

Approved: 2-22-99  
Date

MINUTES OF THE SENATE ASSESSMENT AND TAXATION COMMITTEE.

The meeting was called to order by Chairperson Senator Audrey Langworthy at 11:10 a.m. on February 18, 1999, in Room 519-S of the Capitol.

All members were present except: Senator Lee

Committee staff present: Chris Courtwright, Legislative Research Department  
April Holman, Legislative Research Department  
Don Hayward, Revisor of Statutes Office  
Shirley Higgins, Committee Secretary

Conferees appearing before the committee: Greg Millert, AT&T  
Kevin Kongs, Western Resources  
Mark Beshears, Sprint  
Shirley Sicilian, Department of Revenue

Others attending: See attached list.

**SB 185—Income taxation; authorizing credits for property tax paid by certain telecommunications companies.**

Greg Millert, AT&T, testified in support of **SB 185** which proposes an income tax credit equal to the difference between the public utility assessment rate and the general business rate and which would be phased in over a four-year period. Mr. Millert pointed out that the emergence of a highly competitive industry and the development of sophisticated private networks were not contemplated when the public utility definitions found in the property tax statutes were drafted for telephone companies. He contended that telecommunications providers should be assessed property and other taxes at the same rate and in the same manner as general business. He noted that there are currently only eleven states, including Kansas, whose statutes continue to provide for the disparate property tax treatment of the telecommunications industry. In conclusion, Mr. Millert emphasized that **SB 185** is an important step towards allowing Kansas consumers to continue to receive telecommunication services at reasonable and affordable rates. (Attachment 1)

Kevin Kongs, Western Resources, followed with further testimony in support of **SB 185** as an attempt to alleviate some of the tax disparity between state assessed telecommunications companies and other commercial and industrial companies. He noted that the same disparity exists between electric companies and other businesses in Kansas; therefore, he asked that public utilities be included in **SB 185**. He called attention to a copy of a proposed amendment which offers the benefits of the income tax credit to all public utilities. (Attachment 2)

In response to questions regarding the fiscal note on Mr. Kongs' suggested amendment, Shirley Sicilian, Department of Revenue, noted that the Department estimates that \$25 million in local revenue is at stake if a move from 33 percent to 25 percent is made on generation property, which accounts for most of electric utility property. If the credit is phased in at 25 percent on just the generation property, the approximate fiscal note would be \$6.25 million the first year. Fully phased in, the approximate fiscal note would be \$25 million.

Mark Beshears, Sprint, gave final testimony in support of **SB 185**. He reiterated that the current policy in Kansas of taxing some telecommunications companies at 33 percent and other companies at 25 percent is inherently discriminatory and creates an economic disincentive for investing in Kansas. Sprint is creating a product line which will allow customers to choose from a wide range of services bundled together as an integrated product. He believes those services should be valued, assessed, and taxed in a similar manner and at a similar rate. (Attachment 3) At the completion of Mr. Beshears' testimony, the hearing on **SB 185** was closed.

The meeting was adjourned at 11:30 a.m.

The next meeting is scheduled for February 22, 1999.



# SENATE ASSESSMENT AND TAXATION COMMITTEE GUEST LIST

DATE: February 18, 1999

NAME	REPRESENTING
Cory Miller	AT&T
WILLIAM DVOŘÁK	AT&T
Mark Bank	KDOR
S. Scifano	KDORev.
Phil Alquist	TAXPAYER
Don Schwack	KIOGN
Jack Graves	Duke & N. Eng. & Oly
Jon & Miles	KEC
Doug Lauer	SWBT
Mike Murray	Sprint
Carolyn Gusten	Sprint
Man Hamann	Div. of the Budget
Rob Hodges	KTIA
John Pinegar	SITA
GREGG SVOBODA	SWBT
CAROL DEASON	WESTERN RESOURCES
Kevin Fong	Western Resources
Dave Holburn	Western Resources
Shane Hagelin	Sen. Stephens staff



**Greg Millert**  
Vice President  
External Tax Policy

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Testimony of Greg Millert on Behalf of AT&T  
Before Senate Assessment and Taxation Committee  
Senate Bill No. 185  
February 18, 1999

Madame Chairman, members of the Committee, good morning. My name is Greg Millert. I am the Vice President for AT&T's External Tax Policy organization with responsibility for tax legislative affairs. I appreciate the opportunity to appear before you today to testify in support of Senate Bill 185. AT&T supports the goal of eliminating the disparate property tax treatment of telecommunications providers that exists today. Senate Bill 185 is a first step in keeping Kansas current with other states in regards to the taxation of telecommunications providers. This bill proposes an income tax credit equal to the difference between the public utility assessment rate and the general business rate. The income tax credit would be phased-in over a four-year period.

Telecommunications represents one of the fastest changing industries in the United States economy. This rapid change presents a challenge for Kansas policy makers: how to ensure that a tax system for a continually evolving industry fairly taxes companies while promoting, or at least not hindering, new investments in telecommunications technology. In recognition of these changes and in line with basic fairness and equity in taxation, there should be a modification to the current system. I appreciate the opportunity to share with you AT&T's view of why current tax policy should be revised to recognize these fundamental market changes.

Modern telecommunications enhances everyone's life. We can be better educated, better informed, more productive, and more diversely entertained than a generation or even a decade ago. And yes, we can reach out to a wider circle of friends in less time and in different ways. Indeed, one of the most significant of the qualitative changes now occurring is that the digitized intelligence previously available only to the richest and most powerful of society is rapidly coming down the pipeline to much wider sectors of the population. From the imaginings of Jules Verne to the cartoon wonders of the Jetsons, the visions of science fiction are starting to become practical realities. We are at a point in time where highly intelligent, enormously powerful, and easily usable computers and communications devices proliferate.

One of the most important lessons that economic history teaches us is that commerce centers around points of origin, destinations or links between points. Successful development, however, also requires the establishment of an infrastructure to support economic expansion. Many early American cities developed around shipping centers with access to the ocean. Railroads furthered the economic expansion during the late eighteenth and early nineteenth centuries, hence the growth of towns like Kansas City, Topeka and Wichita. The growth of the U.S. economy since World War II can be tied to the popularity of motor vehicles and

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Attachment 1*

continued building of the highways and mass transportation systems. Think of the importance of Interstates 35 and 70 to the Kansas economy.

Today's economy is no different except that the lifeblood of today is not oceans, railways, or interstate highways; instead, it comes from the ability to transport information through telecommunication networks. According to an article published in the "*New York Times*":

"Just as centers of commerce sprang up along navigable rivers, around natural harbors and parallel to railroad tracks and major roads in earlier centuries...The commercial hubs of the next millenium will take root around pipelines that carry torrents of computer data."

Clearly, the ability to communicate quickly and seamlessly will drive economies in the twenty-first century. Technological advances have increased the portability of telecommunications equipment to such an extent that certain types of equipment can easily be placed outside Kansas to serve Kansas customers. This makes it imperative that Kansas fosters an environment that stimulates continued capital investment by telecommunications providers. In order to understand why telecommunications providers have been assessed higher property taxes and why there is a need for reform, one must possess a sense of the historical background of how telecommunications developed in the United States.

### **Industry History**

From the time of Alexander Graham Bell's invention of the telephone in the 1870's until late in the 20<sup>th</sup> Century, telephone service in America was a limited monopoly business. The Bell System not only provided local service to a large segment of the population but also was the exclusive provider of long distance service. Smaller independent telephone companies operated in exclusive territories and connected with the Bell System for long distance calls made by their customers.

In return for their exclusive franchise rights, telephone companies were regulated at both the state and national level. Regulation was intended to protect consumers from unreasonable prices while guaranteeing the companies a reasonable rate of return. However, starting in the 1960's and continuing to the present, this system has been restructured by a combination of anti-trust and legislative change.

The year 1984 was a watershed time for the telecommunications industry. Responding to lawsuits by the U.S. Department of Justice, AT&T (the parent company of the Bell System) entered into a court-approved settlement known as the Modified Final Judgment ("MFJ"). Under the MFJ, AT&T agreed to divest its local telephone companies. Arranged as seven regional holding companies (known as RBOC's or "Baby Bells"), the local companies (known as Bell Operating Companies "BOC's") were subject to business limitations in procuring products and providing some services. The former Bell Operating Company in Kansas is Southwestern Bell.

A key limitation on the BOC's involved the provision of long distance service. The BOC's could only carry telephone traffic within Local Access and Transport Areas ("LATA's"). Interexchange carriers (known as "IXC's"), who purchased access services from the BOC's or other companies providing local telephone service, carried traffic between LATA's (Kansas is divided into three such LATA's). The acronym "LEC" came into use to describe not only the BOC's but also any company that was a "local exchange carrier" providing local

telephone service. Regulation of the industry continued at the state level by public utility commissions and on a national level by the Federal Communications Commission ("FCC").

While competition in the telecommunications industry increased through the 1980's and into the 1990's, advancements in technology moved at an even faster pace. Key innovations during this period include the rapid improvement of computer equipment and software, advances in optical technology such as fiber optic cable, and new forms of telecommunications equipment. This includes new infrastructures that use digital technologies that can transmit voice and data at high speed. Even the Internet now includes providers who offer voice transmissions through personal computers.

Telecommunications in the 1990's has also become mobile. Users are no longer required to use telephones in their homes or offices. Cellular technology has exploded over the last ten years. In addition, over the last couple of years, mobile digital communications technology has developed to the point that it rivals cellular communications. When our last president took office, cellular telephones were used mainly by the rich. Today, they are practically given way to all consumers.

The new era of competition and advanced technology spurred the federal government to enact sweeping reforms in the Telecommunications Act of 1996 ("The Act"). With the passage of the Act, Congress implemented the most comprehensive overhaul of the country's telecommunications laws in more than 60 years. The Act was intended to transform the telecommunications industry by intending to encourage competition in the telecommunications industry. The original 1934 Communications Act was enacted at a time when telephone and broadcasting technologies were distinct and addressed different consumer needs. The 1934 Act and its accompanying regulatory scheme were designed to compartmentalize the various sectors of the telecommunications industry. However, as technology advanced, the potential for increased competition between telephone companies, cable companies and broadcasting companies increasingly became evident. A simple personal computer of today can be used to watch cable and network TV while at the same time conducting two-way voice communications.

The full effect of the new laws on the telecommunications industry will not be known for years. However, there are examples of the forces of change in the market for telecommunications. AT&T has divided into three independent companies, AT&T for communications, Lucent Technologies for technology development and manufacturing, and NCR for computer systems and services. In addition, there have been a number of mergers and acquisitions of telecommunications companies over the last three years. These mergers may further facilitate the bundling of telephone, cable television, and Internet access to consumers. There now exists a fast paced, communications-based economy that conducts much of its business over digital transmission highways.

### **Why The Discrimination Exists**

The historic rationale for this type of disparate property tax levy was that it constituted a quid pro quo, or mutual consideration, for the special rights and privileges that the state granted to utilities, such as monopoly status within a defined franchise service area. The utility franchise also ensured that the utility has the opportunity to recover its costs and earn a reasonable rate of return on its investment. Utilities are protected from competition to keep them in business and for this protection they pay a premium, for example, higher property taxes.

### *Why The Discrimination Should Be Eliminated*

AT&T ceased to enjoy utility protection since its' divestiture in 1984. Today, competition is now the hallmark of the interexchange telecommunications industry. As a result, AT&T has become by necessity, an enterprise no different in virtually all respects from other service or product providers. Under such circumstances, it is not reasonable to subject us to differentiated taxing schemes based essentially on factors that are incompatible with competition. Interexchange carriers are no longer protected from competition by the state, so the arguments that they should be subjected to discriminatory taxation in exchange for monopoly franchise no longer exists.

A principle that is often used in evaluating a state's tax structure is that of equity. The tax burden for taxpayers with similar resources should be related to the value of the public services that are received. States such as Kansas that continue to tax interexchange telecommunications companies in a manner similar to monopoly utilities clearly violates this principle since we have no monopoly franchise in any service area.

The extent of competition that currently exists within the interexchange industry is readily concluded from the barrage of advertisement in newspaper, magazines or television commercials. AT&T's market share has fallen dramatically, from over ninety percent in 1984 to less than sixty percent today. Consumers are inundated with advertising regarding MCI Worldcom's One Savings, AT&T's Personal Network, and Sprint's ION services. Interexchange carriers offer numerous incentive to consumers in attempts to get them to switch their long distance providers such as cash, free minutes of usage, airline mileage, and points that can be redeemed for merchandise. In order to reinforce the extent of competition within our industry, I would like for you to consider that in Kansas there are over eighty such carriers offering interexchange long distance services.

Given the degree of competition that currently exists within the industry, this discriminatory treatment takes on even greater significance when it is recognized that the interexchange industry competes not only among itself, but also against businesses in other industries. For example, Martin Marietta, IBM and DEC have all bid against AT&T for telecommunications projects. Yet, these companies would not be subject to a higher property tax assessment rate in Kansas because they are not considered "public utilities". AT&T is operating at a competitive disadvantage.

Another attribute of any fair tax system is that it does not cause business to change investment decisions based upon tax criteria alone. AT&T is not espousing that the telecommunications industry will collapse if we are not treated as a general business concern for property tax purposes. As long as consumers need telecommunication services, that need will be satisfied. The question is, in what manner and at what cost? Existing facilities in states such as Kansas that continue to impose onerous taxing schemes will be maintained and maybe even enhanced. Special property tax burdens increase the cost of telecommunication services to the users and reduce demand. The artificial suppression of the market demand for telecommunication services makes investments to meet that demand less attractive, thereby resulting in lower investment in telecommunications.

Additionally, taxes are one of several factors that are considered when making location decisions. Technology has made the design of telecommunication systems more modular. Additional distance adds little additional cost. Therefore, location decisions are becoming

much less sensitive to distance and much more discretionary. This is particularly true of high-investment components like electronic switching equipment. To the extent that customers in a state imposing a discriminatory property tax scheme can be serviced by equipment placed in a state with a more favorable property tax climate, the sound business decision becomes obvious. Of the states bordering Kansas, only the State of Oklahoma imposes a tax on telecommunications providers' property at a rate higher than that of general business property.

### Current Trends

Senate Bill 185 is a first step in keeping Kansas current regarding the taxation of telecommunications providers, that being the recognition of the competitiveness within the interexchange industry and the entry of companies not included within the definition of a public utility which provide their own telecommunication services. With this realization, there no longer exists any rational basis from a tax perspective to treat the telecommunications companies in a manner that differentiates us from the general business community.

There are currently only eleven states<sup>1</sup>, including Kansas, whose statutes continue to provide for the disparate property tax treatment of the telecommunications industry. That is, the property of interexchange carriers is, by statute, assessed at rates either in excess of those imposed upon the general business community, or portions of our property are subject to taxation while that of the general business community is not. In each of these eleven states, the tax is imposed as part of the overall treatment of utilities doing business.

The States of New Jersey, Arizona, Ohio and Wisconsin have already eliminated the discriminatory property tax treatment that once was in effect in those states. Other states, among the eleven remaining, are taking steps to remove the discriminatory treatment. Legislation is pending in the State of Montana (HB128) and we anticipate the introduction of legislation this year in at least three other states. It is not inconceivable that by year end 1999, the number of states taxing telecommunications companies in a manner differing from general business concerns will be in the single digits.

### Summary

Technological innovations have significantly changed the telecommunication industry. The emergence of a highly competitive industry and the development of sophisticated private networks were not contemplated when the public utility definitions found in the property tax statutes were drafted for telephone companies. AT&T supports the goal of eliminating the disparate tax treatment of telecommunications service providers that exists today. Telecommunications providers should be assessed property and other taxes at the same rate and in the same manner as general business. It is critical that Kansas' consumers continue to receive telecommunication services at reasonable and affordable rates.

Again, I appreciate the opportunity to express AT&T's support of this initiative and urge you to support this bill. Thank you and I will answer any questions that you may have at this time.

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<sup>1</sup> The eleven states include: Alabama, California, Iowa, Kansas, Louisiana, Massachusetts, Maryland, Mississippi, Montana, Oklahoma, and South Dakota



Senate Assessment and Taxation Committee  
Thursday, February 18, 1999  
Senate Bill No. 185

Madam Chairman and Members of the Committee:

My name is Kevin Kongs. I am Senior Director of Taxation for Western Resources.

Thank you for the opportunity to speak before you.

The bill before you today is an attempt to alleviate some of the tax disparity between state assessed telecommunications companies and other commercial and industrial companies. The bill phases in an income tax credit similar to the income tax credit allowed other commercial and industrial business.

Under this system, local government would not suffer loss of revenue, and telecommunications companies would secure a credit to reduce income tax liability.

As you know, the same disparity exists between electric companies and other businesses in Kansas. Therefore, we ask that you include all public utilities in this bill. In an effort to alleviate one inequity, we ask that you not create another by different treatment among state assessed companies and the industries they represent.

Attached to your copy of this testimony is proposed language to be amended into the bill which will offer the benefits of the income tax credit to all public utilities.

Thank you for your consideration. I will be happy to answer any questions the members might have.

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Attachment 2

Session of 1999

SENATE BILL No. 185

By Committee on Assessment and Taxation

2-1

9 AN ACT relating to income taxation; authorizing credits for property tax  
10 paid by certain telecommunications companies.

11  
12 *Be it enacted by the Legislature of the State of Kansas:*

13 Section 1. There shall be allowed as a credit against the tax liability  
14 imposed by the Kansas income tax act of a telecommunications company,  
15 as defined in K.S.A. 79-3271 and amendments thereto, an amount equal  
16 to the difference between the property tax levied and paid on property  
17 assessed at a 33% assessment rate and the property tax which would be  
18 levied and paid on such property if assessed at a 25% assessment rate  
19 except that, for taxable year 1999, the credit shall be equal to 25% of such  
20 amount, for taxable year 2000, the credit shall be equal to 50% of such  
21 amount, for taxable year 2001, the credit shall be equal to 75% of such  
22 amount and for taxable year 2001, and all such taxable years thereafter,  
23 the credit shall be equal to 100% of such amount. If the amount of such  
24 tax credit exceeds the tax liability for the telecommunications company  
25 for the taxable year, the amount thereof which exceeds such tax liability  
26 shall be refunded to the telecommunications company. If the telecom-  
27 munications company is a corporation having an election in effect under  
28 subchapter S of the federal internal revenue code, a partnership or a  
29 limited liability company, the credit provided by this section shall be  
30 claimed by the shareholders of such corporation, the partners of such  
31 partnership or the members of such limited liability company in the same  
32 manner as such shareholders, partners or members account for their pro-  
33 portionate shares of income or loss of the corporation, partnership or  
34 limited liability company.

and "public utilities",

35 Sec. 2. This act shall take effect and be in force from and after its  
36 publication in the statute book.





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*Mark Beshears*  
*Assistant Vice President*  
*State and Local Tax*

**MEMORANDUM**

To: The Honorable Audrey Langworthy, Chairperson  
Senate Committee on Assessment and Taxation

From: Mark Beshears, Assistant Vice President,  
State and Local Tax for Sprint

Re: Senate Bill No. 185

Date: February 18, 1999

**Testimony on behalf of Sprint Corporation**

**In support of Senate Bill 185**

**Topeka, Kansas**

**February 18, 1999**

I am Mark Beshears; AVP of State and Local Tax for Sprint Corporation located in Westwood, Kansas. I am pleased to be here today to provide input and ask for your support of SB 185, which authorizes certain income tax credits for telecommunication companies. The creation of a sound, fair and equitable tax system is of paramount importance to Sprint and the economy of Kansas. The current policy in Kansas of taxing some telecommunication companies at 33% and other companies at 25% is inherently discriminatory and creates an economic disincentive for investing in Kansas. In developing tax policy in Kansas and in other states, there must be a consistent vision to create a fair and equitable system of taxation that does not discriminate against one type of telecommunication provider over another.

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*Attachment 3*

Kansas has a property tax system for state assessed telecommunication companies based on the old concept that rate regulated companies should bear a higher property tax burden as a monopoly than a typical commercial business. In the past, providers of telecommunications were public utilities with no competition and little need for tax incentives. However, the recent deregulation of the telecom industry has dramatically changed the industry's competitive landscape. Deregulation has brought about a constant increase in demand by consumers and business for more affordable, advanced and accessible telecommunications. This trend will continue in Kansas and nationwide as our economy becomes more service based and increases its reliance on telecommunications. As our industry grows, the state's current tax structure needs to be updated to keep pace with the industry's rapidly advancing technology, competition and other changes attributable to deregulation.

Today, traditional telecommunication providers such as Sprint, face new competition from cable companies, resellers and paging companies. Many of these new competitors are able to provide telecommunication services in Kansas and are assessed at the lower 25% assessment rate and thus, receive an economic advantage.

In 1998, telecommunication companies assessed by the State PVD paid approximately \$69 million in property tax to local tax districts in Kansas. The language in SB 185 is a very simple proposal. It creates a refundable income tax credit equal to the difference between the property tax paid at the 33% classification rate versus property tax paid at the 25% classification rate. Because this is an income tax credit, the local tax jurisdictions continue to receive the same tax revenue. The bill provides for a phase-in over a four-year period commencing with the 1999 tax year. In conjunction with PVD, we have estimated the first year fiscal impact to be \$4.2 million.

At Sprint, we are creating a product line of seamless services that we refer to as "One Sprint". This concept will allow our customers to choose from a wide range of services bundled together as an integrated product. These services include long distance, wireless,

paging, Internet and local telephone service. We believe these services should be valued, assessed and taxed in a similar manner and at a similar rate. I respectfully request your support of this bill and ask that you recommend it favorably for passage.

If you have any questions, I would be happy to address them at this time.