commodity through an unrelated transmission and distribution provider.

**2. Apportionment—Effect on State Revenues and Competition.** The sales factor of the Kansas apportionment formula allocates sales differently depending upon whether they are considered sales of tangible personal property or sales of services. Most states, including Kansas, have not conclusively categorized electricity as one or the other. The answer could have tax liability implications for both Kansas companies apportioning out of Kansas, and out-of-state companies apportioning into Kansas.

If states are inconsistent in their categorization of electricity as either tangible property or a service, utilities may be subject to double taxation, or less than full taxation. For example, if a public utility generates electricity in one state, which characterizes the sale as a service, and then sells the electricity to another state which treats the sale as the sale of tangible personal property, both states would claim the right to count the sale in their apportionment sales factor. If the consumption and production were reversed, the sale would be excluded from the sales factor in both states. This possibility could result in unintended tax consequences and a non-level competitive playing field.

**3. Tax Treatment of Cooperative and Municipal Generators.** Some rural electric cooperatives and municipal generators could have a tax advantage in competition with other generators to the extent they are not required to pay state

income taxes. Municipal generators do not pay local property taxes.

#### IV. Sales and Use Tax

**A. General Administration. 1. Base and Rate State Sales and Use Tax Is Imposed at a Rate of 4.9 percent on Sales of Electricity to Retail Customers.** (K.S.A. 79-3603 (c)). It applies to electricity furnished by both privately owned and municipal utilities.

There are at least five tax exemptions. Four are contained in K.S.A. 79-3606(w) which exempts electricity "delivered through . . . lines"

- to residential consumers,
- for agricultural use,
- for use in severing oil, and
- to properties exempt from property tax under 79-201(b) second through sixth (certain housing for children, handicapped, and the elderly; political subdivisions; and religious institutions, schools, hospitals). K.S.A. 79-3606(n) exempts sales of electricity consumed in the production of tangible personal property. In addition, the retail sales tax is not imposed on wholesale electric sales which are considered sales for resale.

Many city and county governments in Kansas impose a sales tax in addition to the state sales tax. (As of October 1, 1998, 157 cities and 71 counties were imposing sales taxes. Individual city and county rates range from 0.25 percent to 2.0 percent. The highest combined local sales tax rate in the state existed in the City of Delphos, where taxable retail sales were subject to a 1.0 percent city tax and a 2.0 percent (Ottawa) county tax.) Local governments utilize the same tax base as the state and must provide the same exemptions as the state, with two significant exceptions relative to retail wheeling: residential and agricultural electricity sales are both taxed at the local level even though they are exempt at the state level (K.S.A. 12-189a). The tax is applied where the electricity is consumed.

**2. Nexus.** Similarly to the income tax, the state can only impose a duty to collect sales tax

on those vendors with sufficient nexus in Kansas. Again, the state may define nexus in its statutes, and again the due process and commerce clauses of the *U.S. Constitution* create limits on the states ability to find nexus. For example, in *Quill Corp. v. North Dakota*, 504 U.S. 298, 112 S.Ct. 1904 (1992), the U.S. Supreme Court found a company cannot be required to collect and remit sales tax if the company has no connection to the state other than through the U.S. mail or common carrier. However, there are fewer limitations for sales tax purposes than for income tax purposes.

**B. Receipts. 1. State Receipts.** In fiscal year 1997, businesses classified as electric utilities or gas and electric utilities remitted approximately \$23 million in state sales tax. That is approximately 1.8 percent of the \$1.31 billion state sales tax collected in fiscal year 1997.

**2. Local Receipts.** Also in fiscal year 1997, this same utility classification remitted approximately \$18 million in city and county sales taxes. That is approximately 4.6 percent of the \$395 million in total local sales tax collected in fiscal year 1997.

**C. Issues. 1. Clarifications of Exemptions.** Retail wheeling will allow consumers to purchase electricity from one firm and have it distributed/transmitted by another. K.S.A. 79-3603(c) imposes a tax on the "sale or furnishing of . . . electricity which . . . is not otherwise exempt under this act." K.S.A. 79-3606(w) exempts the "sales of . . . electricity . . . delivered through lines . . ." for agriculture, residential, oil production use, and for use on property exempt from property tax. (Emphasis added.) The meaning of the word "furnishing" in the imposition statute is not perfectly clear in the context of retail wheeling. If the intent of the electricity sales exemption statutes was to exempt both types of transactions, generation, and transmission/distribution, the Legislature should clarify that statute.

Likewise, 79-3606(n) exempts "tangible personal property consumed in production." K.S.A. 79-3602(m) defines "property which is consumed"



to include electricity. If the intent was to exempt both the electricity and the distribution/transmission, the Legislature again should clarify the law.

**2. Consistent Taxation of Third Party Transmission and Distribution.** Under current law, unbundled transmission and distribution could be considered a nontaxable service if provided by a third party, unrelated to the generator; but a taxable service if provided by the generator or its affiliate.

This situation arises because sales tax is computed on the "gross receipts from the sale or furnishing of electricity." "Gross receipts" is the "total selling price" which is defined as "the total cost to the consumer . . . including freight and transportation charges." The department would consider transmission and distribution charge components to be part of the total selling price as "freight and transportation charges." Thus, unbundling a bill for services supplied by a single company would not, by itself, change sales tax treatment. However, if the services were functionally unbundled, *i.e.*, supplied by different, unaffiliated companies, there may be issues which need to be addressed. For example, delivery services are not subject to tax. If unbundled transmission or distribution charges were supplied by an unaffiliated third party, these charges may be considered "delivery services" and may not be subject to tax. Electricity generators who supply the full range of services may be at a competitive disadvantage compared to those who supply only the generation component.

**3. Nexus—Effect on Competition and Government Revenues.** Under current case law, it is clear an electric generator located in Kansas, selling to a Kansas consumer, has sufficient nexus to require the collection and remittance of state and local sales tax. Retail wheeling will allow consumers to purchase from out-of-state generators. If those generators do not themselves deliver the power into Kansas, or otherwise establish nexus, the state may not be able to impose the collection requirement. If the sale of electricity is considered the sale of a service, rather than tangible personal property, the Commerce Clause

standard may be met if the service originated or terminated in Kansas and the service is charged to a service address within Kansas (*Goldberg v. Sweet*, 488 U.S. 252 (1989) regarding telecommunications).

In many cases where there is not sufficient nexus for sales tax to apply, the Kansas compensating use tax would apply (K.S.A. 79-3701 *et seq.*). The state compensating use tax is imposed on the consumer for use of a product or service in Kansas in any case where the sale of that product or service would have been subject to sales tax, but for the fact that it did not take place in Kansas. The purpose of the use tax is to level the competitive playing field between in-state and out-of-state suppliers.

There are two reasons why the use tax may not lead to a perfectly level playing field. First, with the exception of motor vehicles and watercraft, there is no city or county use tax. Thus, to the extent local taxes are due on in-state sales, there may still be an advantage for out-of-state suppliers with insufficient nexus. Second, the experience with mail order companies is that not all consumers are aware they owe the use tax and therefore many perceive a price difference where there really is not one. To the extent these nexus issues are similar across the states, the Kansas supplier may have the same advantage in other states that the out-of-state supplier has in Kansas.

If out-of-state generators are not required to collect state use taxes, there could be a reduction in tax revenue to the state. Residential consumers are currently exempt from state sales and use tax, but business consumers would need to be aware that they do owe use tax. Local governments have no authority to impose a use tax on electricity to make up for lost sales tax revenue. However, if the sale is considered a sale of services, it is possible that the service may be considered to be performed in the state and the nexus issues would not arise for either the state or local governments.

**4. Effect of Electricity Price Changes on Government Revenues.** Some observers have



commented that retail wheeling will introduce competition into the generation market and that competition will drive overall electricity prices downward. If that price decrease occurs and does not lead to an offsetting overall increase in electricity consumption, sales tax revenues could decrease.

5. *Effect of Unbundling on Government Revenues.* The current price of electricity includes cost recovery for a generating plant which may in the future be deemed a "stranded investment." Likewise, the cost of providing universal service is currently just another cost of doing business recovered in the electricity bill. As long as these costs continue to be recovered through electricity rates, they may be considered simply part of "gross receipts," and may remain a part of the tax base. However, if these costs are not borne by the generation utility, so the alternative cost recovery method for these components is no longer associated with the taxable sale of electricity, there may be an issue as to whether the charges, on a stand-alone basis, remain subject to sales tax. Also, as mentioned above, the provision of unbundled transmission and distribution by a third party may be a nontaxable service and be removed from the sales tax base where provided on a stand-alone basis by an unaffiliated third party. These changes would impact the local, as well as the state, sales tax base. Metering and billing services may also be exempt if provided on a stand-alone basis.

## V. Property Tax

A. *General Administration.* At its most basic level, determination of property tax due involves three steps: (1) appraisal, (2) determining assessed value, and (3) applying the mill levy. In Kansas, as in most other states steps 1 and 2 are different for public utilities than they are for other commercial and industrial property. Furthermore, public utility valuation requires an additional step between steps 2 and 3. The additional step is the allocation of value to Kansas and to the local taxing jurisdictions.

1. *Determining Value.* Utility property is valued as a "going concern" vs. as a set of individ-

ual assets. The determination of value for most property in Kansas is made by a county appraiser in accordance with K.S.A. 79-501, which references 79-1439, and K.S.A. 79-503a.

- **Real Estate.** K.S.A.'s 79-501 and 79-1439 require residential, commercial and industrial real estate to be appraised at the fair market value of the property. Fair market value is defined as the value which would be arrived at by a willing, informed buyer and a willing, informed seller.
- **Tangible Personal Property.** K.S.A. 79-1439 reflects that commercial and industrial tangible personal property must be appraised in accordance with a formula in the *Kansas Constitution*. The constitutional formula requires appraisal equal to the property's retail cost when new, depreciated over its economic life to a maximum seven-year period. However, so long as the property is used, it is valued at no less than 20 percent of its retail cost when new. Sales tax is not included in the original cost when new, and freight and installation may not be included if those costs are readily discernible. There is an exemption for items which were \$250 or less.

Value for public utilities is determined by the state, rather than the county. The state appraiser follows the requirements of the *Constitution* and of K.S.A. 79-5a04. This statute allows the value of all public utility property, "both real and personal, tangible and intangible" to be determined together as one going concern at its fair market value. As in the case of commercial and industrial (C&I) real property, market value is defined as the price which would be arrived at by a willing, informed buyer and a willing, informed seller.

For C&I real property, market value of each real asset is determined separately. For public utility property, market value of the business will reflect the synergies of all the assets operating together, and will include the contribution of intangible assets, as well as real and tangible personal assets. The unit value of the enterprise

as a going concern may be either more or less than the sum of the value of the individual assets. In most cases you would expect that if each asset were sold separately, the total price received would be less than the value of the enterprise as a going concern.

Three approaches are used to establish market value. There are three well established approaches for determining market value. All three are referenced in the Kansas property tax statutes. For C&I real property, the reference is in K.S.A. 79-503a, and for public utility property the three approaches can be found in K.S.A. 79-5a04. These three approaches are:

- income approach,
- cost approach, and
- market approach.

In the income approach, an appraiser looks at what someone would be willing to pay for the property in light of the amount of income the market is indicating the property is able to produce over the time. Again, for C&I real property, the approach is applied to the single asset and not the company as a whole.

In the cost approach, the appraiser is looking at what it would cost to build a similar property today, less depreciation.

In the sales approach the appraiser looks at what similar properties have recently sold for and makes appropriate adjustments to reflect the subject property. Public utility companies do not sell frequently, so the appraiser looks at stock and debt under this approach.

With public utility valuation, just as with all C&I valuation, the three approaches to value are used by the appraiser to establish a reasonable

estimate of fair market value.

*2. Allocating and Distributing Value.* Because market value is determined for a utility company as a going concern, and not on an asset by asset basis, the state must next determine how much of that final value is allocable to Kansas, if the company is a multistate utility, and then to each taxing jurisdiction within Kansas. The method Kansas has chosen to allocate value to the state and to distribute value to the counties and each county's taxing units is the ratio of original cost to the estimate of market value. This allocation and distribution method can have a significant impact on the amount and shifting of value when companies add or delete significant portions to their operations, merge with other companies, or break up into functional segments.

*3. Applying the Assessment Rate.* The assessment rate for public utility property in Kansas is 33 percent, compared to 25 percent for C&I real and tangible personal property.

*4. Applying the Mill Levy.* Public utility assessed valuation is then subject to the mill levies of the different taxing jurisdictions. Statewide mill levies include the State Institutions Building and Educational Building Funds and the State School District Finance Fund.

## **B. Current Property Tax Revenues**

The following tables provide disaggregated property tax data by type of public utilities; by general versus transmission and distribution (from within electric utility valuation and taxes); and by county (for those with electric generating facilities).

### Public Utilities and Property Taxes

Utility Type	Total 1997 Statewide Assessed Valuation	% Utility is of Total County	Total 1997 General Utility Tax	% Utility Tax Levied of Total County Tax
Electric Utilities	\$ 1,453,091,344	8.0%	\$ 124,496,626	6.3%
Pipeline—Oil and Gas	701,829,855	3.9	71,946,650	3.7
Railroads	166,323,260	0.9	18,956,817	1.0
Telecommunications	579,602,778	3.2	68,713,329	3.5
Water Companies	2,186,910	0.0	276,752	0.0
Barge Lines	24,091	0.0	2,760	0.0
Total—All Utilities	\$ 2,903,058,238	16.0%		14.5%
Total Valuation in Kansas	\$ 18,149,985,463		\$ 1,967,712,703	

### Electric Utilities and Property Taxes

Electric Utility Type	1997 Statewide Assessed Valuation	% Utility Valuation of Total Valuation	1997 Tax Levied on Utilities	% Utility Tax Levied of All Property Tax
Generation Facilities	\$ 864,879,358	4.8%	\$ 70,754,718	3.6%
Other Electric Facilities (Transmission and Distribution)	588,211,986	3.2	53,741,908	2.7
Total—Electric Utilities	\$ 1,453,091,344	8.0%	\$ 124,496,626	6.3%

**ASSESSED VALUATION COMPARISON**  
**Counties with General Facilities**  
**County Totals and Electric Utility**  
**Tax Year 1997**

<u>County Name</u>	<u>County Assessed Valuation (All Property)</u>	<u>All Electric Utility Assessed Value</u>	<u>% All Electric of Total County</u>	<u>Estimated Generation Facilities Value</u>	<u>% Electric Generation of Total County</u>
Barton	\$ 151,842,768	\$ 10,178,108	6.7%	\$ 2,071,967	1.4%
Cherokee	95,971,690	12,829,448	13.4	7,167,414	7.5
Coffey	533,352,716	486,829,796	91.3	464,012,753	87.0
Dickinson	98,495,127	7,231,653	7.3	1,434,891	1.5
Douglas	579,925,927	46,229,382	8.0	25,506,945	4.4
Finney	360,837,049	53,790,790	14.9	44,994,532	12.5
Ford	171,926,151	8,556,705	5.0	2,397,788	1.4
Linn	145,881,201	102,354,455	70.2	89,800,877	61.6
Pottawatomie	308,987,846	216,673,653	70.1	184,260,128	59.6
Reno	355,618,792	24,590,950	6.9	10,258,274	2.9
Sedgwick	\$2,335,445,804	82,534,161	3.5	15,297,262	0.7
Seward	207,866,759	4,831,215	2.3	1,531,043	0.7
Shawnee	955,366,196	54,503,761	5.7	15,030,474	1.6
Washington	44,670,041	2,728,618	6.1	1,115,010	2.5
 Total for 14 Counties	 \$ 6,346,188,067	 \$ 1,113,862,695	 17.6%	 \$ 864,879,358	 13.6%
 Statewide Total	 \$ 18,149,985,463	 \$ 1,453,091,344		 \$ 864,879,358	

**TAXES LEVIED COMPARISON**  
**Counties with General Facilities**  
**County Totals and Electric Utility**  
**Tax Year 1997**

County Name	County Taxes	Electric Utilities Taxes	% All Electric of Total County	Generation Facility Tax (Estimated)	% Generation of Total County Tax
Barton	\$ 20,158,270	\$ 1,317,086	6.5%	\$ 266,465	1.3%
Cherokee	7,954,526	1,028,633	12.9	575,794	7.2
Coffey	33,192,390	29,700,957	89.5	28,281,209	85.2
Dickinson	9,363,704	669,609	7.2	131,353	1.4
Douglas	60,920,799	4,683,928	7.7	2,598,188	4.3
Finney	35,751,479	4,786,367	13.4	3,979,946	11.1
Ford	22,657,501	1,074,985	4.7	300,551	1.3
Linn	11,803,876	8,252,228	69.9	7,233,793	61.3
Pottawatomie	24,851,103	16,246,966	65.4	13,805,487	55.6
Reno	43,477,844	2,887,855	6.6	1,217,790	2.8
Sedgwick	244,220,498	8,525,657	3.5	1,578,952	0.6
Seward	21,437,551	493,560	2.3	158,377	0.7
Shawnee	132,448,235	7,233,356	5.5	2,007,185	1.5
Washington	5,666,568	331,642	5.9	129,715	2.3
<b>Total for 14 Counties</b>	<b>\$ 673,904,343</b>	<b>\$ 87,232,829</b>	<b>12.9%</b>	<b>\$ 62,264,805</b>	<b>9.2%</b>
<b>Statewide Total</b>	<b>\$ 1,967,712,703</b>	<b>\$ 124,496,626</b>	<b>6.3%</b>	<b>\$ 62,264,805</b>	<b>3.2%</b>

C. **Issues.** There may be no immediate impact to property tax as a direct result of retail wheeling. Article 11, Section 1 of the *Constitution* requires public utility property to be assessed at 33 percent of market value. K.S.A. 79-5a01 defines a "public utility" as any company or persons which "control, manage or operate a business of . . . (5) generating, conducting or distributing to, from, through or in this state electric power." Any firm which has a business of generating electric power, whether rate regulated or not, may arguably still fit the definition of "public utility" set out in the statute.

However, there may be an argument to the contrary. In two recent cases, the Kansas courts struggled with the issue of whether the company

was "(3) transmitting to, from or through the state a telephonic message" (K.S.A. 79-5a01). One case dealt with a pager company and the other a cellular company. In both cases the court ultimately found the company was not transmitting telephonic messages and therefore was not a public utility under K.S.A. 79-5a01. However, it is not perfectly clear from the cases the extent to which the courts took into account the fact that neither company was regulated, and how that might affect whether those companies would then come under the natural and ordinary meaning of the term "public utility" as that term is used in the *Constitution*. (*First Page, Inc v. David C. Cunningham, et al.*, 252 Kan. 593; *In re Appeal of Topeka SMSA Ltd., Partnership*, 260 Kan. 155).



In a letter to Representative Holmes, the Kansas Attorney General reiterated that:

"the Legislature may define what is meant by 'public utility . . .' as long as those definitions are consistent with the commonly understood meanings of those terms at the time the current version of Article 11, Section 1 was adopted."

An attached Attorney General Opinion No. 93-142 stated that:

"The term 'public utility' first appeared in article 11, section 1 when the 1985 amendment to that provision was adopted in November of 1986. (citations omitted) In 1985 the term was commonly defined as '[a] private business organization, subject to government regulation, that provides an essential service or commodity, such as water, electricity, transportation, or communication, to the public.' The American Heritage Dictionary 1001 (2d College Ed. 1985). Blacks Law Dictionary defined the term generally as '[a] privately owned and operated business whose services are so essential to the general public as to justify the grant of special franchises for the use of public property or of the right of eminent domain, in consideration of which the owners must serve all persons who apply, without discrimination. It is always a virtual monopoly.' Blacks Law Dictionary 1108 (5th Ed. 1979)."

The differential assessment rates (33 percent versus 25 percent) were adopted by voters in November of 1992.

If the courts were to find that unregulated

electric generation companies cannot be considered "public utilities" for purposes of the property tax statutes, there would be two major changes. First, that electric generation property would no longer be state assessed—it would most likely be valued by the county appraiser on an asset by asset basis with real property set at market value and tangible personal property set in accordance with the constitutional formula. Second, the value would most likely be assessed at the C&I 25 percent rate, compared to the 33 percent public utility rate.

The impact would be a decrease in assessed value, with a revenue impact to the local taxing jurisdictions and the state of an estimated \$25 million. The tax year 1997 state education and building funds revenues would have been reduced approximately \$500,000/year. State revenues would also have been impacted as the tax year 1997 statewide school levy would have been reduced by approximately \$6.75 million.

A change like this would significantly reduce property tax owed by electric generators. Some electric generators have argued such a reduction in property tax liability is important to reducing the overall tax burden on Kansas generators relative to their out-of-state competitors. Of course, any property tax change for electric generators has the potential to affect property tax for other types of property if local jurisdictions raise the mill levy to make up for significant reductions in the electric generation property tax base.

**Difference in Assessment Value and Tax Revenue  
Reduction Electric General Facilities by County**

Location by County	Assessed Value as Utility	Estimated Assessed Value as C&I	% Decrease in Assessed Value	Estimated Decrease in Tax Revenue <sup>a</sup>	Electric Generating Plants
Barton	\$ 2,071,967	\$ 1,298,497	37.33%	\$ (99,472)	Mullergren
Cherokee	7,167,414	3,827,329	46.60	(268,326)	Riverton
Coffey	464,012,753	298,893,872	35.58	(10,065,421)	Wolf Creek
Dickinson	1,434,891	597,155	58.38	(76,688)	Abilene
Douglas	25,506,945	11,740,347	53.97	(1,402,293)	Lawrence
Finney	44,994,532	47,663,139	(5.93)	236,049	Holcomb
Ford	2,397,788	1,533,462	36.05	(108,339)	Judson Large
Linn	89,800,877	43,894,829	51.12	(3,697,450)	La Cygne
Pottawatomie	184,260,128	95,742,350	48.04	(6,641,637)	Jeffery
Reno	10,258,274	4,355,333	57.54	(700,755)	Hutchinson
Sedgwick	15,297,262	7,388,035	51.70	(816,374)	Gills & Evans
Seward	1,531,043	881,876	42.40	(67,152)	Cimarron River
Shawnee	15,030,474	6,953,358	53.74	(1,078,627)	Tecumseh
Washington	1,115,010	547,627	50.89	(66,007)	Clifton
Totals:	\$ 864,879,358	525,317,209	39.26%	\$ (24,852,492)	

- The Decrease in Tax Revenue represents the estimated tax dollars difference between the utility assessment method and the combination method of C&I personal property & market value of real estate. The amount was generated by calculating the actual mill levy paid by the utility company on the generating property times the difference between the two assessments. For example, in Coffey County the mill levy for 1997 was 60.931 mills. The difference of the two assessments is \$165,118,881 (\$464,012,753 - \$298,893,872). The decrease in tax revenue is \$10,065,421 (\$165,118,881 \* 60.931 mills).

**Methodology for Computing the  
Assessment Valuation**

Data for the example was extracted from actual company renditions:

- The assessment of real property is based on 75 percent of the original cost.
- All property is assessed as commercial and industrial.
- Assumes the economic life of the majority of personal property is seven years or more.
- The assessment of personal property is based on using a 30-year life for all personal property. The estimate assumes that 80 percent is seven years or older or is at the end of its economic life.
- The Kansas Supreme Court held that the term "retail cost when new," (a unique term used in the *Constitution* for valuing commercial and industrial machinery and equipment) never includes sales tax and may not include freight and installation costs if these items are separable and readily discernible. This is

contrary to appraisal practices used to determine the market value of property. There are likely considerable installation costs associated with the heavy industrial equipment common to electric generation. The reduction in value due to removing sales tax and installation costs, estimated to be significant, have not been taken into account in calculating this estimate.

- The \$250 small item exemption has not been taken into account in calculating this estimate.

### Policy Options Evaluated by the Committee

The following is a summary checklist of key tax issues which may arise in four major tax types if Kansas allows retail wheeling of electricity. For each issue, options are provided which have been suggested by various conferees. The four major tax types and their key issues are:

- Sales and use tax
  - Nexus
  - Unbundling
- Income tax
  - Nexus
  - Apportionment
  - Generation Cooperatives
- Property tax
  - Market value determination
  - Assessment rate
  - Replacement revenue
  - Municipal Generators
- Franchise fees
  - Franchise fee base erosion

#### Sales Tax

##### 1. Nexus. Out-of-state sellers:

- will not be required to collect Kansas use tax if they do not have nexus in Kansas, and

- will not be required to collect local use tax under any circumstances because there is no local use tax on electricity sales.

A company cannot be required to collect and remit use tax if it has no connection to the state other than through the U.S. mail or a common carrier. (See *Quill Corp. v. North Dakota*, 504 U.S. 298, 112 S.Ct. 1904 (1992)). Thus, an out-of-state generation company which has no people or property in Kansas, and which simply transmits power to its Kansas customers using third-party transmission and distribution, may not be required to collect Kansas use tax. This could create revenue reductions for state and local governments, and competitive problems for in-state generators.

**Option A.** Deem the distributor to be the "retailer" for purposes of collection of the sales and use taxes. This would essentially shift the state use tax collection responsibility to an entity which will certainly have nexus because the nature of its business requires it to have property in the state. To require the distributor to also collect local taxes will require enactment of a local use tax on electricity. Consideration: Out-of-state generators will be required to supply proprietary business information (customer names and negotiated price of electricity) to distribution companies which may be affiliated with their generation competitors.

**Option B.** Rely on the fact that all generators may be required to maintain in-state offices for purposes of public health and safety. This would essentially require out-of-state generators to have property in Kansas, which may have the indirect effect of giving them nexus for tax purposes. To require these out-of-state firms to also collect local tax will require the enactment of a local use tax on electricity. Consideration: Whether requiring an in-state office for health and safety purposes creates nexus for tax purposes is currently subject to a court challenge in another state.

**Option C.** Deem the generation of electricity to be the provision of a service that is performed where the electricity is delivered. The U.S. Supreme Court concluded that a state may

claim nexus on the provision of a service where the service originated or terminated in the taxing state and the service is charged to a service address in that state (*Goldberg v. Sweet*, 488 U.S. 252 (1989) regarding telecommunications services; see also *Oklahoma Tax Commission v. Jefferson Lines Inc.*, S.Ct. 1331 (1995) regarding bus service). If electricity is considered a service performed in the state, the state and local sales taxes would apply and could be required to be collected. Considerations:

- There would be no need to enact a local use tax on electricity.
- If the Legislature deems electricity to be a service for sales tax purposes, it should probably do the same for income tax apportionment formula purposes to be consistent.

**Option D.** Eliminate the sales tax on electricity and create a new, replacement tax per unit of electricity delivered to be collected by distributors. The tax could be set to replace both state and local sales tax revenues (with a distribution back formula for local governments) and would be collected regardless of whether the electricity distributed is from an in-state or out-of-state firm. Consideration: Administratively, the creation of a new tax can be very complicated.

**Option E.** Make no changes in the law. While we could not require out-of-state generators to collect the use tax, the law does require Kansas consumers to pay it. Because we would mainly be dealing with commercial customers (residential customers are exempt) there would be a fairly high awareness of the need to pay this tax. Considerations:

- Compliance may be uneven, which results in an unfair burden for those who do pay.
- There is no local use tax required to be paid on electricity sales, and because residential customers are not exempt from the local sales, this could cause a large revenue loss for local governments.

2. **Unbundling.** It is not clear that sales tax would apply to unbundled third party transmission and distribution services.

"Gross receipts" are defined as the "total selling price" which is defined as "the total cost to the consumer . . . including freight and transportation charges." On the other hand, tax is not imposed on stand alone delivery services when provided by an unaffiliated third party. Thus, functionally unbundled transmission and distribution services, offered separately from the purchase of electricity, may be considered "delivery" services and may no longer be subject to tax (K.S.A. 79-3602 (g) and (h)).

**Option A.** Clarify that K.S.A. 79-3603(c) imposes a sales tax on electricity distribution and transmission by imposing a tax on the "sale and furnishing . . ." of electricity. Likewise, clarify that where there is a current exemption for particular types of electricity consumption, the exemption is also intended to apply to all three functions. The sales tax exemptions for electricity consumption currently exempt the "sales of . . . electricity . . . delivered through lines . . ." (K.S.A. 79-3606(w)). K.S.A. 12-189a, imposing local sales tax on "sales" of electricity should also be clarified. Considerations: Clarifying that transmission and distribution of electricity will remain taxable even if they are provided by unaffiliated third parties will ensure a level playing field for integrated and nonintegrated utilities.

**Option B.** Clarify that K.S.A. 79-3603(c) does not impose a sales tax on transmission and distribution of electricity when provided by an unaffiliated third party by removing the reference to "furnishing" of electricity. The exemption statutes would not need to be changed. Considerations: According to K.S.A. 79-3602(g) and (h), these services would be taxed inconsistently in a manner that might give an advantage to unaffiliated third-party generators. Transmission and distribution would be subject to tax if they are provided together with generation from the same, or an affiliated, firm. They would be exempt if the generation being delivered is coming from an unaffiliated firm.

## Income Tax

1. **Nexus.** Out-of-state electricity generators may not be subject to Kansas income tax if they do not have nexus for income tax purposes.

Generally, a state may only tax a business if the business has property or personnel in the state. In addition, a state is prohibited from taxing a business which sells tangible personal property, even if there are personnel in the state, when the personnel are only soliciting orders that are sent outside the state for approval or rejection and, if approved, are filled and shipped by common carrier from outside the state. Public Law 86-272.

This issue exists today because out-of-state electricity providers currently make wholesale sales into Kansas. But the issue could grow as the magnitude of interstate electricity sales grow with retail wheeling. Eventually, this could create revenue reductions for the state and competitive problems for in-state generators.

**Options:** The options are the same as those listed for the nexus issue under sales tax.

2. **Apportionment.** It is not clear whether electricity is tangible personal property or the provision of a service for purposes of income tax apportionment.

The sales factor portion of the three-factor apportionment formula treats the sale of tangible personal property as taking place in the state where the property is delivered. However, a service occurs where the performance of the service, or "the greater proportion of the income producing activity," takes place. (K.S.A. 79-3286 and 3287.)

**Option A.** Clarify that generated electricity will be considered tangible personal property. Considerations: The determination should probably be consistent with the sales tax determination.

**Option B.** Clarify that generation of electricity will be considered the provision of a service. Considerations: Same as Option A above.

3. **Cooperatives.** Generation Cooperatives are exempt from Kansas income tax.

## Property Tax

1. **Market Value Determination.** Fair market value for "public utility" property is determined by the state for the total utility company as a going concern, rather than by the Counties as separate pieces of real and personal property.

The state determines the value of all public utility property, both real and personal, tangible and intangible, together as one going concern. In contrast, the counties determine the fair market value of each piece of a C&I firm's real property separately, on an asset-by-asset basis. Each piece of a C&I firm's personal property is valued separately by the county according to a formula. Sales tax, freight, and installation costs are not included in the C&I valuation of personal property. Inventories are exempt under the C&I calculation. For these reasons, the C&I method of valuation will usually produce a lower value for a firm's property than the public utility "unit value" approach.

**Option A.** Continue to have the state value electric generation property as "public utility" property, even under retail wheeling. Considerations: The courts may find that the term "public utility," as it is used in the *Kansas Constitution*, only applies to regulated monopolies.

**Option B.** Change the valuation methodology for electric generation property to the regular C&I method, carried out by the counties. Considerations:

- A good portion of public utility property crosses county, and even state, lines.
- Because the total value of any given public utility is likely to decrease under the C&I methodology, county revenue reductions and/or tax shifts may occur. The state may also experience a revenue loss. Revenue replacement may be an issue.



- If electric generation is valued as C&I property, but transmission and distribution continue to be valued as public utility property, a method must be developed to separate these types of property and their values.

**2. Assessment Rate.** "Public utility" property is assessed at 33 percent of its fair market value, compared to a 25 percent assessment rate for other commercial and industrial property.

The *Kansas Constitution* sets the assessment rate for public utility property at 33 percent, the highest for any Kansas property. The Kansas statutes define the constitutional term "public utility" to include "any company . . . which . . . operates a business of . . . (5) generating . . . in this state electric power."

**Option A.** Do not amend the *Constitution* and maintain the 33 percent assessment rate for electric generation property. Consideration: Unless the *Kansas Constitution* is amended, the courts may find that the term "public utility," as it is currently used in the *Constitution*, only applies to regulated monopolies.

**Option B.** Amend the *Constitution* to remove unregulated electric generators from the public utility assessment level and reassess their property at 25 percent, rather than 33 percent of value. Consideration:

- Fourteen counties with high concentrations of utility property would be exposed to significant revenue loss and/or tax shifts. The state would also suffer some revenue loss. Therefore, revenue replacement may be an issue.
- If electric generation is valued at a 25 percent rate, but transmission and distribution continue to be valued at a 33 percent rate, a method must be developed to separate these types of property and their values.
- Voter adoption of a constitutional amendment is by no means guaranteed.

**Option C.** Amend the statute to redefine "public utility" for the purpose of disaggregating

the property of unregulated electric generators from other public utility property subject to the higher assessment level. Considerations:

- Same as Option B above, except voter approval would not be required.
- Statutory action could be subject to legal challenge.

**Option D.** Amend the *Constitution* to give the Legislature the flexibility to establish the assessment level on electric generation property as part of any proposed statutory measure designed to implement retail wheeling in Kansas. Considerations: Same as Option B above.

**Replacement Revenue.** If electric generators are valued as C&I property, rather than public utility property, 14 Kansas counties with concentrations of generation property may experience revenue loss and/or tax shifts.

If electric generators are valued as C&I property, rather than public utility property, and the local mill rate is not adjusted, the estimated revenue loss to local government is approximately \$25 million.

**Option A.** Do not replace revenue. Consideration: Significant tax shifts among local property taxpayers will likely occur.

**Option B.** Allow phased-out revenue replacement from the State General Fund.

**Option C.** Create a new local option tax, or a new state tax with a distribution back to local governments. For example, the tax could be based on units of electricity distributed.

**3. Municipal Generators.** Municipal generators are not subject to property tax.

## Franchise Fees

**1. Franchise Fee Base Erosion.** Most franchise fees charged by cities to the franchise holders are based on a percentage of the gross

receipts received from the sale of electricity within the city's corporate limits. Retail wheeling could decrease the amount of electricity sold by these franchise holders, thus reducing the gross receipts and the amount of franchise fee due to the city. Franchise fees are a significant revenue source for cities.

**Option A.** Cities can include provisions in their franchise agreements as they are renewed. Considerations: Most agreements are long-term contracts which may not be due for renegotiation for several years.

**Option B.** Impose a duty on the franchisee to remit a fee based on its distribution of electricity. Consideration: The distribution company be able to recover these fees easily if the alternative electricity supplier is doing its own billing.

**Option C.** Amend K.S.A. 12-194 to authorize cities to impose surcharges or fees for the "furnishing, delivery or distribution of electricity or gas service within the corporate limits of the city."

**Option D.** Statutorily authorize cities to renegotiate existing agreements.

#### COMMITTEE ACTIVITIES

At the July meeting, the Committee received briefings on a number of tax issues from the Department of Revenue and from Western Resources. Staff in August provided information regarding city and county local sales taxes. Matthew Brown from NCSL then outlined retail wheeling tax actions taken in other states, and the Committee began holding public hearings. Staff was instructed to prepare a "policy options checklist." In September, the Department of Revenue presented information comparing Kansas state and local tax structure with the tax structure in other states using a "hypothetical

firm" model. In October, staff presented the "policy options checklist" and the public hearings were reopened to give conferees a chance to react to that document. Staff presented a revised checklist at the November meeting, and the Committee made its final recommendations.

#### CONCLUSIONS AND RECOMMENDATIONS

The Committee provides these policy options to the 1999 Legislature as a valuable resource document to help decide how Kansas should best address taxation issues if the state decides to proceed with retail wheeling. The Committee recommends that the standing tax committees be briefed with these options during the first week of the 1999 session to determine if any legislation needs to be developed.

The Committee believes that the Legislature should continue to make preparations to address the broad spectrum of issues associated with retail wheeling and encourages the taxation and utility committees to work together so that the tax issues are not considered in isolation.

When tax issues are addressed, the Committee recommends that a flexible tax policy be developed with the potential to be proactive and provide economic development incentives for electricity generation. The Committee believes that Kansas is well positioned geographically to be an exporter of electricity.

If retail wheeling tax issues are not addressed during the 1999 Legislature, the Committee strongly believes that another interim study would be warranted during the summer and fall of 1999 to monitor all relevant actions of other states and the federal government, update the policy options, continue educating policymakers and the public, and begin drafting whatever statutory and constitutional changes are necessary.

KANSAS HOUSE OF REPRESENTATIVES  
COMMITTEE ON TAXATION

1. In any case where committee rules do not apply, House Rules shall govern. All powers, duties and responsibilities not addressed herein are reserved to the chair.
2. The chair shall determine the committee agenda, including scheduling and the order of business.
3. The chair reserves the right to limit testimony that is cumulative in nature and may limit testimony, when necessary, to a specific number of minutes.
4. The chair reserves the right to limit questioning of conferees by committee members in the interest of time and in the interest of fairness to conferees and other committee members. Committee members shall address conferees only when recognized by the chair.
5. Committee members shall not be approached during committee hearings or deliberations by anyone other than fellow legislative members or legislative staff.
6. No conferee shall be interrupted during presentations of their testimony, except with the permission of the chair.
7. Questioning of a conferee shall be limited to the subject matter of the agenda item for the day, except as may otherwise be allowed by the chair.
8. No bill or resolution shall be taken up for a committee vote unless it is announced by the chair.
9. Amendments to motions are in order with permission of the committee member making the motion to be amended.
10. A substitute motion is in order, but no additional substitute motion shall be in order until the prior substitute motion is disposed of.
11. A motion requires a second to be in order.
12. A motion to table or take from the table shall be in order only when such item is on the agenda or is taken up by the chair. The motion requires a simple majority and is, unless otherwise determined by the chair, non-debatable.
13. There shall be no recording, audible, photographically or otherwise, of committee meetings, except by the committee secretary, without permission of the chair.
14. A request from any member that their own vote be recorded shall be granted.
15. Granting excused absences is reserved by the chair.
16. The chair reserves the right to take such action as may be necessary to prevent disruptive behavior in the committee room during the hearings and deliberations.
17. Adjournment is reserved to the chair.

*HOUSE TAXATION  
1-14-99  
ATTACHMENT 3*

NOTICE TO CONFEREES ON TAXATION  
HOUSE COMMITTEE ON TAXATION

It is the policy of the House Committee on Taxation to ensure and promote free and open discussion of matters coming before the Committee. Because of the important issues that are to be discussed certain rules are necessary. Just as there are rules relating to the conduct of committee business when matters are debated among committee members, the following rules apply to the hearing process itself. Any questions about these rules should be directed to the committee chair.

By appearing before the Committee each conferee is presumed to have read the attached rules and to have agreed to be bound by said rules.

We thank you for your understanding of, and compliance with, these rules.

RULES FOR CONFEREES APPEARING BEFORE THE  
HOUSE TAXATION COMMITTEE

1. The chair shall determine the committee agenda, including scheduling and the order of business.
2. The chair requests that individuals wishing to appear and provide verbal testimony before the committee notify the committee secretary at least 24 hours in advance of the hearing.
3. Testimony must be in written form and 40 copies made available to staff prior to testifying.
4. Conferees shall introduce themselves, identify on whose behalf they appear, identify whether they appear as an opponent, proponent or interested neutral party and shall, as briefly as possible, state the reasons for their position. If suggestions for amendment(s) are to be offered, a proposed draft of the amendment(s) should be included in the written testimony.
5. When the conferee is, or represents, the sponsor of the measure under consideration, the conferee is responsible for briefing the committee on the specific provisions of the legislation, section by section, where necessary.
6. Conferees shall address their remarks during testimony to committee members and staff only.
7. Where the number of hearings and/or conferees scheduled warrant time limitations, the Chair may limit testimony to a specific number of minutes. The Chair reserves the right to limit testimony that is cumulative in nature.
8. Testimony shall relate to the subject matter of the measure under consideration. Conferees testifying on unrelated subjects will cause the chair to terminate that conferee's testimony.
9. While the taking of testimony in committee is not preceded with the formality of an oath, by appearing before the committee every conferee hereby certifies that his or her testimony is truthful, based upon facts that are capable of verification and offered in good faith. Conferees shall bring to the committee's attention any qualifications or corrections to their testimony.
10. The chair reserves the right to take such action as may be necessary to prevent disruptive behavior in the committee room during hearings and deliberation.
11. The committee reserves the right to take such action as may be necessary when a violation of the previous rule is suspected.
12. Cellular phones and audible pagers, as well as television and video cameras, are accepted with advance permission of the committee chair. Pagers or cellular phones with audible features which are activated during committee proceedings shall be surrendered to the chair for the balance of any such meeting.
13. Committee members shall not be approached during committee hearings or deliberation by anyone other than fellow legislative members or legislative staff.
14. There shall be no recording, audibly, photographically or otherwise, of committee voting except by the committee secretary.

*HOUSE TAXATION  
1-14-99  
Attachment 4*