Approved: February 23, 1999
Date

MINUTES OF THE HOUSE COMMITTEE ON TAXATION:

The meeting was called to order by Chairperson David Adkins at 9:00 a.m. on January 20, 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:
Mike Armstrong, Johnson County Water District #1
Robert Hall, CAS Construction, Topeka
Mike Taylor, City of Wichita
Don Seifert, City of Olathe
Dennis Schwartz, Kansas Rural Water
Chris McKenzie, League of Kansas Municipalities
Shirley Sicilian, Dir. Of Policy and Research, KDOR
Robert Krehbiel, Kansas Independent Oil & Gas Assn.
Nick Powell, COLT Engineering
Natalie Bright, Kansas Chamber of Commerce & Industry
Bernie Koch, Wichita Chamber of Commerce
Bill Barnes, Kansa Corporation of Emporia
Frank Meyer, Custom Metal Fabricators of Herington
David Mauersberger, Superior Industries of Pittsburg
Dennis D'Orvillies, Goodyear of Topeka
Doug Wareham, Kansas Grain and Feed
Bob Leake, Allen, Gibbs & Houlik, P.C., of Wichita
Woody Moses, Kansas Ready Mix Association
Tom Whitaker, Kansas Motor Carriers Association
Shawn Herrick, Mid-America Tire Dealers Assn. (written)
Bob Vancrum, Greater Kansas City Chamber of Commerce (written)

Others attending: See attached list.

The Chairman opened the public hearing on:

HB 2011 - Water district purchases sales tax exempt

The Chairman introduced April Holman of the Legislative Research Department who gave a Staff briefing on **HB 2011**.

Proponents:

The Chairman introduced Mike Armstrong, Proponent, Director, Legal/Auditing, Johnson County Water District #1 (Attachment 1). Mr. Armstrong mentioned for the purposes of clarifying the bill for the District's purposes, a couple of changes were suggested and are listed on a balloon version of the bill attached to his testimony.

The Chairman introduced Robert Hall, Proponent, CPA and Treasurer of CAS Construction, Inc. of Topeka (Attachment 2).

MINUTES OF THE HOUSE COMMITTEE ON TAXATION, Room 519-S Statehouse, at 9:00 a.m. on January 20, 1999.

The Chairman introduced Mike Taylor, Proponent, Government Relations Director for the City of Wichita (Attachment 3).

The Chairman introduced Don Seifert, Proponent, of the City of Olathe (Attachment 4).

The Chairman introduced Dennis Schwartz, Proponent, currently President of the Kansas Rural Water Association and also General Manager of Rural Water District Number 8 in Shawnee County (Attachment 5). Mr Schwartz suggested an amendment to the introduced bill to also extend this clarification to the public wholesale water supply districts formed under KSA 19-3545 inasmuch as they are essentially a similar utility to a rural water district which was listed in his testimony.

The Chairman introduced Chris McKenzie, Proponent, Executive Director, League of Kansas Municipalities (Attachment 6).

The Chairman closed the public hearing on **HB 2011**.

The Chairman opened the public hearing on:

HB 2009 - Sales tax exemption for business machinery and equipment.

The Chairman introduced April Holman of the Legislative Research Department who gave a Staff briefing on **HB 2009**.

The Chairman introduced Shirley Sicilian, Director of Policy and Research for the Kansas Department of Revenue who presented additional information regarding **HB 2009** (Attachment 7).

Proponents:

The Chairman introduced Robert Krehbiel, Proponent, Executive Vice President, Kansas Independent Oil and Gas Association (Attachment 8). Mr. Krehbiel introduced six representative letters to enter on record that illustrate the condition of the crude oil industry and the price crisis (Attachment 9), with the Chairman's permission.

The Chairman introduced Nick Powell, Proponent, President of COLT Engineering (Attachment 10).

The Chairman introduced Natalie Bright, Proponent, Director of Taxation and Small Businesses, Kansas Chamber of Commerce and Industry (Attachment 11).

The Chairman introduced Bernie Koch, Proponent, Vice President of Governmental Affairs, Wichita Chamber of Commerce (Attachment 12).

The Chairman introduced Bill Barnes, Proponent, President of the Kansa Corporation of Emporia (Attachment 13).

The Chairman introduced Frank Meyer, Proponent, President, Custom Metal Fabricators of Herington (Attachment 14).

The Chairman introduced David Mauersberger, Proponent, Controller, Superior Industries of Pittsburg (Attachment 15).

The Chairman introduced Dennis D'Orvillies, Proponent, Engineering Technology Leader for Goodyear's Plant in Topeka (Attachment 16).

The Chairman introduced Doug Wareham, Proponent, Vice President of Governmental Affairs, Kansas Grain and Feed (Attachment 17).

MINUTES OF THE HOUSE COMMITTEE ON TAXATION, Room 519-S Statehouse, at 9:00 a.m. on January 20, 1999.

The Chairman introduced Bob Leake, Proponent, Managing Consultant, Allen, Gibbs & Houlik, P.C., of Wichita (Attachment 18).

The Chairman introduced Woody Moses, Proponent, President, Kansas Ready Mix Association (Attachment 19). Mr. Moses suggested a balloon amendment that would add additional language on page 17 of the bill which was attached to his testimony.

The Chairman introduced Tom Whitaker, Proponent, Director of Government Relations, Kansas Motor Carriers Association (Attachment 20). Mr. Whitaker suggests an amendment, listed in his testimony.

Written testimony:

Bob Vancrum, Proponent, Greater Kansas City Chamber of Commerce submitted written testimony (Attachment 21).

Shawn Herrick, Proponent, Mid-America Tire Dealers Association, submitted written testimony (Attachment 22).

The Chairman closed the public hearing on **HB 2009**.

The meeting adjourned at 10:45 a.m.

The next meeting is scheduled for January 21, 1999.

HOUSE TAXATION COMMITTEE
GUEST LIST
DATE: Jan. 20, 1999

Dennis Schwartz	Ks Rural Water Assoc
ROBERT HALL	CAS CONSTRUCTION, INC
ROBERT LEAKE	ALLEN, GIBBS & HOULIK, L.C.
Chris McKenzie	League of Ks. Municipalities
Joe Dick	BPU KCK
Tom Whitaker	Ks Motor Carriers Assn
J.P. SMALL	KOCH INDUSTRIES / LEARJET
Jack Glaves	Duke Energy & KN Energy
Bernie Koch	Wichita Area Chamber of Commerce
Marci Ross	Sedgwick County
Rich McKee	KS Livestock Assoc.
Doug Wareham	Ks. Grain & Feed Assn.
Dave Holthaus	Western Resources
Bert Hubbell	Anadarko
[illegible] Peterson	Ks Taxpayers Network
DAVID L. ROSS	COMMERCE & HOUSING
DON SNODGRASS	KS FOOD DEALERS ASSOC
Jackie Clark	Hallmark Cards Inc
Jeff White	City of Topeka

HOUSE TAXATION COMMITTEE
GUEST LIST
DATE: WED - 1-20-99

Doug Smith	City of Topeka
Larry Kleeman	League of KS Municipalities
Leslie Kaufman	Ks Farm Bureau
Jim Kaup	City of Topeka, City of Garden City
Christy Caldwell	Topeka Chamber of Comm.
Dennis D'Ouvilliers	Goodyear
Ashley Sherard	Overland Park Chamber
Jenny Unruh	Greater Kansas City Chamber of Commerce
Bob Totten	Ks Contractors Association
TOM PALACE	PMCA OF KANSAS
Shawn Herrick	MATDA
Julie Hein	Hein and Weir, Chtd.
Julie Stroud	Arthur Andersen
LAURIE KRAUSE	WD #1 of Jo. Co.
Larry Rosenow	WD#1 of Jo Co
Don Seifert	City of Olathe
Ron Appletoft	Water District No 1 of Jo. Co.
SCOTT SCHNEIDER	McGILL, GAUCHER & ASSOC.
Lee Eisenhauer	Propane Marketers Assn of KS

HOUSE TAXATION COMMITTEE
GUEST LIST
DATE: 1-20-99 WED

Tom Bruno	Allen & Assoc.
Bill Lauree	BOEING
John Frederick	Boeing
Natalie Bright	KCCI
E.C. "Woody" Moses	KRMCA
Wendy M. Harms	KRMCA
Kelly Kultala	City of Overland Park
MIKE ARMSTRONG	WATER DISTRICT No 1
SHANNON GREEN	Kansas City Power & Light Co.
Don Schnacke	KIOGA
Robert E Krehbiel	Kans Independent Oil + Gas Assoc
NICHOLAS K. POWELL	COLT ENERGY, INC.
DAVID MAUERSBERGER	SUPERIOR INDUSTRIES.
Frank Meyer	custom metal Fab
Bill BARNES	BALDWIN KANSA
Tom Hatted	KDR
S. Sicilian	K D of Revenue
Peggy Long	Legislator

WATER DISTRICT NO.1 OF JOHNSON COUNTY

Mailing Address: P.O. Box 2921, Mission, KS. 66202
5930 Beverly, Mission, Kansas 66202

Tel. (913) 895-5500
FAX (913) 895-1825

Testimony On House Bill 2011

Presented at the
House Committee On Taxation
On January 20, 1999

Water District No. 1 of Johnson County appears in support of House Bill 2011 which would exempt publicly owned water utilities, including Water District No. 1, from sales tax on purchases of property and services used in the construction, operation and maintenance of publicly owned water utilities.

Water District No. 1 is organized as a regional public water utility and serves over 330,000 consumers in and around Johnson County. The Water District is operated as a quasi-municipal corporation pursuant to K.S.A. 19-3501 et seq.

In recent decades, providing water to the public has increasingly become a governmental function and should be exempt from sales tax similar to other governmental services. The Water District pays approximately $500,000.00 in sales tax per year. If the Water District was exempt from this tax burden, its operational costs could be reduced, which would have a beneficial impact on water rates.

Current sales tax law, as applied to publicly owned water utilities, contains a number of very confusing exemptions which cause a significant administrative burden and increased operating costs. The Water District has been forced to file several appeals challenging the Department of Revenue's application of the sales tax laws to the District. It is our understanding that many other publicly owned water utilities have also challenged the Department's interpretations on this issue. Current Department of Revenue interpretations require the creation of very intricate bidding documents for construction projects. It is suspected that these provisions confuse contractors and cause the costs of publicly bid contracts to be inflated. A total exemption of sales tax for publicly owned water utilities would solve all of these problems.

For the purpose of clarifying this bill, it is suggested that the term "funds", which is defined on lines 28 through 30 of page 2, be expanded to include "all other types of revenues", and that the word "construction" be inserted prior to the word "operation" in line 14 on page 6.

Water District No. 1 urges your support of House Bill 2011. By lowering operating costs and simplifying administration of publicly owned water utilities, the public would be benefited statewide.

House Taxation
1-20-99
Attachment 1

1-8

a public or private elementary or secondary school or public or private nonprofit educational institution and used primarily by such school or institution for nonsectarian programs and activities provided or sponsored by such school or institution or in the erection, repair or enlargement of buildings to be used for such purposes. The exemption herein provided shall not apply to erection, construction, repair, enlargement or equipment of buildings used primarily for human habitation;

(d) all sales of tangible personal property or services purchased by a contractor for the purpose of constructing, equipping, reconstructing, maintaining, repairing, enlarging, furnishing or remodeling facilities for any public or private nonprofit hospital or public hospital authority, public or private elementary or secondary school or a public or private nonprofit educational institution, which would be exempt from taxation under the provisions of this act if purchased directly by such hospital or public hospital authority, school or educational institution; and all sales of tangible personal property or services purchased by a contractor for the purpose of constructing, equipping, reconstructing, maintaining, repairing, enlarging, furnishing or remodeling facilities for any political subdivision of the state *or district described in subsection (s)*, the total cost of which is paid from funds of such political subdivision *or district* and which would be exempt from taxation under the provisions of this act if purchased directly by such political subdivision *or district*. Nothing in this subsection or in the provisions of K.S.A. 12-3418 and amendments thereto, shall be deemed to exempt the purchase of any construction machinery, equipment or tools used in the constructing, equipping, reconstructing, maintaining, repairing, enlarging, furnishing or remodeling facilities for any political subdivision of the state *or any such district*. As used in this subsection, K.S.A. 12-3418 and 79-3640, and amendments thereto, "funds of a political subdivision *or district*" shall mean general tax revenues, the proceeds of any bonds and gifts or grants-in-aid. Gifts shall not mean funds used for the purpose of constructing, equipping, reconstructing, repairing, enlarging, furnishing or remodeling facilities which are to be leased to the donor. When any political subdivision of the state, *district described in subsection (s)*, public or private nonprofit hospital or public hospital authority, public or private elementary or secondary school or public or private nonprofit educational institution shall contract for the purpose of constructing, equipping, reconstructing, maintaining, repairing, enlarging, furnishing or remodeling facilities, it shall obtain from the state and furnish to the contractor an exemption certificate for the project involved, and the contractor may purchase materials for incorporation in such project. The contractor shall furnish the number of such certificate to all suppliers from whom such purchases are made, and such suppliers shall execute invoices covering the same bearing the number of such

all other types of revenues,

1-3

ment used to replace or substitute for any missing part of the body; used to alleviate the malfunction of any part of the body; or used to assist any disabled person in leading a normal life by facilitating such person's mobility; such term shall include accessories attached or to be attached to motor vehicles, but such term shall not include motor vehicles or personal property which when installed becomes a fixture to real property;

(s) all sales of tangible personal property or services purchased directly by a groundwater management district organized or operating under the authority of K.S.A. 82a-1020 *et seq.* and amendments thereto, *by a rural water district organized or operating under the authority of K.S.A. 82a-612, and amendments thereto, or by a water supply district organized or operating under authority of K.S.A. 19-3501 et seq.*, and amendments thereto, or K.S.A. 19-3522 *et seq.*, and amendments thereto, which property or services are used in the operation or maintenance of the district;

construction,

(t) all sales of farm machinery and equipment or aquaculture machinery and equipment, repair and replacement parts therefor and services performed in the repair and maintenance of such machinery and equipment. For the purposes of this subsection the term "farm machinery and equipment or aquaculture machinery and equipment" shall include machinery and equipment used in the operation of Christmas tree farming but shall not include any passenger vehicle, truck, truck tractor, trailer, semitrailer or pole trailer, other than a farm trailer, as such terms are defined by K.S.A. 8-126 and amendments thereto. Each purchaser of farm machinery and equipment or aquaculture machinery and equipment exempted herein must certify in writing on the copy of the invoice or sales ticket to be retained by the seller that the farm machinery and equipment or aquaculture machinery and equipment purchased will be used only in farming, ranching or aquaculture production. Farming or ranching shall include the operation of a feedlot and farm and ranch work for hire and the operation of a nursery;

(u) all leases or rentals of tangible personal property used as a dwelling if such tangible personal property is leased or rented for a period of more than 28 consecutive days;

(v) all sales of food products to any contractor for use in preparing meals for delivery to homebound elderly persons over 60 years of age and to homebound disabled persons or to be served at a group-sitting at a location outside of the home to otherwise homebound elderly persons over 60 years of age and to otherwise homebound disabled persons, as all or part of any food service project funded in whole or in part by government or as part of a private nonprofit food service project available to all such elderly or disabled persons residing within an area of service designated by the private nonprofit organization, and all sales of food products for use in preparing meals for consumption by indigent or home-

CAS CONSTRUCTION, INC.
WATER & WASTEWATER TREATMENT PLANT SPECIALISTS
501 N.E. Burgess • P.O. Box 8270 • Topeka, KS 66608-8270

TESTIMONY TO KANSAS HOUSE OF REPRESENTATIVES
COMMITTEE ON TAXATION
Re: HB2011- Sales Taxes on Publicly Owned Water Utilities
January 20, 1999

Members of the Committee:

I am Robert F. Hall, Treasurer of CAS Construction, Inc, of Topeka, KS, and we thank you for the opportunity to present testimony for a third time on this issue.

CAS Construction is a prime contractor working exclusively in the market of building rehabilitating water treatment and wastewater treatment plant facilities in Kansas, Missouri, Nebraska, Colorado, Iowa and Oklahoma.

As a registered sales/use tax collector for the Kansas Department of Revenue, we are constantly faced with the challenge of interpreting and applying the rules set out in **Sales and Use Tax for Contractors, Subcontractors and Repairmen (28 pages)** and **Sales and Use Tax for Kansas Political Subdivisions (26 pages)**. We are obviously concerned with the difficulty and frustration involved with fulfilling the administrative reporting requirements placed upon us by these rule books, but this concern pales when contrasted to the real issues.

Unlevel playing field on bid day: knowing the range of interpretation of the referenced rules that can be offered by Department of Revenue employees, imagine the range of interpretations that can be made by contractors on bid day. Contractors could potentially submit bids on the same project that (1) calculate taxes comparable to a Department of Revenue auditor, (2) do not include any tax or (3) attempt to calculate tax correctly but fall somewhere in between scenario (1) and (2).

A definite potential exists that the real competitive low-bidder is not identified and the apparent low-bidder may not be collecting tax for the State of Kansas.

Dilution of funding resources: we follow our market closely and know that the number of Kansas communities that have real water treatment infrastructure needs far outweighs the existing funding. It does not make sense that state funding be used for paying sales taxes...how much additional work could be accomplished if this tax funding were available for construction?

Our neighbors choose to exempt ALL municipal construction: via our experience in working in Missouri, Nebraska and Colorado, we know first-hand that the administrative process for exempting municipal construction projects can be SIMPLE. The states of Missouri, Nebraska and Colorado use a one-page form that essentially delegates the municipality's tax-exempt status to the contractor for a specific named project (for state revenue auditing purposes). In the case of Missouri and Nebraska, absolutely no involvement by Department of Revenue personnel is required to properly execute this delegation.

We strongly encourage your consideration for eliminating the taxation of water utility construction projects.

House Taxation
1-20-99

PHONE: 785/354-9953 • FAX: 785/354-4939 • E-MAIL: cascon@casconstruction.com

Attachment 2

CITY OF
WICHITA

TESTIMONY
to
House Committee on Taxation
January 20, 1999

House Bill 2011
Water Utility Sales Tax Exemption

In 1996, 1997 and again in 1998, the City of Wichita along with others, proposed changes in the way sales tax is applied to municipal water utilities. The City of Wichita's concern was prompted by a Department of Revenue audit which demanded sales tax be paid on all kinds of purchases and operations the water utility. Purchases and operations which had never before been taxed.

Traditionally, City governments do not pay sales taxes to the State government for providing municipal services. As the Wichita audit proves, that is not true when it comes to providing water to our residents. In fact we are finding the interpretation and application of the law amounts to an aggressive effort to tax all kinds of basic municipal services, including not just the providing of water, but fire protection, and street repairs if they are related to water utility projects. It also means sales tax must be paid on city vehicles, telephones and computers purchased by clearly tax-exempt City departments if those items are in anyway at anytime used by a Water Department employee. The issue is complex, but in effect Revenue Department auditors contend anything the Water Department "touches" is fully taxable at 5.9% (that includes the 1% local sales tax).

The lawyers and accountants can talk about this issue in far more technical terms than I, but let me explain in practical terms how this situation plays out in Wichita. I knew a secretary who worked in the Wichita Police Department on the fourth floor of City Hall. She answered phones and worked on a computer. She transferred to the Water Department offices on the eighth floor of City

House Taxation
1-20-99
Attachment 3

Hall. She did similar work on an identical computer and answered citizen calls on an identical telephone. But the cost of that phone and computer service is 5.9% more expensive because they sit in the Water Department offices and not the Police Department offices. It's especially hard to understand when you realize all computer and phone services in Wichita City Hall are provided through our own in-house Data Center. Money shifting from one City department to another is suddenly taxable.

One of the biggest issues involves electricity used to pressurize water for distribution. Revenue auditors say that electricity is fully taxable. But more than half of all electricity consumed at the pump station is to generate enough pressure for fire protection, making sure the system is charged so water comes out of the hydrant when its needed. By determining that all of the electricity is taxable, the State is taxing Wichita for providing fire protection to its residents. Most of you probably thought fire protection was clearly a basic, tax exempt function of City government. Except of course for fire hydrants. Since in Wichita the water department purchases fire hydrants as part of its operation of the water system, they too are fully taxable.

The current approach and interpretation of the law also means the City must maintain an entirely different and separate asset base and purchasing system for the water utility to protect general assets and operations of the City from taxation. This results in inefficiency and cumulative administrative expenses. And there is lots of confusion caused for contractors and vendors who never quite know whether or how to determine if sales tax should be included in bids on city contracts. Another interesting note: under current interpretation, if a city government built a new city hall, the water offices, staff and accounting systems would have to be kept out of the building to prevent the entire city building from being taxable.

Providing water to citizens is a basic function of city government, the same as filling potholes, putting out fires or providing police protection. As such, exempting municipal water utilities from paying sales tax on purchases will clarify and correct the confusing, inconsistent question of what's taxable and what's not when comes to providing basic City services.

City of Olathe

MEMORANDUM

TO: House Committee on Taxation

FROM: Donald R. Seifert, Management Services Director DRS

SUBJECT: HB 2011, Sales Tax Exemption for Municipal Water Utilities

DATE: January 20, 1999

On behalf of the city of Olathe, thank you for the opportunity to support this bill recommended by the interim assessment and taxation committee. **HB 2011** would exempt purchases made by municipal water utilities and other providers of water service from the state and local sales tax.

The city of Olathe has operated a municipal water utility since 1884. Under current law, the treatment and distribution of water is the only area of municipal government where the purchase of goods and services are subject to the sales tax. Purchases made in all other areas of the city have traditionally been exempt from the sales tax.

We estimate the application of sales tax to the water utility adds an additional $35,000 annually to the operating cost of this service. t also adds to the cost of every capital item the city purchases for its water system, such as pipe, trucks, and treatment capacity. For example, the city currently is cons :ucting a $20 million capacity expansion project at its Water Plant No. 2. The application of sales tax to materials used in this project is significant.

Application of sales tax also presents additional accounting confusion, where certain line items in the city's budget are taxable and most are not. For budgeting and accounting purposes, the city operates a combined water and wastewater utility fund. It is especially confusing for purchases relating to our line maintenance division, which maintain both water (taxable) lines and wastewater (non-taxable) lines.

We believe there is no more basic municipal service than the furnishing of water to city residents, and that it should be sales tax exempt like the rest of city government. The city urges this committee to recommend **HB 2011** favorably for passage.

Thank you again for the opportunity to support this bill.

rc

House Taxation
1-20-99
Attachment 4

KANSAS
RURAL
WATER
association
Quality water, quality life

P.O. Box 226 • Seneca, KS 66538 • 785/336-3760
FAX 785/336-2751 • http://www.krwa.net

COMMENTS ON HOUSE BILL No. 2011
BEFORE THE HOUSE COMMITTEE ON TAXATION
January 20, 1999

Mr. Chairman and Members of the Committee:

Thank you for the opportunity to present comments on House Bill No. 2011. I am Dennis Schwartz, a member of the Board of Directors of the Kansas Rural Water Association; I am also General Manager of Rural Water District No. 8, Shawnee County, KS. The Association provides technical assistance to public water and wastewater systems and a variety of training opportunities for operators, board and council members. The Association's membership includes 275 rural water districts and 325 cities and 232 supplier/vendor associate members.

The Kansas Rural Water Association supports House Bill No. 2011. As an employee of a rural water district, and from my experience with the Association, I know of no administrative aspect that consumes as much time as trying to determine the application of state sales tax. As an example, I would like to read directly from the guideline booklet, Sales and Use Tax for Kansas Political Subdivisions:

-*"A city uses electricity or gas to power a water pump that extracts water from a well. This utility use qualifies for exemption as tangible personal property "consumed in production".*

The next example: *"The generator that generates electricity at an electrical power plant qualifies as manufacturing machinery. Also qualifying is the pump used to pump water from the ground to the treatment plant. CAUTION: This exemption applies ONLY to manufacturing machinery and equipment and those repair and replacement parts that are major components, such as a compressor or a motor. Repair parts (fan belts, spark plugs, etc.), peripheral equipment such as control panels and electrical conduit, and ALL labor services to install or repair a qualifying item are TAXABLE."*

At best, this is confusing -- to the utilities, contractors, designers and also to the Department of Revenue. A control panel to operate a pump which may be tax-exempt is only exempt to the extent of use required to operate the pump; the conduit to connect the pump, even when the contractor bids a unit price, is taxable but the electrical wiring may not be. In many cases, the control panel is more of a component than is the pump or motor. We also know of situations in water districts and cities in Kansas where the power bills are being divided to separate the power required to lift water out of the well to that required to send it to the tank.

The water district I manage is working to build an addition to its treatment plant. We have had to structure construction bid documents into four segments -- with the separation being what components are taxable and which are not. This splitting of bid documents has no relationship to construction time-frames or what anyone could conceive as being based on good business judgment. Ensuring the highest level of compliance with sales tax application likely is costing the utility thousands of additional dollars because of ramifications that go far beyond concerns for paying of appropriate sales tax.

The Kansas Rural Water Association suggests that the public at large will benefit if HB 2011 were approved, the Dept. of Revenue would be relieved of trying to administer an exceedingly confusing law and regulatory relief would be gained by water utilities, designers and contractors. We suggest that an amendment be introduced to also extend this clarification to public wholesale water districts formed under K.S.A. 19-3545. Cities and rural water districts encourage you to support this tax clarification.

Respectfully submitted,

Dennis P. Schwartz

Dennis Schwartz
Director

House Taxation
1-20-99
Attachment 5

League of Kansas Municipalities

PUBLISHERS OF KANSAS GOVERNMENT JOURNAL 300 S.W. 8TH TOPEKA, KS 66603-3896 (785) 354-9565 FAX (785) 354-4186

TO: **House Committee on Taxation**
FROM: Chris McKenzie, Executive Director
DATE: January 20, 1999
SUBJECT: Support for HB 2011

Thank you for the opportunity to appear today in support of HB 2011, which would exempt purchases by public water utilities from state and local retailers' sales tax. As you know, current law provides that purchases by political subdivisions are exempt from the sales tax when the subdivisions are acting in their governmental capacity. When a city is acting in a proprietary capacity, however, such as in furnishing gas, water, electricity or heat, sales taxes are due and payable.

The provision of water supplies to Kansas citizens today is largely the function of local governments in Kansas. Unlike gas and electric service, only a handful of private water companies exist today. In other words, water service, like wastewater service, can more accurately be described as a core government service and, therefore, an appropriate object for exemption from the sales tax. In fact, with increasing federal regulation of drinking water supplies, it appears unlikely to us that future growth in the privatization of water utility service is a long term possibility.

For many smaller cities there is another reason to approve this exemption. Cities with water utilities also purchase equipment which is used for the street maintenance, park maintenance, and other traditional municipal functions. In the recent edition of the League's *Governing Body Handbook*, we felt it was important to advise city officials that a city's application for exemption for such mixed use equipment (e.g., pickup truck) may be denied by the state because it is not used exclusively for an exempt purpose. Unfortunately, the result of this situation is either a higher cost for equipment used for governmental purposes or duplication of equipment purchases--both unacceptable results.

For larger cities that consume electricity and other property in the pressurization and delivery of water for fire suppression purposes (clearly a traditional function of government), a similar problem has arisen, requiring extensive bookkeeping to segregate fire suppression-related water utility expenses from all others.

RECOMMENDATION: We respectfully submit that it is time to end the taxation of the governmental function of providing water utility services, and we recommend the enactment of HB 2011.

House Taxation
1-20-99
Attachment 6

S E OF KANSAS
Bill Graves, Governor

DEPARTMENT OF REV UE
Karla Pierce, Acting Secretary

Office of Policy & Research
Shirley K. Sicilian, Director
915 SW Harrison St.
Topeka, KS 66625

(785) 296-3081
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Hearing Impaired TTY (785) 296-6461
Internet Address: www.ink.org/public/kdor

Office of Policy & Research

TESTIMONY

To:	Chairman David Adkins House Taxation Committee
From:	Shirley Sicilian Kansas Department of Revenue, Director of Policy & Research
Re:	**House Bill 2009**
Date:	January 20, 1999

Good morning Chairman Adkins and members of the House Tax Committee. My name is Shirley Sicilian and I serve as Director of Policy & Research at the Department of Revenue. I appreciate the opportunity to testify before you today regarding HB2009, which would broaden the sales tax exemption for machinery and equipment.

I. Background on the Manufacturing Machinery and Equipment Exemption.

Almost all states have some form of sales tax exemption for manufacturing machinery and equipment. The exemption makes sense from a tax policy perspective. In principle, sales taxes are designed to be levies on final consumer expenditures. If goods used in production are taxed, as well as the goods which are finally produced, there is an element of multiple taxation. 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(cc) is focused on economic development. It is a very broad exemption for all tangible personal property and service purchases "made in conjunction with constructing, reconstructing, enlarging or remodeling a business or retail business" which has increased employment by at least two. K.S.A. 79-3606(kk) is an exemption for manufacturing or processing machinery and equipment, and has no employment criteria. House bill 2009 would expand the exemption for manufacturing machinery and equipment in 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 integrated 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, 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

House Taxation
1-20-99
Attachment 7

cc ation of the two different theories which has been difficult for the department to interpret an administer consistently over the years. For example, one Kansas appellate court judge stated, albeit in an unpublished opinion dealing with a superseded statute, that Kansas has adopted the integrated plant theory.[1] Because the court did not publish this ruling, its legal impact is limited to the parties to the case. Meanwhile writers for publications that provide in-depth tax analysis, classify Kansas as an "Ohio rule" state.[2] Furthermore, as recently as July 10, 1998, the Kansas Supreme Court upheld the department'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):

> In BOTA's view an exempt item would be "integral to the process," would have an "essential function" and without it, "the operation would quickly grind to a halt." (The Kansas Supreme Court in its *Alsop* decision overturning BOTA).

The *administrative* history of this statute is clear. Since its enactment ten years ago, the department has understood it to be "an Ohio rule with a handful of enumerated expansions," and this understanding has never been overturned.[3]

Two and a half years ago the department 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 House bill 2643 which would have, among other things, clarified and expanded these two statutes. The clarifications would have made it crystal clear Kansas is adopting a broadly defined integrated plant theory. But those provisions did not pass.

Over the 1998 interim session, the department worked closely with members of the Tax Coalition and the Kansas Chamber of Commerce and Industry on improvements to these two provisions. We submitted a proposal to the Interim Tax Committee. The proposal, along with additional exemptions for oil and gas exploration and drilling equipment, was adopted as a Committee bill and then pre-filed as House bill 2009.

II. Summary of HB 2009.

House bill 2009 would amend the two related statutes exempting goods consumed in production and manufacturing machinery and equipment:

I. Expand the exemption for "consumed in production."

- Expands the exemption for property which is "immediately" consumed to property which is consumed with-in one year. This eliminates confusion over what is meant by "immediately" consumed.
- Clarifies the exemption applies to certain lubricants and catalysts.

II. Expand the manufacturing machinery and equipment exemption.

- Expands the 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:
  - ⇒ 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.)

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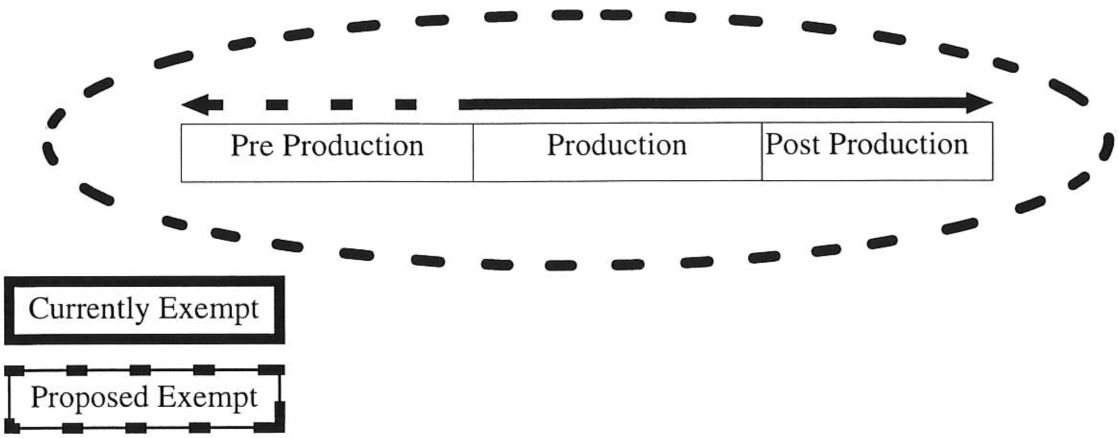
[1] *In re Lubrication Eng'rs, Inc.*,No. 70,980 (Kan. Filed Mar. 10, 1995) (No. 94-70980-A).
[2] See e.g. Goodman, Marcus and Husghes, 1330 Tax Management, Inc., Sales and Use Taxes: *The Machinery and Equipment Exemption; Multistate Tax Portfolio Series* (1997).
[3] See Department of Revenue Information Guide 19-88-1 (1988).

⇒ Machinery that deals with by-products of production (e.g.: pollution control equipment, waste handling equipment equipment, etc.)

⇒ Ancillary property that might otherwise not be viewed as "machinery or equipment" (e.g. gas pipes, electric wiring, special foundations, clean rooms, etc.)



- Exempts labor services for installation and repair of this machinery. This expands the exemption and eliminates the requirement that taxpayers separate out installation costs from equipment costs.

- Clarifies, without narrowing, the types of firms eligible to receive the exemption.

- The Governor's 1998 bill also proposed expanding the exemption for *major* component parts of such machinery to include *all* component parts. This allowed all repair and replacement parts of such machinery to be exempt and, together with the expansion of the consumed in production exemption, helped close the gap between property which is immediately consumed and property which is consumed over several years (the machinery itself). This particular expansion was accomplished last session in House bill 2584. It prospectively mooted the Kansas Supreme Court decision in *Alsop,*[4] which upheld the department's interpretation of the old law.

- Expands the exemption to include oil and gas exploration and extraction equipment. The current law is limited to processing machinery and equipment, and some oil and gas equipment does qualify currently as processing equipment. This expansion is conceptually different from the ones mentioned above. Those listed above expand the types of processing equipment which would be exempt, and the labor associated with installing and servicing the processing equipment. This expansion would bring in two new exempt functions, exploration and extraction, in addition to processing.

Our goal was to make it easier for taxpayers to interpret and follow these laws. Our belief is that in this case simplicity can best be achieved by clarifying and expanding the exemption.

III. Fiscal Impact.

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[4] *In re Alsop Sand Company, Inc*., Docket No. 76,870 (Kansas Supreme Court; Filed July 10, 1998).

T cal year 2000 impact would be $5 million for the manufacturing machinery and equipment an the consumed in production expansion. The addition of Oil and Gas exploration and extraction adds another $6.3 million. The total fiscal impact for fiscal year 2000 is $11.3 million. The state general fund impact would be $10.7 million and the state highway fund impact would be $0.6 million. The fiscal year 2001 impact would be $12.8 million in total, with a $12.2 million impact to the state general fund and $0.6 million to the state highway fund.

The fiscal impact for the manufacturing machinery and equipment and the consumed in production expansion was developed mainly from department data. In FY 97, 5% of the manufacturing industry was audited and assessed $139,270 for underpayment of sales tax for equipment purchases and labor services. From discussion with the audit staff, the level of compliance in remitting sales tax on machinery is estimated to be between 60% and 70%. Applying a 4% annual growth rate to these figures implies that the value of the exemption for all manufacturing firms in fiscal year 2000 would be $5 million, with $4.79 impact to the state general fund and $0.26 impact to the state highway fund. This $5 million figure is consistent with capital expenditure data from the U.S. Bureau of the Census. The figure could also be somewhat overstated due to the overlapping economic development related exemption at K.S.A. 79-3606(cc). The fiscal impact has been reduced from last year's estimate due to the 1998 Legislature's exemption of repair parts and accessories which was estimated to reduce state revenues by approximately $1.6 million annually.

The fiscal impact for the oil and gas exploration and extraction expansion is based on cost information received from Kansas Independent Oil and Gas Association (KIOGA) and drilling information received from the Kansas Corporation Commission (KCC). In 1998, the KCC reports 839 oil and gas wells were drilled. This reflects a 43% drop from the previous year. Of those 839, 13% are expected to be dry wells and therefore have no equipment costs. Another approximately 33% of the wells drilled were in Eastern Kansas where the cost of completion is low and equipment costs average $25,000 per well. The remaining 54% of the wells to be drilled were in Western Kansas where cost of completion is higher, approximately $35,000. Based on this data, the fiscal impact of adding drilling equipment as exempt would result in a estimated $1.9 million annual loss of sales tax revenue.

KIOGA also provided an Authority for Expenditure (AFE) report that provides the costs for drilling a new well. This report indicates the equipment costs for drilling a new well in western Kansas may be twice the equipment cost estimate used above, or $70,000. If this is typical of drilling costs, the fiscal impact would be closer to $3.4 million.

The KCC has just recently released its estimate for the number of wells which will be drilled in 1999. Those estimates show an additional 11% decrease from 1998 drilling activity. Applying that reduction to these figures would lower these amounts to a midpoint of approximately $2.4 million.

In addition to the equipment being exempt, the costs associated with servicing wells would also be exempt under this proposal. The State Sales Tax Collection reports by 2-digit SIC show that the oil and gas extraction industry group (SIC 13) paid $4.5 million in state sales tax in fiscal year 1998. Further review shows that 95% of the tax paid was by businesses classified as performing oil and gas field services.

For fiscal year 2000, using a midpoint of $6.9 million and assuming a July 1 implementation date, the loss of revenue would be $6.3 million for the 11 months of fiscal year 2000 collections.

KIOGA

KANSAS INDEPENDENT OIL & GAS ASSOCIATION

105 S. BROADWAY • SUITE 500 • WICHITA, KANSAS 67202-4262
(316) 263-7297 • FAX (316) 263-3021

Testimony of
Robert E. Krehbiel, Executive Vice-President
Kansas Independent Oil and Gas Association
on H.B. 2009-Sales Tax
before the House Committee on
Assessment and Taxation
January 20, 1998

Mr. Chairman and Members of the Committee:

My name is Robert E. Krehbiel and I am appearing on behalf of the Kansas Independent Oil and Gas Association in support of House Bill 2009. This Association was organized 62 years ago to speak for the many independent oil and gas producers and their supporting service providers throughout the State of Kansas. This Bill is of vital importance to all Kansas crude oil producers as well as the Kansas economy.

The dramatic and sustained decline in the price of crude oil at the wellhead has placed the future of marginal oil production in all producing states in America in serious jeopardy. The seriousness of this issue has drawn the attention of the media and has been well publicized. The Governor's of the producing states have established Task Forces in conjunction with the U.S. Department of Energy to determine how to deal with the price crisis. This issue is complex.

Governor Keating of Oklahoma has called a special session of the Oklahoma Legislature to convene January 20, 1999, for the proposed repeal of 6/7ths of their severance tax, retaining only 1/7 dedicated to public education. Oklahoma has no property tax on oil and gas. Other Task Force proposals include repeal of the sales tax on oil and gas machinery and equipment and services relating thereto.

Governor Graves is also well aware of the crisis facing this industry and stated in his address to the legislature that "the Kansas oil industry has been devastated" and challenged the legislature to "do what we can and be sensitive to those needs as we make public policy". This bill is one very important step that can be taken by the 1999 legislature to help reduce the costs associated with maintaining marginal oil production in Kansas and incent the continued exploration and development of oil and gas in Kansas.

1998 was, without doubt, the most difficult year in recent history for the nation's 24,000 independent oil producers. Oil prices in Kansas and all other producing states have reached historic lows which last week were ranging from $5.90 per barrel for North Dakota sour crude

House Taxation
1-20-99
Attachment 8

oil to $10.25 per barrel for West Texas intermediate crude oil. The posted price for Kansas crude oil last week ranged from $8.75 per barrel in Eastern Kansas to $9.75 per barrel for Central Kansas crude. Production costs exceed oil prices for much of the crude oil that is produced throughout the state. As a result, many of the state's 40,000 marginally economic stripper wells have been shut-in, hundreds of employees have been laid off, rigs have been stacked and drilling has ceased.

A recently completed crude oil price crisis survey conducted by our Association in conjunction with the Independent Producers Association of America was an attempt to quantify the impact of low crude oil prices on our industry. The response was overwhelming and the results were startling. With operators of over 13,000 wells responding in Kansas the survey indicates that 40% of oil wells are shut down as unprofitable and an additional 40% will be shut down within the next few months. This is a crisis of enormous proportions.

To help define the problem and the impact on the U.S. and Kansas economies I have attached various studies from the educational and governmental communities. The first is a publication of the Interstate Oil and Gas Compact Commission entitled "Marginal Oil and Gas Report". The IOGCC is a 63 year old state government organization representing the governors of 29 oil and gas producing states. The mission of the IOGCC is to promote conservation of domestic oil and gas by minimizing waste and maximizing production while protecting health, safety and the environment. Governor Bill Graves was recently appointed to serve as Chairman, replacing Governor Jim Geringer of Wyoming.

This Marginal Oil and Gas Report indicates that in 1997 there were 436,084 stripper wells in the United States which produced 352,938,000 barrels of crude oil in 1997 at an average daily rate of 2.22 barrels per well. 15,173 of these wells were plugged as uneconomical in 1997. The remaining stripper wells have the potential to recover an additional 2.577 billion barrels of oil through continued primary and secondary recovery production. Today this enormous natural resource is threatened by premature plugging due to low wellhead prices (see page 5 of the report).

This Report also demonstrates that the State of Kansas had 40,504 stripper wells producing in 1997, accounting for 30,675,301 barrels produced in 1997, ranking fifth in the nation (see page 2 of the report). 1,765 stripper wells were plugged in Kansas in 1997. The remaining Kansas stripper wells have the potential to recover an additional 138,806,000 barrels if they are not prematurely plugged due to low wellhead prices. A recent study involving technologically advanced secondary recovery methods indicates that an additional 100 million barrels of oil could be recovered from the Morrow Formation, 300 to 400 million barrels from the Lansing-Kansas City Formation and up to 300 million barrels from the Arbuckle Formation.

A second publication attached is entitled "The Economic Impact of Stripper Wells in the United States", prepared by Dan Olds, Energy Management Consulting Services, PricewaterhouseCoopers, for the Interstate Oil and Gas Compact Commission. His economic analysis would indicate (page 5 of the Report) that the 15,173 stripper wells that were plugged in 1997 will result in lost production of 14,049,479 barrels of crude valued at $253,239,922 using the 1997 average price of $18.02 per barrel. The multiplier effect of this loss of production and value is reflected in the loss of 977 jobs in the industry with the loss of $24,968,000 in earnings and 2,220 jobs in the overall economy with the loss of $51,427,000 in earnings.

The Report indicates (page 5 of the Report) that the lost revenue resulting from plugging the 1,765 stripper wells in Kansas in 1997 was $24,902,817, which multiplies (page 8 of the Report) to $37,309,000 of lost output, $4.794 million in lost earnings and 354 lost jobs. Finally, Page 10 of the Report, hypothesizes that if all stripper wells in Kansas were plugged and abandoned lost output would total $856 million, lost earnings would total $110 million and 8,115 jobs would be lost.

Though Kansas data for 1998 is not yet complete, Dr. Tim Carr, at the University of Kansas Geological Survey, has estimated the decline in wellhead value in Kansas will result in the loss of 5,680 jobs in Kansas. A copy of his report is available.

In 1997 the Kansas Oil and Gas Industry produced nearly 40 million barrels of crude oil and 678,654,000 MCF of natural gas to create over $2.2 billion in value at the wellhead. To put that number into perspective it is roughly the equivalent value of all of the wheat and soybeans produced in Kansas in 1997. The average wellhead price for crude oil in 1997 was approximately $18.23 per barrel. The average wellhead price for natural gas in 1997 was approximately $2.18 per barrel.

The industry paid $203,825,743 in severance and property taxes to state and local governments in 1997, slightly over 9.1% of gross wellhead value. In 1997, the Kansas oil and gas industry employed 6,829 people at the production level and an additional 16,600 people downstream. The development of secondary recovery methods has the potential to add an additional 6,000 employees in Kansas.

Although Kansas is considered to be a mature producing province it clearly retains enormous potential when the price of crude oil and natural gas reflects the cost of production and tax policy reflects the ability of the industry to pay.

But the problems facing this industry are serious and immediate. The figures for 1998 have not been finally tabulated, but it is estimated with reasonable certainty that the price of crude oil sold at the wellhead will have averaged $11.21 per barrel. The most recent price posted by crude oil purchasers for Central Kansas crude oil was $9.75 per barrel, up from a recent low of $7.50 per barrel, and $8.75 per barrel for Eastern Kansas crude oil, up from a recent low of $6.50 per barrel. The most reliable energy analysts, the Energy Information Administration, U. S. Department of Energy, predicts these prices will be with us for some time to come. Likewise, industry analysts, agree we are faced with a long siege of low wellhead prices.

One industry analyst calculated that in the United States, a one cent per gallon decline in gasoline prices translates into $1.2 billion in annual cost saving. "If gasoline prices remain at crude oil is taxed.

In 1991, Governor Joan Finney proposed removing all exemptions to the sales tax to use in lowering property taxes. Many members of this Committee know the entire list of exclusions and exemptions from the sales tax existing in 1991 exceeded $900 million. This tax committee reviewed those exemptions and determined they could be justified on the basis of the economic activity they generated and the nature and condition of the industry they benefitted. The committee determined that the benefits to the state of these sales tax exemptions exceeded their cost and should be retained.

At that time Secretary of Revenue Mark Beshears estimated the repeal of the sales tax on machinery and equipment used directly and primarily in the production process would generate $42.5 million and this exemption was retained. The Department of Revenue, however, opined, in Information Guide 19-88-1, that this exemption did not apply to oil and gas machinery and equipment because the word "extraction" was not included. This interpretation effectively precluded the industry from this much needed exemption.

Last summer we asked the Interim Committee to review the policy of taxing oil and gas production machinery and equipment in the context of current economic conditions while reviewing the manufacturing machinery and equipment exemption to the sales tax. The Committee agreed that oil and gas machinery and equipment should be included in this exemption.

H.B. 2009, as proposed by the Interim Committee would recognize that the extraction of crude oil and natural gas is an integrated production operation by a processing facility and that machinery and equipment associated and services related thereto, associated with drilling and pumping and use at well sites would be exempt.

The average Kansas stripper well produces 2.2 barrels of oil per day. When these wells go down the sales tax on the repairs and replacement machinery and equipment is a significant disincentive and abandonment becomes the alternative. The sales tax on equipping new wells is also a serious disincentive to drilling and exploration activities.

A recent study by the Interstate Oil and Gas Compact Commission reveals that tax incentives applied to the oil and gas industry returns $2.27 for every dollar invested. The oil and gas industry is no different than any other industry included within this exemption and we urge passage of HB 2009 for the benefit of the industry and the people of Kansas.

Thank you very much for your time and consideration.

GRIGGS OIL, INC.
SUTTON PLACE
SUITE 220
209 E. WILLIAM
WICHITA, KS 67202
316-267-7779
fax 316 267 4866

December 16, 1998

Bill Richardson
Secretary of Energy
Department of Energy
Washington, D.C.

Dear Mr. Richardson:

Griggs Oil, Inc. is a small, family-owned Kansas independent producer. The 90 or so oil and gas wells we operate produce over 200 barrels per day if all our wells are up and running. When the price of oil dropped below $12.00, however, we had to shut down many of our wells because they were not economical. We determined that the price of oil would need to be in the $16.00-17.00 range for these wells to break even, so we had no choice but to cease their operation. By doing so, we have taken about 30-35 barrels per day off the market, and we have serious doubts that we will be able to get the wells back to that level of production if we try to re-start them. In addition, if the price remains below $8.00 per barrel, we are facing the prospect of shutting down most of our remaining oil wells.

Many if not most, of the wells that are shut down due to low prices will never recover and will have to be plugged. Once plugged, the remaining oil reserves in the ground will be forever lost. Bear in mind that new oil wells cost over $150,000.00 to drill, complete and equip in most areas of Kansas, and that the cost to re-enter an old one is well over half of that. It is inconceivable that anyone would ever drill a new well, or even re-enter an old one, to get 3-4 barrels of oil per day, even though the well may produce at that level for many years.

Since we are not operating as many wells, and since oil revenues from our best wells barely cover their operating costs at current prices, our company's income has been severely reduced. In response, we have had to cut our costs by laying off two of the company's six employees, both of whom had been with us for many years. We have also moved to smaller offices, delayed repairs and workovers to producing wells, and reduced our exploration budget to the absolute minimum. In other words, we are just trying to survive until the oil price improves.

But the impact of low oil prices goes beyond our company and its employees. The wells we operate are owned in part by investors, including ourselves, who helped drill these wells with their hard-earned, after-tax dollars. These people are now seeing the value of

HOUSE TAXATION
1-20-99
Attachment 9

their investment and the income from it reduced in some cases to zero. A lot of these people depend on oil income from the wells we operate. The current situation has put them into an immediate financial bind, and has undermined the value of the estate they had hoped to leave to their heirs.

The effect of shutting down oil wells must also be looked at from the point of view of our contract pumpers who are paid $125.00-150.00 per producing well per month. The families of these skilled, experienced workers are now really struggling financially with so many wells no longer producing. The same can be said for suppliers and service companies, many of whom have sold out or just shut their doors. We worry that many of these people will permanently leave the industry if the present situation continues, and that it will be extremely difficult to operate in the future without them.

We also feel that there will be significant negative consequences to state and local governments due to reduction in severance and property tax collections. Since these taxes are based on the value of what is produced, they will have to be made up from increases in other taxes, such as real estate or income taxes. This will have an overall negative impact on oil producing states by burdening other taxpayers, and by discouraging economic development and location of new businesses in these states due to prohibitive tax levels.

Finally, we are grimly concerned over the long-range effects to our nation of this most recent blow to the oil industry caused by prolonged low prices. The United States is one of the top oil producing countries in the world, a fact that helped us win World War II and one that remains pivotal to our national defense and independence. Our position as a major energy producer has played a large role in making the United States the world power it is, but that position is now in more jeopardy than ever since we already import about 56% of the oil we use. A great number of the wells in this country are uneconomical at present prices, so we as a nation are in imminent danger of forever losing a significant percentage of a valuable national asset as well as a major strategic defense advantage. If a large percentage of the stripper wells in this country were plugged, we would have to replace hundreds of thousands, and perhaps as many as a million of barrels of oil per day with imported oil. This would increase our trade deficit by billions of dollars per year; but more importantly, it would put this country in real peril from a defense standpoint.

Everyone seems to take for granted that the present free flow of oil will always continue, and that the domestic oil and gas industry will always survive. The leaders of this country need to question those presumptions and plan for a day when enough imported oil is not readily available. If that day ever comes, the nation will look for help, as it always has in the past, to its domestic oil producers. If nothing is done to help producers survive, the nation will find that its domestic oil industry has been neglected to death by short-sighted leadership that prizes the positive economic effects of low fuel prices over the survival of the vital industry that produces that fuel here at home.

We need, at a minimum, some form of tax relief for marginal wells, but a better alternative would be to establish a floor price for domestic crude. This would ensure the health of our industry and the continued prominence of this country as an energy producer. To do less than the minimum, or to do nothing at all, will have consequences far beyond the borders of oil producing states. The future of this country, the quality of life of its citizens, their children and grandchildren depends on what is done now to preserve the domestic oil industry. We ask that you make this issue one of highest priority, and that you give it the immediate attention it deserves.

Sincerely,
GRIGGS OIL, INC.

RBGi

Ross B. Griggs
Vice President

DAVID AND JEAN MAI
P.O. BOX 842
RUSSELL, KS 67665
785 483 4848

HONORABLE BILL RICHARDSON
SECRETARY OF ENERGY USA
WASHINGTON, D.C.

DEAR MR. RICHARDS,

WE ARE PRINCIPAL STOCKHOLDERS IN MAI EXCAVATING INC. A CLOSE HELD, FAMILY CORPORATION, INVOLVED IN THE OIL INDUSTRY AS A SERVICE COMPANY. OUR MAIN INCOME SINCE 1964 HAS BEEN DERIVED FROM THE OIL INDUSTRY, THEREFOR WE ARE VERY CONCERNED ABOUT THE SHAPE THE INDUSTRY IS IN THROUGH NO FAULT OF IT'S OWN. WE HAVE HAD HARD TIMES BEFORE BUT NEVER HAS THE OIL INDUSTRY SUFFERED AS MUCH AS IT IS SUFFERING NOW.

WE HAVE HAD TO GO FROM 30 EMPLOYEES TO 6 IN THE PAST 13 YEARS WE HAVE BEEN FORCED TO SELL EQUIPMENT BECAUSE THERE WAS NO WORK FOR IT, WE HAVE SEEN ALL OUR YOUNG PEOPLE LEAVE THE AREA AND LOOK FOR OTHER KINDS OF EMPLOYMENT, LEAVING PRECIOUS FEW IN THE OIL INDUSTRY THAT KNOW WHAT OIL PRODUCTION IS.

THIS HAS AFFECTED OUR COUNTY TAX BASE, PUTTING THE BURDEN ON SMALL BUSINESS SUCH AS OURS, WE ARE IN DANGER OF LOSING OUR HOSPITAL AND THE SCHOOL SYSTEM IS IN JEOPARDY. THE AREA FROM NORTH DAKOTA TO TEXAS GULF IS HURTING AND NO ONE IS LISTENING TO US.

IT LOOKS LIKE FOREIGN OIL IS MORE IMPORTANT TO OUR LEADERS THAN THE UNITED STATES OIL INDUSTRY. WHAT HAPPENS WHEN FOREIGN OIL COMPANIES DECIDE NOT TO SEND OIL TO OUR COUNTRY IT WILL TAKE YEARS TO REDO THE OIL INDUSTRY EVEN IF WE WERE TO START TOMORROW. PEOPLE ARE NOT GOING TO BE ABLE TO DO A NEW START UP BECAUSE THEY HAVE HAD TO SPEND THE RESOURCES THEY HAVE TO JUST SURVIVE.

WE ASK THAT YOU PLEASE TAKE OUR CASE TO GOVERNMENT LEADERS, WE DON'T WANT A GOVERNMENT HAND OUT WE JUST WANT THE RIGHT TO A DECENT INCOME, OUR OIL INDUSTRY SHOULD BE MORE IMPORTANT THAN JOBS FOR PALESTINIAMS.

SINCERELY,

David Mai Jean Mai

DAVID AND JEAN MAI

TELEPH .6-793-9556 FAX 316 71

CHASE WELL SERVICE, Inc.

P.O. Box 355 · 5619 8th Street
GREAT BEND, KANSAS 67530

Dec. 17. 1998

The Honorable Bill Richardson
Secretary of Energy, U.S. Department of Energy
1000 Independence Ave., SW
Washington, DC 20585

Dear Secretary Richardson:

I am writing you this letter on why it is important that our government set a realistic price on domestic crude for the survival of our industry, National security, and livelihood of thousands of workers that are left in our industry. The oil industry has made western Kansas and other states prosper when other industries were down. Our industry has helped build schools, roads, made towns grow and pumped thousands of dollars if not millions in local communities which were passed on to others. With Kansas crude at $7.25 a barrel it is hard to put people to work. **Oil producers can not afford to pump their wells, wells are being shut down, people are being laid off, and are forced to leave our area.** With the people that are left, they are forced to pay higher taxes to live in the same home they have had for years. There is no money that we can call extra to take our families on vacations, out to eat, or any of the nice thing we would like to do. We just try to make ends meet.

We are not people that that work for Mobil, or Exxon, but people who work for small independent oil companies. Companies that have been hit hard by over burden taxes, raising cost of health insurance and repair cost of equipment. We make a small wage compared to the big boys. We are honest hard working people, that just want to work. If things continue, on as it has on the past year, we will be forced to leave are homes and towns and move to the large cities.

I have seen this company that I have worked for the last 27 years, go from 48 employees in the late 70's & early 80's , decline down the 11 employees at the present time. Surviving day by day, wondering if it is worth staying in business, trying to fight the Federal , State, and local bureaucracy.

You take the Mid Continent area of this country, we tend to make this country run. The oil industry supplies jet fuel, diesel fuel and gasoline for planes, trains, and automobiles. Heating oil for factories and even fuel for generators for electricity. Compounds that are vital in making plastics, which are a by product of oil, is used in everyday living from coast to coast.

Our country can not depend on foreign oil as a sole provider. If our country depends on foreign oil, it will only be a matter of time before our country is being

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GREAT BEND, KANSAS 67530

controlled and manipulated by non-American outside forces. Just think our Army, Navy, and Air Force, being controlled by some foreigner, **(scary thought)**. Our President wants to send our naval fleet somewhere to protect a little county, but we can not go because we have no fuel. **Foreign countries have cut off U.S. oil imports.** If you don't think this can happen, just remember oil embargo of 1973!! Fuel storage coast to coast and America was at the mercy of foreign oil ministers.

I hope you can see the urgency in helping the OIL INDUSTRY survive and protect one of our Nations most important asset for global survival.

Sincerely,

Mark A. Link

Mark A. Link
President of Chase Well Service, Inc.

•Rod & Tubing Service •Single & Double Drum Units •Reverse Circulator •KCC & ICC Reg. Trucks

Heavy Pole Masts
Telescoping Single & Double Derricks
Workover & Completions
Water & Vacuum Trucks
High Pressure Pump Truck
Experienced Crews

PRATT WELL SERVICE INC.
AC 316 672-2531
COMPLETE OIL WELL UNIT SERVICE
In Business Since 1946

Kenneth C. Gates, President
Kevin C. Gates, Vice President
Sandra L. Gates, Sec.-Treas.
P.O. Box 847
Pratt, Kansas 67124

December 16, 1998

The Secretary of Energy Bill Richardson
Washington D.C.

Dear Mr. Secretary,

I am writing this letter to let you know the effect of the low oil prices on an almost 53 year old oil and gas well service company. I am the second generation of a family owned business and my son is in his final year at Wichita State University hoping to be the third generation of the company. But the low oil/gas prices may set the scenario differently for that. In this family owned business we have been totally dependent on the oil industry to provide for our 52 employees and their families. In 1986 we had 88 employees until the "boom" busted. The average years of employment for each of our employees is 15 years which is very unusual for the well service industry.

Pratt Well Service is located in an area with a population of approx. 6500 people that is supported by agriculture, railroads, and oil industry. Pratt, in the middle 80's had around ½ of the population working in the oil industry. Today we have less than 125 people employed in the industry. The tax base has been supported by the oil industry but now with the price of oil so low, I am not sure where the tax money will come from. Programs have already been dropped or scaled back to offset the lowering tax income.

The oil industry has been a 600,000 or larger industry and due to low oil prices we have lost at least 2/3 of that number, or more, due to the mergers taking place. I do not understand as important oil is to the world, why is the price of oil so low? Because, this product is used up it is gone for ever.

Please, Mr. Secretary do something for this industry to help the pricing, otherwise this industry could be in the hands of the auctioneers. The old saying is "We will pay now or pay later".

Sincerely,

Kenneth C Gates

Kenneth C. Gates
President

9-7

CLA-MAR OIL COMPANY

P.O. Box 1197, Hays, Kansas 67601, (785) 625-3863 Cellular (785) 623-1700

December 15, 1998

Mr. Bill Robinson
Secretary of Energy
Washington, DC

Dear Secretary Robinson:

I am a small independent oil producer in Ellis County, Kansas. In the nearly 20 years that I have been in business I have put everything into my business, always keeping a close eye on expenses. Over the average of this time I have been able to make a reasonable living. There have been some good times and there have been some tough times. In the tough times we have always been able to cut a little here and a little there to get by.

This time things are different. There is no way we can cut any more to get by when it costs more to produce oil than what the product is worth. If I were totally debt free, it would still be impossible to make a living with these oil prices. All I want to be able to do is make a living and be able to help my boys through college.

Right now, I would shut down my wells and look for other work, but there are others who depend on me to make a living. Pumpers (those who look after the wells on a day to day basis) depend on me and other operators for work. They need producing wells to stay in business. Service companies and suppliers are finding it tough and some have closed their doors and laid off employees. The repercussions are also being felt by electrical service providers. Western Cooperative Electric draws more than 70% of their business from oil producers. A very high percentage of the wells they supply are shut down and more are being shut down each day. Again, this will mean more loss of jobs. So for now, I will operate at a loss while looking for the light at the end of the tunnel.

Ellis County depends very heavily on oil production for tax revenues. This year the valuations were down more than 30 million dollars and next year will be down even more. Where will the money be made up? It's put on other property owners, of whom I'm one, who can ill afford it.

It seems that Washington and the energy secretary are far removed from our plight. We are not asking for a hand out. All we are asking for is a sensible energy policy that will allow us to get a fair price for our product.

Many others are also writing letters and I'm sure you will get more of the same and in some cases even greater detail. I won't go on anymore because I'm sure that you understand what we are faced with. The purpose of this letter is to let you know that oil producers, pumpers, suppliers, service companies, electrical companies and tax payers need your help.

The Secretary of Agriculture has helped the farmer. Can the Secretary of Energy help the domestic oil producer?

A time of Christmas joy and celebration is certainly not that for anyone in the oil business.

Sincerely,

Jim D. Clark

Jim D. Clark

9-8

RONALD S. SCHRAEDER
212 N. Market, Suite 405
Wichita, KS 67202

December 14, 1998

Bill Richardson, Secretary of Energy
U.S. Department of Energy
1000 Independence Ave., S.W.
Washington, D.C. 20585

Dear Mr. Richardson:

I am a consulting petroleum engineer. I work for small companies that do not have an engineer on staff full time. I have been doing well completions, workovers to older wells, and prospecting for new wells since 1966. These are the worst economic conditions I have seen in the domestic oil business since I have been out of college.

Most of the small oil companies in Kansas have fewer than five employees, which is why I can stay busy most of the time. These companies have a handful of investors who love the oil business and are willing to "take a chance" to see if there is oil and gas under a lease. If the well "hits" they usually get their money back and make a little extra to try again. I am hired to set the production casing, perforate and stimulate the "pay" zone, and set the equipment so the well will recover the newly found reserves. All of this has come to a screeching halt!

Over the last six months Kansas independent oil companies have struggled to keep their doors open. I have lost half of my client companies because no company can profit at today's oil prices. Kansas is mostly an oil province with only the lower third of the state having gas reservoirs. In addition, Kansas is a mature producing area where literally tens of thousands of wells have been drilled since 1907. The major oil and gas fields have been found and mostly depleted. The larger companies have long since moved out of state. The independent oil producer is the last bastion between Kansas producing its own oil or having oil brought in from some other state or country.

We are now selling oil equivalent to prices that existed in the late 1970's. If we could roll back prices for the vehicles, equipment, transportation, services, parts,

9-9
~~9-10~~

chemicals, employee pay, and all o[illegible] myriad of other items that are 20 years higher in price, the oil business could withstand these prices better. But no industry can have the price on their product cut in half (or more) for any lengthy period of time and remain solvent. The oil business is no different.

You can not continue to allow cheap oil to flood into this county without the consequences of losing all of what remains of the independent Kansas oil companies. In addition, numerous communities also lose those associated service companies (mechanics, welders, dozer services, trucking services, water haulers, etc.) and their income. When oil companies are making money they spend money freely in the communities in which they live (homes, schools, restaurants, movies, etc.). All I see by having cheap oil is the fact that you can fill up the car with gasoline for less money. But that's at the expense of oil men leaving the country to invest in drilling deals elsewhere in the world. We lay off dozen here at home so we can spend money in some other country and hire a dozen of their people and put them to work. The revenues from oil and gas production are usually in the form of royalties and taxes when it comes to government income. Just think about what you are doing! By forcing the oil business out of this country to invest overseas, you are sending the government's royalty and tax incomes overseas as well. Fewer wells here-fewer government dollars. More wells there-more dollars for that government.

There's this expression going around: "Buy American". That means keep our people employed rather than some foreigner. It's now time to apply that to our oil business. Let's keep our investment dollars at home and see to it that our people come first. So it costs an extra dollar or two to fill up the car. At least we won't have to wait in line to do it some day.

Sincerely,

Ronald S Schraeder

Ronald S. Schraeder

9-10

Testimony of
Nicholas K. Powell, President
Colt Energy, Inc.
On H.B. 2009 - Sales Tax
before the House Committee on
Assessment and Taxation
January 20, 1999

Mr. Chairman and Members of the Committee:

My name is Nick Powell and I am an independent oil producer from Eastern Kansas appearing in support of House Bill 2009.

Oil prices are at an inflation adjusted 50 year low. I have employees that have been in the business for over 35 years and have never experienced this bad a situation.

Just last Friday we laid off 3 full time employees, dropped two employees from full time to part time and cut wages by 15%. Since last February, when we made our first cuts, we have dropped our work force from 33 full time to 20 full time and 2 part time. This is a reduction of over 33%. And this will only reduce our losses at the current price of oil. We will have to see a rise in the price, before we will break even on lifting costs of $12.00 per barrel. We are doing everything we can to hold on to our remaining employees, these are individuals with many years experience, who would be very difficult to replace.

In addition to the lay offs we have shut in or plugged 247 wells, which accounts for 37% of our producing wells and our production has dropped by 20% and our revenues are down 40% from a year ago.

I know that every night when our employees go to sleep they worry whether or not they will have a job when they go to work in the morning. Every morning I come to work and watch the price of oil to see if we are getting any relief wondering how long I can hold out until we have to make another round of lay offs, if the price doesn't recover. When our employees see the devastation to the oil industry they wonder if anybody understands what's going on. They see the farmers getting billions of dollars of relief from the government, talk of steel import quotas, but no talk of help to the oil industry.

The full removal of the severance tax on oil currently being considered would be a great help to many producers in our state. However, the removal of the severance tax on oil would not benefit most of the producers in Eastern Kansas, because of current exemptions for low producing wells. House Bill 2009 would be a direct benefit to Eastern Kansas producers at a time when every dollar counts. This proposed sales tax exemption, though not enough help to save our industry, would be a very welcome relief when an operator is trying desperately to keep their employees and their doors open. It would also serve the purpose to show the producers and their employees that the state has not abandoned them and that their representatives understand the situation we

HOUSE TAXATION
1-20-99
Attachment 10

are in and are trying to do everything they can to help.

This downturn in the price could be easier to deal with if, as in the past, it had only lasted 6 to 8 months. We are now in our 13th month of this devastating drop and from everything I read this will last for two to three more years. If this is true, there may not be much of an industry left in Kansas.

I have brought copies of an article which ran in the Kansas City, Star January 5th which does a good job of explaining the condition of our industry.

As I look at what is happening to the infrastructure of our industry and the devastating effect this oversupply of foreign oil is having on my company, It not only makes me mad, but also sick to think that two years from now my 16 year old son may find himself risking his life fighting a war in the Middle East to protect the foreign oil that is trying to drive me out of business.

Please support H.B. 2009 and let the producers know that someone understands our plight and is willing to help our industry, which has provided so much economic benefit to this State in the past and is in great need of help to survive into the future.

Thank you very much for the opportunity to speak to you today.

The dark side of cheap oil

SUSAN PFANNMULLER/Special to The Star

Declining oil prices have had a big effect on Nick Powell (left) of Colt Energy, who was forced to shut down oil wells and reduce Colt's work force last year. Powell sits with his son, David, at one of the company's oil rigs near 175th Street and Renner Road.

It aids consumers, but hurts owners of marginal wells

By ERIC PALMER
The Kansas City Star

As million-dollar missiles blasted Baghdad recently, Nick Powell had a flash of clarity about what this display of military might meant for his family.

And he felt sick.

In two years, Powell realized, it could be his son fighting in the Middle East. Sixteen-year-old David Powell could be risking his life to protect the foreign crude oil that has pushed small domestic producers such as his father's Colt Energy in Fairway to the brink of catastrophe.

"Don't ever think that is about anything but oil," Nick Powell said of the situation in Iraq. "What gets me as I sit here and lay off employees and shut down wells is that, because we allow our domestic oil business to go to pot, I may be asked to put my son into harm's way to fight a war over oil that competes with me."

Colt Energy has about 550 wells after closing 25 percent of its wells last year and reducing its 38-person work force by 11 positions as declining prices made its marginal wells unprofitable.

"The politicians are all wrapped up in how great it is to have cheap oil, but I see what it means because I'm in the business," Powell said.

Cheap oil certainly is good for the overall economy, most economists think.

The United States is enjoying the lowest inflation-adjusted gasoline prices in decades, prompting an economist with

See OIL, D-11

Source: New York Mercantile Exchange, Independent Petroleum Association of America

The Kansas City Star

10-3

OIL: Low prices put the squeeze on producers

Continued from D-1

NationsBanc Montgomery Securities to liken it to a tax cut for consumers. Energy-dependent companies such as airlines are reaping huge savings. And falling energy prices help keep inflation low and help offset lost sales in an economically depressed Asia.

"Most people are happy with things the way they are," said Russell Lamb, senior economist with the Federal Reserve Bank of Kansas City. "They don't want anyone to do anything that raises gasoline prices. In a macro sense, the positive outweighs the negative."

But there is a dark side to this windfall, warns Powell and other owners of the marginal wells in Kansas, the ninth most productive oil state. They can't stay in business for long at prices below $15 a barrel. Indeed, they are now getting about half that much.

That means a loss of jobs rural areas already whipped by depressed agriculture commodity prices. It means tax losses for the state. If the domestic industry dries up, it will mean America will have nothing to turn to if foreign producers cut the flow of oil as they did in the 1970s.

"It scares the heck out of me that we might become 70 to 80 percent dependent on foreign production. I would think we would see the price of gasoline skyrocket then," said Danny Biggs, vice president and partner in Pickrell Drilling Co. of Great Bend, Kan. As president of the National Stripper Well Association, Biggs recently sent an open letter to Congress pleading for help for his industry.

Crude business decisions

Prices of crude oil have been falling for more than a year, in part because Saudi Arabia and Venezuela were increasing production in a battle over market share, even as Asia's oil needs were reduced by its recession.

Prices on the New York Mercantile Exchange averaged $14.49 a barrel in 1998, down from $20.79 a barrel in 1997. Midwest producers get about $2.50 a barrel less.

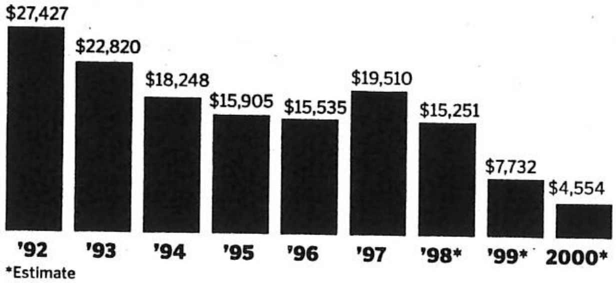
Local gasoline prices dipped into the 75-cent range for unleaded regular by early December. At the same time, oil behemoths Exxon Corp. and Mobil Corp. announced they would merge in an effort to deal with collapsing margins by cutting costs. The two said they would eliminate 9,000 jobs worldwide for an expected annual savings of $2.8 billion.

The same price drop has been squeezing the domestic oil market as the price paid falls below the cost of pumping it. In Kansas alone an estimated 10,280 wells were idled in 1998. Forty oil service companies have closed, costing an estimated

Slip, slipping away

Kansas has seen its taxes from oil production slide precipitously. Estimates for 1999 and 2000 suggest huge drops as low price of oil puts many Kansas oil producers out of business.

General fund taxes



Source: Kansas Department of Revenue

785 jobs, according to statistics from the Interstate Oil and Gas Compact Commission, a cooperative association of oil-producing states.

The implications for Kansas go much further than that, however, according to a report by the Kansas Corporation Commission. It estimated that the oil industry in Kansas saw the value of oil at the well drop by $400 million in 1998. It estimated a loss of 5,680 jobs in the state from less oil money.

More closures are expected now that the holidays are over. Powell and others said that once lost, many of those wells would never be brought back on-line, not even when oil prices rebound. They rue the loss of experienced oil field workers to other industries, saying they are losing the infrastructure essential to the domestic market.

Biggs explains that while Kansas producers can cut some costs, and have by laying off employees, it is hard to find cost savings on oil wells in Kansas that produce an average of only 2.7 barrels of oil a day.

"Even with low overhead, you have fixed costs," Biggs said. "We are seeing an oil industry that is just going to be gone if the price doesn't change. It's the same for other states like Texas, Oklahoma, Ohio, Kentucky and Illinois."

A marginal industry

According to the Independent Petroleum Association of America, about 85 percent of U.S. oil production comes from marginal, or stripper, wells — each of which produces 15 barrels of oil or less daily. However, those wells collectively produce about 1.3 million barrels of oil a day, equivalent to what the United States imports daily from Saudi Arabia.

The letter Biggs and the chairman of the Independent Petroleum Association of America sent to Congress asked that domestic oil producers get at least some of the same considerations as agriculture. Agriculture producers got about $11 billion in aid in 1998, including about $6 billion in emergency aid because of falling commodity prices.

The letter also said the United States was essentially subsidizing foreign oil with its military presence in the Middle East while running the risk of losing an industry that pays taxes and serves as a protection against foreign countries holding America hostage to their production.

Biggs and the chairman of the petroleum association are seeking tax credits that they estimate would cost the United States about $600 million over 10 years but that would help producers now. They want the U.S. Strategic Petroleum Reserve, a federal energy safety net, to acquire about $420 million in oil, in hopes that would help stabilize prices. They also want the United States to send a message to foreign producers that it "does not intend to stand by and lose its marginal well oil reserves to overproduction by foreign countries."

A spokesman for the Department of Energy said Secretary Bill Richardson had a department task force preparing recommendations and would make his suggestions on what to do about the situation later this month.

Ultimately, the producers are looking for action that will escalate the price of oil, and that will be a hard sell.

Fueling the economy

The pain felt by marginal oil producers is fueling at least a short-term gain for the economy.

The loss of marginal oil production is causing some "very intense pain in rural America," said Lamb of the Federal Reserve. But it is a "very localized pain that is overwhelmed by the hugely favorable economic conditions resulting from low oil prices."

Lower oil prices have got to be a factor in the rising sales of larger, more expensive automobiles and in the improved performance of industries such as aviation, Lamb said. He thinks it is hyperbole for independent producers to suggest wells that are capped now because they are unprofitable won't be reopened if prices rise.

The United States imports most of its oil from Venezuela, Canada, Mexico and Saudi Arabia. In recent years, when some oil-producing countries have tried to reduce production and raise prices, others have stepped in at lower prices to grab market share, Lamb said.

"I do not want to sound like I am dismissing it, but I think it would be a very hard sell politically to say we are going to buy up a lot of oil to push up oil prices and as a result have higher gasoline prices," Lamb said.

Bill Garrett, chief financial officer for Vanguard Airlines, can talk about the positive aspect of low oil prices.

"Without a doubt, jet fuel prices are the lowest they have been in the 1990s, and that translates into huge savings for us," Garrett said.

For example, Vanguard saved $300,000 on fuel in September when compared with prices it paid in September 1996, Garrett said.

At Trans World Airlines in St. Louis, the benefits of cheap fuel are more arresting. According to Security and Exchange Commission filings, TWA saved $75 million in the first nine months of 1998 because of reduced jet fuel prices.

Powell thinks the giddiness felt by Americans over cheap oil will easily turn to outrage, even fear, if oil-producing countries regain the will to raise prices. If the U.S. industry is allowed to languish, that scenario becomes easier, he said.

"There ought to be a serious debate about energy in the country," Powell said. "We are good at this type of discussion when prices are high, but you need to take a look at that when prices are low.

If foreign producers ever choke back supplies and gasoline prices soar, Powell said, "I tell you who will get blamed. The same oil companies that are saying we should save this industry.

To reach Eric Palmer, Kansas business editor, call (816) 234-7740 or send e-mail to epalmer@kcstar.com

10-4

LEGISLATIVE TESTIMONY

Kansas Chamber of Commerce and Industry web: www.kansaschamber.org

835 SW Topeka Blvd. Topeka, KS 66612-1671 (785) 357-6321 FAX (785) 357-4732 e-mail: kcci@kansaschamber.org

HB 2009 January 20, 1999

KANSAS CHAMBER OF COMMERCE AND INDUSTRY

Testimony Before the

House Tax Committee

by

Natalie Bright
Director of Taxation

Honorable Chair and members of the Committee:

My name is Natalie Bright and I am here on behalf of the members of the Kansas Chamber of Commerce and Industry (KCCI). Thank you for the opportunity to appear before you today to express our members' support for HB 2009.

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

KCCI is comprised of more than 3,000 businesses which includes 200 local and regional chambers of commerce and trade organizations which represent over 161,000 business men and women. The organization represents both large and small employers in Kansas, with 47% of KCCI's members having less than 25 employees, and 77% having less than 100 employees. KCCI receives no government funding.

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

In a 1996 survey, auditors for the Kansas Department of Revenue identified K.S.A. §79-3603 and K.S.A. §79-3606 as two of the most problematic sales tax exemptions the Department administers. In response to this survey, the Governor and the Department of Revenue introduced HB 2684 last session as an effort to clarify the sales tax exemption. Unfortunately, the bill did not receive

House Taxation
1-20-99
Attachment 11

er. ...n support to pass during the 1998 Legislative Session. However, the need to "fix" the exemptions has not subsided. At the encouragement of the Interim Committee on Assessment and Taxation, the Kansas Department of Revenue, KCCI, local chambers and several manufacturers formed a working group to develop the proposed changes encompassed in HB 2009.

The first issue addressed in HB 2009 is clarification of the existing standard used in administering the sales tax exemption for manufacturing machinery and equipment. Currently, the Kansas Department of Revenue requires manufacturing machinery and equipment to have a "direct and immediate effect" on the transformation of raw materials into the finished products. The "Ohio Rule", as this current method is entitled, has proven to be too difficult for both the taxpayer and the auditors to ascertain exactly what has a "direct and immediate effect" on a finished product. Today's manufacturing process is highly technical and as a result no longer simply involves a machine that has an ascertainable "direct effect" on the final product. As a result, the Department of Revenue has reported excessive litigation transpiring over the exemptions. Unfortunately, when a manufacturer has to litigate whether it qualifies for the exemption, the intended benefit is offset by the cost of litigation.

HB 2009 proposes adoption of the "integrated plant" theory that will broaden the manufacturer's exemption to encompass all machinery and equipment that constitutes an integral or essential part of the manufacturer's production process. By expanding the boundaries of the exemptions, its administration will be simplified, taxpayer's confusion cleared up and litigation over the exemptions eliminated. As a result, the true value of the intended benefit can be bestowed upon the taxpayer. In fact, adoption of the integrated plant will simplify the administration of the exemption and may even save tax dollars.

The next issue addressed in HB 2009 is an effort to eliminate confusing language contained in K.S.A. §79-3603 (m). Under current law, in order for property consumed in production to be exempt, it must be consumed "immediately." The proposed changes in HB 2009 will expand the definition to include property that is consumed within one year. If enacted, auditors will no longer have to su_ .ively interpret what is "immediately" consumed in production and manufacturers will hav clearer threshold as to what the exemption encompasses.

Finally, HB 2009 includes language to expand the existing exemption to include machinery and equipment used in the extraction of oil and gas. This proposal is an attempt to provide the ailing oil and gas industry with additional tax relief. Industry producers indicate this expansion will decrease exploration costs and offset the losses they are experiencing in their declining markets as well as grant exemptions consistent with those granted to other Kansas industries.

As Kansas continues to strive to compete with our neighboring states in the new millennium, it is changes such as HB 2009 that will set it apart from our neighboring states. By implementing HB 2009, manufacturers and producers will perceive Kansas as a favorable taxing environment and easily recognize the exemption benefits Kansas has to offer. **Currently, Kansas has 3,221 manufacturers who have made an investment and commitment to produce in Kansas.** By passing HB 2009, this Legislature will not only be simplifying a problematic exemption but has the opportunity to encourage manufacturers to continue their investment and commitment in the State of Kansas.

Again, the members of KCCI strongly support the implementation of an "integrated plant" method of assessing manufacturing machinery and equipment sales tax exemptions. Thank you for your consideration of HB 2009.

THE CHAMBER

Testimony to
House Taxation Committee
January 20, 1999

H.B. 2009

Bernie Koch
VP/Government Relations
Wichita Area Chamber of Commerce

Mr. Chairman, members of the Committee, thank you for the opportunity to appear today.

I'm Bernie Koch with the Wichita Area Chamber of Commerce. This issue is especially important to our area because of our strong manufacturing economy. Sedgwick County companies disburse about thirty-eight percent of the manufacturing wages paid in Kansas. Twenty-six percent of our work force is manufacturing. That's the fifth highest percentage in the country.

We support House Bill 2009. I've spoken to some medium and small manufacturers about his issue and I'd like to pass on their comments.

Leon Lungwitz is one of our members. He owns Staats Decals. Wichita has become a major center for the high tech manufacturing of decals that go on cars and other vehicles.

Leon notes that his company has put down an extra thick floor for certain pieces of equipment to eliminate vibration. He's also familiar with the need to install special electric lines to machines. You don't just plug this equipment into the wall. There can be a lot of expense associated with it.

I received the same comment from Patricia Kohler of JR Custom Metal. This is a longtime Wichita company that is family and minority-owned. JR Custom Metal is growing and will soon double its employment to 100 people.

Ms. Kohler tells me that large ovens are needed to dry and cure paint on the metal parts that the company manufactures. Under current law, it appears those ovens are subject to a sales tax exemption.

However, Ms. Kohler, like Mr. Lungwitz, does not know if equipment to bring electricity to large machines, such as the ovens, is subject to sales tax or not.

For many manufacturers, underground trenches are dug under the facility to carry electric lines, but JR Custom Metal has run into a problem. The water table at the plant is such that the company must go with something called overhead bus bars. Ms Kohler describes these as a kind of power strip that hangs from the ceiling. Her actual cost for these on

House Taxation
1-20-99
Attachment 12

new equipment will be $160,000. She's not clear if this is subject to sales tax, which in this case would be $9,440.

Finally, there's one more point in favor of clearing up the questions surrounding manufacturing sales tax.

The smaller manufacturers tell me one of their biggest problems is trying to keep up with all of the information they need to know to operate within the law. The executives at JR Custom Metal are currently evaluating their responsibilities as they expand. They don't have an attorney or a tax expert on the staff, so they are will probably have to go out of house to find the expertise to keep them out of trouble. For a small business, that's another expense.

So, beyond the taxation question, anything that simplifies their understanding will be helpful. This bill appears to address that understanding in a very comprehensive manner.

Thank you again for the chance to appear today.

STATEMENT TO
HOUSE TAXATION COMMITTEE
January 20, 1999

Bill Barnes
President, Kansa Corporation
Emporia, KS

On behalf of Kansa Corporation, I am pleased to offer my comments on the proposed modifications concerning the sales tax on manufacturing machinery and equipment as contained in HB2009. As background, three individuals who purchased a product (a machine to mechanically insert or stuff various advertisements or sections into a newspaper) from another company in Emporia founded Kansa Corporation in 1977. The company manufactures material handling equipment for the newspaper and commercial printing industries. In 1989 the company was sold to Baldwin Technology. Our products are sold all over the world and we currently employ almost 70 people, all of whom live in Kansas. Our annual payroll is over two million dollars.

I certainly appreciate the positive changes the state legislature has made over the past few years as it relates to taxes on manufacturers. The elimination of the tax on inventory, the elimination of the sales tax on the purchase of production machinery and equipment, and the moratorium on unemployment tax have all been positive investments for Kansas manufacturers. The collective impact of these positive tax changes has been significant for Kansas businesses. We are seeing the benefits of these investments today. The Kansas economy is extremely strong with the employment rate at record highs. You can not open a newspaper without seeing page after page of want ads.

The sales tax modifications you are considering are another positive step to help Kansas manufacturers compete in the global environment of today. It is amazing how many small Kansas manufacturers are international or have international competitors. Over 30 percent of our sales for this fiscal year have been international to include sales to companies in Belarus and Saudi Arabia. Our three major competitors are foreign based. The changes being proposed help us in two ways. First, they simplify something that is complex. Second, they help reduce our costs. Simplifying laws and reducing costs are extremely important to all business but its impact on small manufacturers can be huge.

The parts of this proposed legislation that impact my company the most are the exemption for repair and maintenance services on production equipment, the exemption for "consumed in production" and to define the sales tax exemption as an integrated production process. Dollars we can save here allow us to invest more dollars in research and development, new equipment, and our employees. As I mentioned earlier, we are owned by another company who owns other companies not only in the United States but also in other countries around the world. Periodically our parent company evaluates where they should locate product lines. One of the sister companies we are compared to is located in California. The changes Kansas has made with sales tax exemptions have helped give us a competitive edge when our two plants are compared. We are currently in discussions to determine if a product line should stay in California or be moved to Kansas.

This proposal is another positive step to help manufacturers in Kansas stay competitive. The changes I mentioned earlier have allowed my company to double its company's research and development budget. This is an investment Kansa is making to allow us to be competitive in the future and provide good jobs for our employees. I urge you to favorably consider these positive changes to the sales tax law. This investment will also help maintain Kansas's good economic climate. Thank you for your time in allowing me to present a small manufacturer's view on this important subject.

House Taxation
1-20-99
Attachment 13

January 20,1999

TESTIMONY ON HB 2009 BEFORE THE HOUSE TAXATION COMMITTEE

Good morning Representative Adkins and Committee Members, I am Frank Meyer President and co-owner of Custom Metal Fabricators in Herington Kansas.

We are a small family owned corporation with 45 employees. This year as in past years over 35% of our production was exported, going to Sweden, Argentina, Romania and other countries. Over the years we have shipped equipment to over 30 countries around the world.

I am grateful for the opportunity to be here today, first of all to thank you for the legislation you passed a few years back giving Kansas manufactures sales tax relief on machinery and equipment used to transform raw material into new products. This Legislation made Kansas Manufactures, more competitive with companies in other States and overseas.

Today our investment in real estate, buildings, Machinery, Equipment, tooling and other items needed to produce "World Class" products is over $90,000 per employee.

As you can see prior to the passage of K.S.A. 79-3606(kk) paying a $6,000 penalty to the State every time we created a new job had a negative effect on our ability expand our operation, hire more people and compete on the world market. So what you have done for us and the Kansas economy is much appreciated.

Now, if I may, let me show why we need to do a little more work to develop the full potential of Kansas manufacturers to compete world wide.

What I have is the skyline of Chicago.

> The Machine that cut the blank and all the holes cost $400,000 and as I understand current law is sales tax exempt.
>
> The machine that bent the metal cost $100,000 and as I understand current law is sales tax exempt.
>
> The computer hardware and software our engineering department used to design the part and send commands to the computerized machinery so it can cut and form the part cost $125,000.
>
> Now the problem, my accountant says "you need to pay sales tax on the $125,000".

House Taxation
1-20-99
Attachment 14

My lawyer says "don't pay the tax and we will litigate it".

When I ask him what that would cost he smiled and said "oh $25,000 -- or more if we go to the supreme court."

Another example:

One of our product lines is machinery and equipment for grain elevators. If we sell a machine to a Kansas elevator that has a feed mill as part of their operation they must determine if it will be used in the feed mill which produces a product or is part of the machinery that loads grain for outbound shipment.

or what tax do they pay if it is used in both operations?

I could go on and on but I am sure you see current law, while it improves the competitive advantage of Kansas manufactures, needs the clarification included in the proposal you have from the department of Revenue and I urge it's passage.

Thank You for all the time and hard work you do for the people of Kansas.

Do you have any questions?

SUPERIOR

SUPERIOR INDUSTRIES INTERNATIONAL, INC.
1500 E 27th TERRACE • PITTSBURG, KS 66762
(316) 232-3344 • FAX (316) 232-3323

House Taxation Committee

RE: HB 2009

I am David Mauersberger, Controller for Superior Industries International located in Pittsburg, Kansas. Superior Industries is a cast aluminum wheel manufacturer for the auto industry.

First of all, I would like to thank you for the opportunity to speak before you on taxation of manufacturers, or rather, exemption from taxation.

Manufacturers have been waiting way too long for changes to KSA 79-3606 (kk). The 1988 statute was too limited in its exemption. The statute, besides being limited, was vague and ambiguous in its language. Manufacturers were sometimes paying taxes on items that were exempt by the interpretation of the Office of Policy and Research within the Department of Revenue. However, through an audit by the Department of Revenue, you could run into conflicts. The auditor would say the item was taxable, but the Office of Policy and Research said it was exempt. Therefore, manufacturers depended on private letter rulings for interpretation of the statute. I would say that, in most cases, manufacturers overpaid in sales taxes.

Changes in the statutes are definitely needed – broadening the exemptions to manufacturers will benefit economic growth and development in the state of Kansas. To increase revenues means broadening the tax base. Kansas needs to improve on the incentives for new and existing businesses and stay competitive with the surrounding states. This all means economic growth. Lowering the sales taxes would give the potential for expansion of existing manufacturers and attracting new manufacturers to locate in Kansas. This would ultimately result into a broader base for Corporate Income taxes. Business is very competitive in today's environment. In order to be competitive, a manufacturer needs more than what just the leading edge technology offers.

Exemptions were limited to materials consumed in the process or an ingredient or component part of the product. Last July, the exemption was broadened to include repair and replacement parts, including but not limited to: belts, drill bits, grinding wheels, cutting bars, saws, dies, jigs, and molds. This was a big improvement but needs to go further. This change in expanding the exemptions was very beneficial and important to Superior Industries, as well as most manufacturers. We have high expenses in these new exempt areas.

House Taxation
1-20-99
Attachment 15

Superior Industries, like many other manufacturers, have support machinery and equipment that repair: tools, dies, molds, forms and other parts of qualified machinery and equipment. The exemption should include all support machinery for operation of a manufacturing facility and equipment and tools used primarily in maintaining and repairing already exempted machinery and equipment. The purposed bill would encompass these other components of manufacturing, giving manufacturers the added benefits for growth. The support machinery and equipment is essential to the manufacturing process – can't have one without the other. This would reflect the integrated plant theory.

In summary, Superior Industries supports the proposed HB 2009 and would like to see this bill pass through the legislature in this session.

T ony before the House Taxation Committee

January 20, 1999

By: Dennis J. D'Orvilliers
Engineering Technology Leader
Goodyear Tire & Rubber Company / Topeka Plant

Chairman Adkins and members of the committee, my name is Dennis D'Orvilliers. I am the Engineering Technology Leader for Goodyear's Topeka Plant. I would like to express our support for House Bill 2009. Goodyear supports: 1) expansion of the exemption for property which is "immediately" consumed to property which is consumed within one year; 2) expansion of the manufacturing and machinery 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; and 3) exemption of 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.

Additional Comments:

1. The Goodyear Topeka Plant currently pays approximately $400,000 in sales tax per year. Adopting the above changes would yield an estimated $100,000 improvement in our tax liability (per Vince Magnacca, our corporate sales tax expert). During an expansion project (like we have going on right now) the savings figure would be somewhere around $200,000 depending on the size of the expansion project.

2. The adoption of this proposal is not a new idea in the other states where Goodyear does business, in fact, Kansas is the only state that hasn't adopted these kinds of exemptions. Our sister plant in Danville, Virginia pays $0 for sales tax on equipment and labor. Acceptance of this would only put us on a more even playing field with other Goodyear plants and those manufacturing facilities of our competitors.

3. We request speedy adoption of this proposal and encourage consideration of expanding the Kansas Income Tax Credit on our property taxes from 15% to 20%. This proposal could become a very substantial amount of tax relief. Last year Goodyear Tire and Rubber Company paid approximately $10 million in property taxes nationally, of that amount the Topeka Plant paid (or will pay) approximately $2 million for 1998. The additional 5% would mean approximately $100,000 in additional tax savings in 1998.

4. Add up the estimated savings from both proposals for 1998 would result in a tax liability reduction of $200,000. That translates into a lower cost of operations and more contribution towards Goodyear's growth. We would be more competitive in our markets and better positioned for additional plant expansions which brings more jobs. These changes would benefit all Kansans.

House Taxation
1-20-99
Attachment 16

K A N S A S G R A I N & F E E D *Association*

Statement of the

Kansas Grain and Feed Association

to the

House Taxation Committee

Regarding H.B. 2009

Representative David Adkins, Chairman

January 20, 1999

KGFA, promoting a viable business climate through sound public policy for more than a century.

House Taxation Committee
1-20-99
Attachment 17

The Kansas Grain and Feed Association....
....a voluntary state organization founded in 1896 providing governmental representation, educational opportunities and a wide variety of professional services to the vast and indispensable grain and feed industry. The 1150 member firms of the KGFA include country elevators, terminal elevators, flour mills, feed manufacturers, grain merchandisers and allied industries.

Chairman Adkins and Members of the House Taxation Committee, my name is Doug Wareham and I am Vice President, Government Affairs for the Kansas Grain and Feed Association (KGFA). The KGFA is a voluntary state association with a membership encompassing the entire spectrum of grain receiving, storage, processing and shipping industry in the state of Kansas. Our membership includes over 1,250 Kansas business locations and represents 99% of the commercially licensed grain storage in the state.

I appear today in support of House Bill 2009 and respectfully request positive consideration of this bill. During the past year other representatives of our organization and I have worked closely with other supporters of this bill and staff from the Kansas Department of Revenue to address a long-standing area of concern for the Kansas grain storage and handling industry. In 1991 and 1992 our organization challenged a ruling by the Kansas Department of Revenue regarding the exemption from sales tax of energy used in grain aeration, turning and blending which had been rescinded by KDR. Our organization challenged KDR's ruling that had denied our exemption and eventually won a Supreme Court ruling in favor of our position.

While the supreme court ruling ended a long and costly debate with KDR in the early 1990's, the language proposed in House Bill 2009 goes one step further by providing a much clearer interpretation of the exemptions that currently apply to the Kansas grain industry regarding the sales tax on energy consumption for grain aeration, turning and blending. We have had House Bill 2009 reviewed by our tax attorney, Carol Bonebrake, a former Kansas Department of Revenue attorney and have received her assurance that House Bill 2009 protects and strengthens the ruling of the Kansas Supreme Court.

We have appreciated the open process which led to the development of this bill and commend the Kansas Department of Revenue for their cooperative spirit when we asked for clarifications and provided recommendations during the development process for House Bill 2009.

Again, I appreciate the opportunity to testify in support of House Bill 2009 and ask that you consider this bill favorably. I would be happy to answer any questions at this time.

Testimony Before the
House Taxation Committee
January 20, 1999

House Bill 2002

By
Robert B. Leake
Managing Consultant
Allen, Gibbs & Houlik, L.C.

My name is Robert Leake. I am with the CPA/Consulting firm of Allen, Gibbs & Houlik, L.C. based in Wichita, Kansas. I specialize in sales and use tax consulting. Before joining Allen, Gibbs & Houlik, L.C. in 1996, I was the Sales & Excise Tax Manager for Koch Industries, Inc. for over 15 years.

My firm has many manufacturing clients within the south central Kansas area. These clients are engaged in manufacturing aircraft interiors, aircraft parts, aircraft instrumentation, automotive parts, lawnmowers, printed materials, chemicals and plastics. While my firm has performed sales and use tax work for some of the largest manufacturers in Kansas, our typical manufacturing client employs less than 100 people and has sales of less than 25 million dollars per year. The types of clients we generally serve are companies like Moridge Manufacturing in Moundridge, Sigma Tek in Augusta, Southwest Publishing in Topeka, Abbott Laboratories in McPherson, Jensen International in Coffeyville and Westland Corporation in Wichita.

A year ago, I appeared before this committee to speak in favor of the "integrated plant theory" exemption. It was, however, with some degree of qualification. That qualification was directed toward the Kansas Department of Revenue and the rather "narrow interpretations" they have concerning Kansas sales and use tax exemptions.

This committee is considering whether or not to recommend this exemption for passage by the Kansas Legislature. Tax exemptions should **not** be passed in order to benefit just one particular business sector. Rather, for an exemption to be passed it should benefit the State of Kansas as a whole more than the cost of the reduced tax revenues to state coffers.

If exemptions are not comprehensive in their application, clear in their understanding and simple to explain to the average taxpayer, similar taxpayers will not be treated the same. To the extent that a taxpayer is denied access to a tax exemption because of an erroneous or narrow interpretation or simply an oversight on the part of the taxpayer, the effect is the same. The benefit to the State of Kansas for having that tax exemption in the statute books is reduced.

I feel that the changes to the machinery and equipment exemption and the consumed in production exemption being considered by this committee will ultimately simplify the tax administration for taxpayers and the KDOR. Further, these changes will be beneficial for

House Taxation
1-20-99
Attachment 18

the Kansas economy and manufacturing employment in this State. Manufacturing typically brings in money from outside our state for goods made here and generally pays better than the average. The benefits from manufacturing to the State of Kansas clearly exceed the loss of tax revenues.

There are three primary beneficial aspects to this legislation:

First, the extension of the exemption found in KSA 79-3606kk to include services being performed on exempt machinery is certainly a positive step. Currently, there is confusion between on-site exempt fabrication labor of an exempt machine and the taxable installation labor. This would simplify that matter. Additionally, many states do not apply sales tax to repair or installation labor services at all. Therefore, specifying that all labor services are exempt will reduce conflicts between taxpayers and the KDOR and permit Kansas manufacturers to remain competitive with their counterparts in other states and countries.

Second, the expansion of the exemption to "machinery and equipment used as an integral or essential part of an integrated production operation" makes the exemption more comprehensive and easier to understand. The current exemption pertains only to machinery and equipment that comes into direct contact with the product being produced. The proposed legislation also includes pre-production machinery and equipment; machinery and equipment used prior to the start of the production line; pollution control equipment; and other ancillary items that normally would be considered part of the building. This includes items such as clean rooms, foundations for machinery, electrical wiring and piping for gas, water and air within the plant. Hopefully, the comprehensive nature of this proposed exemption will translate into a better general understanding among Kansas taxpayers. This will in turn result in greater utilization of the exemption and a greater benefit to the State.

Finally, the establishment of a "one year" time period for an item to qualify for exemption under the "consumed in production" is another beneficial aspect of this proposed legislation. The current statute does not contain a defined time period. Therefore, the Kansas Supreme Court has determined that items would qualify if consumed over a time "reasonably requisite." What the Court means by this term is that welding gases which are consumed instantaneously and platinum which has a useful life of two years when used in oil refinery would both qualify under this exemption. It is only important that consumption begin immediately. While this should be theoretically easy to apply, legal distinctions like these are probably lost on the average taxpayer. Therefore, imposing a "one year" time period makes sense and ensures that this exemption can be fairly applied.

No legislation is completely perfect, including this one. Nevertheless, this should go a long way toward providing manufacturers with <u>simple</u>, <u>clear</u> and <u>comprehensive</u> exemptions that they can apply to their business.

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KRMCA

Kansas Ready Mixed
Concrete Association

Edward R. Moses
Managing Director

Testimony

By The

Kansas Ready Mixed Concrete Association

Before the

House Taxation Committee

Regarding HB 2009

January 20, 1999

Good morning, Mr. Chairman and members of the committee, my name is Edward R. Moses, Managing Director of the Kansas Ready Mixed Concrete Association.

The Kansas Ready Mixed Concrete Association (KRMCA) is an industry-wide trade association comprised of over two hundred fifty (250) members located in all one hundred and sixty five (165) legislative districts in this state, providing basic building materials to all Kansans. Primarily engaged in the manufacture and placement of ready mixed concrete.

We thank you for the opportunity to provide our comments and conditional support of HB 2009. The genesis of this bill is the result of an effort to more clearly define what is commonly called the "integrated plant process" and the tax incentives that may be applied to this process. We appear before you today as an industry whose members are intimately effected by the provisions addressed in this bill. While we are in general support of the broad themes outlined in the bill, we ask you to consider certain amendments to more clearly define your intentions with respect to its application to our industry. In order to do this we make the following suggestions offered in a draft balloon attached to this testimony.

First we would suggest the insertion of the language "mobile concrete mixer trucks" to more clearly indicate the intent of this measure to exempt sales tax on the purchase of

House Taxation
1-20-99
Attachment 19

integrated truck chassis and mixers acquired specifically for the purpose of manufacturing concrete. We are requesting this for the following reasons:

1. Such language would clarify that concrete mixer trucks are a part of the ready mixed concrete production process cited on page 15, line 6. The manufacture of concrete begins with the initial mixing of aggregate, cement, and water in very specific proportions. This mixing then starts a catalytic reaction, which results in the free lime contained in the cement being hydrated and coating the aggregate to eventually form a solid bond. This process usually takes 28 days to complete. During the first part of the process (usually taking less than an hour) it is necessary to mix these ingredients in a mixer unit attached to a truck. The remainder of this process requires placement and finishing at the job site. As it is obviously necessary to mix the product and get to the jobsite where it can be finished and sold we think a sales tax exemption for the equipment to make this possible is appropriate.

2. Concrete mixer truck sales tax exemptions under the integrated plant process theory are currently recognized in many states including Illinois, Indiana, and Mississippi; but most notably in the state of Missouri. Here our members are forced to compete with Missouri producers who enjoy a sales tax exemption on the purchase of their concrete mixer trucks. This is particularly harmful in the Johnson, Wyandotte and Leavenworth counties where Missouri producers (operating under prorated tags) may deliver concrete with no other restriction or requirements. Approval of this amendment and this bill would assist in reducing the competitive advantage currently enjoyed by Missouri producers.

3. Finally, adoption of clear language would assist in resolving conflicts we have had with the Kansas Department of Revenue.

The second change we recommend is more technical in nature. It is suggested the word "portable" be substituted for the word "movable", as this is the term common to the industry. Almost any plant including a 750' cement kiln may be "moved" but is not necessarily is or designed to be "portable". Making this change would narrow the focus of this exemption and improve clarity.

We applaud the efforts of the Special Committee on Taxation in the drafting and introduction of this bill. Passage of HB 2009 will assist greatly in the administration and application of sales tax exemptions granted under the integrated plant process theory. Simple and understandable tax laws assist both regulators and the regulated. We urge you to make HB 2009 even more clear through the adoption of our proposed amendments and its being recommended favorably for adoption as amended by this committee

Once again, thank you for the opportunity to come before you today. I will be happy to respond to any questions you may have.

19-3

ufacturing or processing business to manufacture or rebuild tangible personal property that is used in manufacturing or processing operations, including tools, dies, molds, forms and other parts of qualifying machinery and equipment; (C) oil and gas drilling services and supplies, and drilling, pumping and monitoring equipment, used at a well site or in oil and gas exploration; (D) ~~movable batching~~ plants for aggregate, concrete, bulk cement, ~~and~~ asphalt; (E) industrial fixtures, devices, support facilities and special foundations necessary for manufacturing and production operations, and materials and other tangible personal property sold for the purpose of fabricating such fixtures, devices, facilities and foundations. An exemption certificate for such purchases shall be signed by the manufacturer or processor. If the fabricator purchases such material, the fabricator shall also sign the exemption certificate; and (F) a manufacturing or processing business' laboratory equipment that is not located at the plant or facility, but that would otherwise qualify for exemption under subsection (3)(E).

Insert comma

portable

and

Mobile concrete mixer trucks;

(5) "Machinery and equipment used as an integral or essential part of an integrated production operation" shall not include:

(A) Machinery and equipment used for nonproduction purposes, including, but not limited to, machinery and equipment used for plant security, fire prevention, first aid, accounting, administration, record keeping, advertising, marketing, sales or other related activities, plant cleaning, plant communications, and employee work scheduling;

(B) machinery, equipment and tools used primarily in maintaining and repairing any type of machinery and equipment or the building and plant;

(C) transportation equipment not primarily used in a production, warehousing or material handling operation at the plant or facility;

(D) office machines and equipment including computers and related periheral equipment not used directly and primarily to control or measure the manufacturing process;

(E) furniture and other furnishings;

(F) buildings, other than exempt machinery and equipment that is permanently affixed to or becomes a physical part of the building, and any other part of real estate that is not otherwise exempt;

(G) building fixtures that are not integral to the manufacturing operation, such as utility systems for heating, ventilation, air conditioning, communications, plumbing or electrical;

(H) machinery and equipment used for general plant heating, cooling and lighting;

(I) motor vehicles that are registered for operation on public highways; or

(J) employee apparel, except safety and protective apparel that is pur-

Balloon amendment proposed by Kansas Ready Mixed Concrete Association

STATEMENT

BY KANSAS MOTOR CARRIERS ASSOCIATION
P.O. Box 1673 ▪ Topeka, Kansas 66601
Telephone: 785-267-1641 ▪ FAX: 785-266-6551 ▪ www.kmca.org

Requesting an amendment to House Bill 2009

Appearing before the House Taxation Committee
Representative David Adkins, Chairman
Wednesday, January 20, 1999
State Capitol, Topeka, Kansas

MR. CHAIRMAN AND MEMBERS OF THE HOUSE TAXATION COMMITTEE:

My name is Tom Whitaker, director of governmental relations and membership services for the Kansas Motor Carriers Association. I appear here this morning representing our 1,400 member firms and the Kansas trucking industry.

We are here today to request your favorable action on an amendment to House Bill No. 2009. In 1998, the Graves administration requested introduction of House Bill No. 2643, the "sales tax relief and reform act of 1998." Included in the original legislation was an amendment to K.S.A. 79-3606(f), which reads:

> (f) Tangible personal property purchased by a railroad or public utility for consumption or movement directly and immediately in interstate commerce, *and services for the installation or application there of;*

Currently, for-hire interstate motor carriers are considered public utilities. The original language to this section pre-dates 1947. In 1980, the railroads were granted a sales tax exemption for labor services. It is unclear why public utilities (i.e. motor carriers) were not included at that time.

Thirty-two states provide an exemption from sales tax on labor services provided to interstate for-hire motor carriers when such labor is used to repair or service motor carrier rolling stock. All of the states contiguous to Kansas provide this sales tax exemption. This puts Kansas truck repair and servicing facilities at a competitive disadvantage to the surrounding states.

When the exemption was proposed in 1998, the Kansas Department of Revenue estimated the fiscal note at between $300,000 and $500,000. We believe, however, that adoption of the expanded sales tax exemption will place Kansas on a competitively equal footing with its neighboring states, and provide needed tax equity for the motor carrier industry.

We thank you for the opportunity to appear and ask or your favorable consideration of our request when the Committee takes action on House Bill No. 2009. I will be pleased to respond to any questions you may have.

KANSAS KMCA Kansas Motor Carriers Association MOVES BY TRUCK

House Taxation
1-20-99
Attachment 20

THE CHAMBER

Greater Kansas City Chamber of Commerce

The Honorable David Adkins
Chairman, House Taxation Committee
State Capitol
Topeka, KS 66612

January 20, 1999

Dear Mister Chairman and Committee Members:

As Chairman of The Greater Kansas City Chamber of Commerce Kansas State Affairs Committee, I am writing to express The Chamber's strong support for HB 2009, expanding the state sales tax exemption on sales of machinery and equipment used in manufacturing.

Passage of HB 2009 would not only result in tax savings for many Chamber members and manufacturers statewide, it would also clarify and simplify a confusing area of Kansas tax law. Tax simplification is a top legislative concern of Chamber members. The clarifications in this bill will make an important economic development tool more useful for manufacturers existing in Kansas and manufacturers looking to relocate to the state.

For purposes of tax simplification and tax savings, The Chamber respectfully urges the House Taxation Committee to recommend HB 2009 favorably for passage.

Thank you in advance for your consideration of The Chamber's position on HB 2009. Please contact Jenny Unruh at The Chamber, 816/374-5412, or me at my Overland Park law office, 913/344-8039, if you have any questions.

Sincerely,

Robert Vancrum
Chairman, Kansas State Affairs
Committee

Greater Kansas City Chamber of Commerce | 2600 Commerce Tower • 911 Main Street • Kansas City, Missouri 64105-2049
816/221-2424 • FAX 816/221-7440 • www.kcchamber.com

HOUSE TAXATION
1-20-99
Attachment 21

Mid-America Tire Dealers Association

STATEMENT

OF THE

MID-AMERICA TIRE DEALERS ASSOCIATION

BEFORE THE

House of Representatives
Taxation Committee

Wednesday, January 20, 1998

Mr. Chairman and Members of the Committee:

My name is Shawn Herrick, Executive Director of the Mid-America Tire Dealers Association (MATDA). I am submitting testimony on behalf of the Board of Directors and the membership of the MATDA. Thank you for allowing us to express our position.

The Mid-America Tire Dealers Association is an organization dedicated to the promotion of the image and progress of the tire industry in Kansas and Nebraska. MATDA was incorporated in 1990, and represents over 150 business members and their employees.

The MATDA membership requests language be added to HB 2009 that would expand the current exemption from sales tax for repair parts installed on the rolling stock of common carriers to include the labor services involved in the repair as well.

The number one reason for this request is that there now exists a competitive disadvantage for Kansas dealers because all four surrounding states do not charge this tax.

Also, it is cumbersome and confusing to taxpayers to understand why parts and labor are treated differently in Kansas. This often creates controversy between tire dealers and their customers.

In the 1998 Legislative session, the Governor proposed House Bill 2643, which would have accomplished these changes to the sales tax statutes if it had passed in its entirety.

Also, according to testimony presented in July, 1998 by Shirley Sicilian, Director of Policy & Research for the Kansas Department of Revenue, the Governor and the Department continue to support these initiatives. According to that testimony, the fiscal note of these changes would not be substantial.

With the addition of this language, we support HB 2009. Thank you for allowing me to express our concerns.

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HOUSE TAXATION
1-20-99
Attachment 22