

MINUTES OF THE HOUSE TAXATION COMMITTEE.

The meeting was called to order by Chairperson John Edmonds at 9:00 a.m. on April 3, 2003 in Room 519-S of the Capitol.

All members were present except: Representative Jeff Jack - Excused  
Representative Tim Owens - Excused

Committee staff present: Chris Courtwright, Legislative Research Department  
Gordon Self, Office of the Revisor of Statutes  
Carol Doel, Committee Secretary

Conferees appearing before the committee: Representative Frank Miller  
Representative Doug Patterson  
Mark Beck, Director of Property Valuation  
Department of Revenue  
Jeff Bridges, City Administrator, City of Andover,  
KS.  
Mark Detter, City administrator, Rose Hill, KS.  
Larry Baer, Kansas League of Municipalities

Others attending: See attached sheet

Chairman Edmonds opened the meeting for bill introductions. There were no bill introductions.

The Chairman called to the committee's attention to testimony from Secretary Joan Wagon, Department of Revenue regarding **HB 2464** which was heard on April 2, 2003 (Attachment 1); information concerning fiscal estimate for repeal of custom computer software sales tax exemption from Richard Cram of the Department of Revenue (Attachment 2); and research regarding "Resident Trust" definitions in other states also from Richard Cram of the Department of Revenue (Attachment 3). These articles were submitted for committee review in regards to bills previously heard and requests from the committee.

Chairman Edmonds opened the meeting for public hearing on **HB 2255** and recognized Representative Frank Miller as a proponent. Representative Miller explained that this is a simple bill so as not to penalize property owners who make routine maintenance investments on their home. (Attachment 4)

With no further proponents on **HB 2255**, the Chairman introduced Mark Beck, Director of property Valuation, Department of Revenue as an opponent. Mr. Beck explained that while they understand the concept behind this bill and the desire to mitigate some of the issues, we have a constitution that requires uniform and equal basis of evaluation and rate of taxation. The equal basis of valuation has been determined by the Legislature to be fair market value. (Attachment 5)

With no other person wishing to address the bill, the Chairman closed the hearing on **HB 2255** and opened the meeting for public hearing on **HB 2263**.

Representative Doug Patterson addressed the committee as a proponent of **HB 2263**. In his testimony, Representative Patterson stated that he agreed with Mr. Beck on needing to set fair market value. His bill suggests, maybe for consideration on another day, that tax money needs to be raised the old fashioned way and not the artificial way of establishing appraised valuations based upon computer software without appraisal that raise taxes year after year in absence of a real taxable event such as the issuance of a building permit for a capitol improvement to a property or by the certificate of value filing which means the property was sold and therefore a transaction occurred. Representative Patterson further stated that in Jackson County and Wyandotte County the appraiser is known as the revenue generator and that is not his job. The appraiser is to establish property values. His suggestion is that short of an actual event which improves the value of the property or upon a sale that there be a limit on the assessed evaluation representing what we all realize in every other aspect of our lives, the consumer price index increase of increases in values of property. (No Written Testimony)

CONTINUATION SHEET

MINUTES OF THE HOUSE TAXATION COMMITTEE at 9:00 a.m. on April 3, 2003 in Room 519-S of the Capitol.

With no further proponents on **HB 2263**, Chairman Edmonds recognized Mark Detter, City Administrator, Rose Hill, Kansas as an opponent. Mr. Detter listed constitutional issues, financial impact, and equity as the three reasons the City of Rose Hill opposed the bill. (Attachment 6)

Jeff Bridges, City Administrator, City of Andover, Kansas testified in opposition to **HB 2263**. The opinion of the City of Andover is that this bill is a proposal to limit the growth of the appraised valuation of property by prohibiting an increase in value on existing properties above a set formula. In effect this bill eliminates the entire premise and corner stone of the property appraisal unconstitutional property taxation system. (Attachment 7)

Also appearing as an opponent to **HB 2263** was Larry R. Baer, Assistant Legal Counsel for the League of Kansas Municipalities. It is their understanding that this bill proposes to place a systematic limit or restriction upon the amount of the annual increases in property valuation. The limitation results because the increase is tied to a percentage or fraction derived from the US department of Labor's consumer price index. (Attachment 8)

With no other person wishing to address the bill, Chairman Edmonds closed the meeting for hearing on **HB 2263**.

The chairman called attention to written testimony regarding **HB 2263** from Marlee Carpenter, Director of Taxation and Small Business for KCCI (Kansas Chamber of Commerce and Industry) (Attachment 9), Mark Beck, Director of Property Valuation, Department of Revenue (Attachment 10), and Randall Allen, Kansas Association of Counties (Attachment 11)

There being no further business before the committee, Chairman Edmonds adjourned the meeting at 10:03 a.m.





**K A N S A S**

JOAN WAGNON, SECRETARY

DEPARTMENT OF REVENUE  
OFFICE OF THE SECRETARY

KATHLEEN SEBELIUS, GOVERNOR

Testimony to House Tax Committee  
Joan Wagnon  
Secretary of Revenue

**April 2, 2003**

**House Bill 2464**

Chairman Edmonds and Members of the Committee:

I strongly support House Bill 2464, our Governor's proposal to accelerate by one month, beginning next year, the second half of property tax payments. Under current law, the second half of property tax payments for a given tax year are due on or before June 20 of the next calendar year. Under House Bill 2464 and proposed amendments, starting with the second half of property tax payments for tax year 2003, those payments will become due on or before May 10, 2004. Second half property tax payments for tax years thereafter will be due on or before May 10 of the succeeding calendar years. By moving up the second-half payment of property taxes one month, expenditures from the State General Fund can be lowered by \$161.6 million in FY 2004. Currently, property tax payments from the statewide education mill levy go directly to local school districts, and the state then finances the remaining part of school budgets from the State General Fund. Accelerating second half property tax payments from June to May brings an extra property tax payment to schools, and in that one year, allows a lower payment from the state.

This bill will have a positive fiscal impact in the years after FY 2004, as shown on the attached spreadsheet provided by Legislative Research, because by moving the due date for the second half payments up by approximately one month, anticipated growth in assessed valuations will be reflected in increased property tax receipts earlier than under current law.

The county treasurers have requested certain amendments to the bill, which are intended to align certain revenue distribution schedules, necessitated by the change to the due date for second half of property tax payments. The State Treasurer and the Department of Education have been consulted and expressed no concern with these changes. These amendments are shown in the balloons attached hereto.

I would be pleased to address any questions you may have.

House Taxation  
Attachment 1

Date 4-3-03

### School Finance Property Tax Model

20 mills assumed permanent

20k residential exemption assumed permanent

Revised Tax Base Assumptions Agreed to 11/8/02

Accelerate 2nd Half Property Tax Payment Date to Sometime in May, Beginning in 2004

Calendar Year	Current Assessed Value	Proposed Exemptions	Proposed Assessed Value	Current Mills	Proposed Mills
1994	\$15,502,087,375	--	\$15,502,087,375	35.0	35.0
1995	16,194,057,543	--	16,194,057,543	35.0	35.0
1996	16,703,505,399	--	16,703,505,399	35.0	35.0
1997	16,267,106,394	--	16,267,106,394	27.0	27.0
1998	16,965,505,048	--	16,965,505,048	20.0	20.0
1999	17,689,996,969	--	17,689,996,969	20.0	20.0
2000	18,922,577,736	--	18,922,577,736	20.0	20.0
2001	20,478,966,701	--	20,478,966,701	20.0	20.0
2002	20,950,000,000	--	20,950,000,000	20.0	20.0
2003	21,840,000,000	--	21,840,000,000	20.0	20.0
2004	22,707,000,000	--	22,707,000,000	20.0	20.0
2005	23,607,637,500	--	23,607,637,500	20.0	20.0
2006	24,543,173,906	--	24,543,173,906	20.0	20.0
2007	25,514,917,928	--	25,514,917,928	20.0	20.0
2008	26,524,227,350	--	26,524,227,350	20.0	20.0
2009	27,572,510,876	--	27,572,510,876	20.0	20.0

Fiscal Year	Current Law Property Tax	Proposal Property Tax	Total Fiscal Note
1996	\$526,919,633	\$526,919,633	--
1997	565,976,272	565,976,272	--
1998	487,137,854	487,137,854	--
1999	371,485,590	371,485,590	--
2000	341,072,904	341,072,904	--
2001	361,268,394	361,268,394	--
2002	389,247,913	389,247,913	--
2003	406,945,940	406,945,940	--
2004	421,122,000	582,738,000	161,616,000
2005	438,294,600	444,710,400	6,415,800
2006	455,684,723	462,349,440	6,664,718
2007	473,749,025	480,671,994	6,922,969
2008	492,512,788	499,703,694	7,190,906
2009	512,002,243	519,471,132	7,468,890
2010	532,244,602	540,001,900	7,757,298



**K A N S A S**

JOAN WAGNON, SECRETARY

DEPARTMENT OF REVENUE  
POLICY AND RESEARCH

KATHLEEN SEBELIUS, GOVERNOR

April 2, 2003

To: Representative John Edmonds, Chair  
House Committee on Taxation

From: Richard Cram  
Steve Brunkan

Re: Request for Information Concerning Fiscal Estimate for Repeal of Custom Computer Software Sales Tax Exemption and Department's Interpretations

**Custom Computer Software Fiscal Estimate**

The Department's fiscal estimate for 2002 Senate Bill 39 on the repeal of the sales tax exemption for custom computer software sales was \$14.8 million for FY 03 (based on 11 months of collections).

The fiscal estimate for custom software was developed during the 2001 Legislature session. The source for the estimate is the 1997 Economic Census data for Kansas as published by the Census Bureau, U.S. Department of Commerce. The report provides receipt data by the North American Industrial Classification System (NAICS) broken down by state. The NAICS is a classification system for identifying specific industries and assigning a code number to each. For NAICS code 5415, Computer Systems Design and Related Services, the 1997 receipts reported for Kansas was \$631.4 million.

Within that broad category is NAICS code 541511, Custom Computer Programming Services with receipts of \$258 million for Kansas in 1997. Using only the receipts amount for this NAICS code would yield state sales tax collections of \$12.64 million for 1997. Assuming an annual growth of approximately 3% a year, by FY 03, the estimated sales tax collections would be \$14.8 million (11 months). This is a conservative estimate, because some custom computer software programming services (which would be subject to the sales tax on custom software) are included within other categories of the NAICS codes outside of 541511. For example accounting or consulting firms may provide custom software as a part of their services, yet they would not be captured under NAICS code 541511. Some custom software is provided to nontaxable entities (such as governmental entities). However, because we know that NAICS code 541511 does not capture all of the situations in which custom computer programming services are provided, we did not discount the \$14.8 million estimate, assuming that it would represent a reasonable estimate of taxable custom computer software sales in Kansas.

### Custom Software Receipts in FY 03

Sales reported on returns are not broken down by type of product sold. We cannot isolate sales tax on custom computer software from the data contained on the sales tax returns received from businesses likely to be selling custom computer software. Thus, we must estimate the amount of sales tax received in FY 03 attributable to custom computer software sales. Statistical information from tax returns provides sales tax data by NAICS code of the reporting businesses. We can identify businesses likely to be selling custom computer software by the NAICS code. Our estimate contains sales tax data from businesses within NAICS codes for industry categories that provide custom computer software. However, as discussed above, there will be businesses outside of these NAICS codes also selling custom computer software, so our estimate is likely to be low. Fiscal year 2002 sales tax receipts for businesses in the NAICS codes listed below were included in the estimate. Fiscal year 2002 receipts were identified for those certain NAICS codes, as were FY 03 receipts through December 2002 (the latest data we have available showing complete posting of tax return information). Because FY 03 receipts are not yet available for the entire year, a projection must be developed, based on existing data. The FY 03 receipts through December 2002 are shown below. A projection was developed for full FY 03, based on the ratio between FY 02 receipts and FY 02 receipts as of the end of December 2001. This showed that from July through December 2001, we had collected approximately 30% of the total tax receipts for FY 02 under the NAICS codes shown. That same ratio was applied to FY 03 receipts as of the end of December 2002 to project FY 03 receipts for the entire year. The increase between FY 02 receipts and projected FY 03 receipts for the NAICS codes identified is attributed to sales tax generated from the sales of custom computer software following repeal of the exemption.

	FY 2002 <u>Total</u>	FY 2003 <u>Thtr Dec.</u>	FY 2003 <u>Projected</u>
541511 Custom computer programming services	\$ 2,982,269	\$1,497,393	\$4,848,174
541512 Computer systems design services	\$ 2,372,873	\$3,157,318	\$5,519,255
541513 Computer facilities management services	\$ 502,301	\$ 530,470	\$2,933,790
541519 Other computer related services	\$ 1,306,634	\$ 576,474	\$1,433,054
Total	\$ 7,164,077	\$3,949,726	\$15,484,249

The projection also assumes a general 105% increase in state sales tax collections for FY 03. Assuming the \$8.3 million increase (\$15.5 million in projected FY 03 receipts less \$7.2 million in FY 02 receipts) is the result of custom software sales, it represents over half of the \$14.8 million fiscal note.

The above sales tax receipts data is based on returns received from businesses selling custom computer software. However, if a business purchases custom computer software from an out-of-state firm that does not have nexus with Kansas, the purchasing business is obligated to report and remit use tax on such a purchase. When businesses report and pay consumer's use tax, the returns do not break out the use tax payments by type of product purchased. We cannot isolate from the consumer's use tax receipts data that attributable to custom computer software purchases. For this reason, we know the \$8.3 figure is low, because it does not include consumer's use tax paid on custom software purchases. As mentioned above, companies may provide custom computer programming as a part of their overall business activity and could be classified in a category other than the ones above. Any programming performed by them would be included in their total receipts within their business category but would not be captured in our estimate.

Given that we have identified a projected \$8.3 million increase in sales tax receipts for FY 03 from businesses in the computer programming industry, and knowing that estimate does not include any data on consumer use tax receipts from out-of-state custom software purchases, and does not include data on custom software sales by firms not falling within the above NCAIS codes, we remain confident in our \$14.8 million estimate for FY 03 for sales tax receipts from sales of custom computer software.

### **Department's Interpretation of Sales Tax Imposition on Custom Software**

The imposition of sales tax on the sale of custom computer software, and on the services of modifying, altering, updating or maintaining custom software, is new in Kansas (at least since the exemption of sales tax on custom software was enacted in 1988). Anytime the sales tax laws are changed, questions will arise as to how that change should be interpreted. Because of the characteristics of custom software, it does raise some unique sales tax questions. Unlike something like a hard object such as an automobile part, custom software may be delivered in a variety of forms such as a disc or CD, or it can be transmitted electronically and downloaded to the purchaser's computer. It can also be delivered by placing it on a server, where the purchaser can access and use it. The software programmer could also install it directly on the purchaser's computer at the purchaser's location. These situations can raise interesting sales tax questions, such as where does the sale take place? When is use tax owed and when is sales tax owed?

Attached is a copy of the Department's Notice 02-10, explaining the Department's interpretation of the imposition of sales tax on custom computer software included in 2002 Senate Bill 39. This Notice was published on the Department's website in July 2002. In it, we have attempted to answer some of the most basic interpretation questions that might arise. Taxpayers with additional questions are free to contact us to request private letter rulings on specific situations. Several private letter rulings addressing taxpayers' questions concerning custom software sales tax issues are published on the Department's website. We do intend to publish new regulations concerning sales tax on custom computer software. However, if Kansas adopts legislation to conform to the Streamlined Sales and Use Tax Agreement (such as proposed in Senate Bill 192), then some definitional changes and sourcing rule changes to current law concerning computer software will be made. Thus, we are planning to wait to publish the new regulations until it becomes clear whether legislation conforming to the Streamlined Sales and Use Tax Agreement will be adopted.

If you have other questions or your Committee would like to opportunity to ask questions, please let us know and we would be pleased to appear before the Committee at your convenience.



# Notice

**Notice Number:** 02-10  
**Tax Type:** Kansas Retailers' Sales Tax  
**Brief Description:** Imposition of sales tax on sale custom computer software and services of modifying, altering, updating or maintaining such software.  
**Keywords:**  
**Approval Date:** 07/01/2002

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**Body:**

Office of Policy & Research

July 1, 2002

**Notice 02-10**

**Imposition of sales tax on sale custom computer software and services of modifying, altering, updating or maintaining such software**

**Summary**

Beginning July 1, 2002, Kansas and local retailer's sales tax is imposed on the sale of custom computer software and the services of modifying, altering, updating or maintaining custom software. Under prior law, sales tax was imposed only on the sale of canned computer software, and the services of modifying, altering, updating or maintaining canned computer software. Sales of both custom and canned software are now subject to sales tax, as are the services of modifying, altering, updating or maintaining software.

Canned software includes, among other things, prepackaged word processing programs, game programs, educational programs, spreadsheet programs including bookkeeping and payroll programs, and video game cartridges. Custom programs are those developed from scratch or those uniquely designed and custom tailored to meet the customer's specific requirements.

Under prior law, the sale of any custom computer program originally developed for the exclusive use of a single end user, as well as the sale of modification services when developed exclusively for a single end user (if charges for such modification were separately stated on the invoice), were expressly excepted from the imposition of sales tax on computer software and the sale of services of modifying, altering, updating or maintaining computer software. See K.S.A. 2001 Supp. 79-3603(s). Section 6 of 2002 Senate Bill 39 amended 79-3603(s) by removing the exception for custom computer software.

**Definition of Computer Software**

"Computer software" is defined at Section 6, 2002 Senate Bill 39 as follows:

information and directions loaded into a computer which dictate different functions to be performed by the computer. Computer software includes any canned or prewritten

program which is held or existing for general or repeated sale, even if the program was originally developed for a single end user as custom computer software.

Computer software is defined as "tangible personal property" under Kansas sales tax law at K.S.A. 79-3602(f), which provides:

"Tangible personal property" means corporeal personal property. Such term shall include any computer software program which is not a custom computer software program, as described by subsection (s) of K.S.A. 79-3603, and amendments thereto.

Because Section 6, 2002 Senate Bill 39 deletes the description of custom computer software formally contained in K.S.A. 79-3603(s), custom computer software is also included in the term "tangible personal property" as of July 1, 2002.

K.A.R. 92-19-70 provides:

Computer software. (a) Sales tax shall be imposed on the gross receipts received from the sale of computer software. Computer software includes all software or computer programs, whether contained on tapes, discs, cards or other devices or materials which direct a computer or hardware to perform different functions, and includes customized software, canned software, operational software, application software, systems software and other forms of software or computer programs.

(b) Sales tax shall be imposed on the total cost to the consumer without any deduction or exclusion for the cost of:

- (1) The property or service sold;
- (2) labor or services used or expended, including:
  - (A) Program development, problem definition;
  - (B) analysis, design, coding, testing; and
  - (C) implementation, evaluation, maintenance and documentation;
- (3) materials used;
- (4) losses;
- (5) overhead or any other costs or expenses; or
- (6) profit, regardless of how any contract, invoice or other evidence of the transaction is stated or computed, and whether separately billed or segregated on the same bill.

(c) The principal line of business of the seller is not material when determining the taxability of sales of computer software. Each bank, savings and loan or other thrift institution, accounting firm, computer program developer, dealer and other person is deemed to be a retailer when selling computer software at retail to the final user or consumer. Each retailer shall collect sales tax on the gross receipts received from the retail sale of computer software.

Under K.S.A. 79-3602(c), a sale includes "the sale of the use of tangible personal property by way of a lease, license to use or the rental thereof regardless of the method by which the title, possession or right to use the tangible personal property is transferred." These provisions make sales of licenses to use computer software subject to tax, regardless of whether the software is transferred to the buyer by floppy disc, CD-ROM, telephone modem, or via the

Internet or other electronic media. Sales of computer software are taxable regardless of how possession or the right to use the software is transferred.

Charges for performing the following activities, whether separately stated or not, are subject to sales tax when part of the sale of computer software: (a) designing and implementing computer systems (determining equipment and personnel required and how they will be utilized); (b) designing storage and data retrieval systems (determining what data communications and high-speed input-output terminals are required); (c) consulting services (study of all or part of an information management or data processing system); (d) feasibility studies (studies to determine what benefits would be derived from a software project); (e) evaluation of bids (studies to determine which manufacturer's proposal for computer equipment would be most beneficial); (f) providing technical help, analysts and programmers, usually on an hourly basis; (g) training services; (h) software set up; and (i) maintenance of software.

### **Sales by Kansas software retailer to in-state customers**

Sales by a Kansas retailer of computer software to an in-state customer are considered a Kansas retail sale of tangible personal property, subject to state and local sales tax.

For purposes of determining which local sales tax applies to the sale of computer software, the situs or location of the sale must be identified. The general rule is that local sales tax is situated to the retailer's place of business. K.A.R. 92-21-7 provides:

92-21-7 Place of sale. For the purposes of local sales tax, all retail sales occur at the place of business of the retailer unless delivery is made by the retailer or his agent to an out-of-state destination, or to a common carrier for delivery to an out-of-state destination or unless otherwise specified by Kansas statutes or regulations. For the purpose of this provision it is immaterial that title passes to the purchaser at a place outside of the local taxing jurisdiction in which the retailer's place of business is located, or that property sold is never within the local taxing jurisdiction in which the retailer's place of business is located.

If a retailer has more than one location in Kansas and if two or more of such locations participate in the sale, the sale occurs at the place of business where the principal negotiations are carried on. If this place is the place where the order is taken, it is immaterial that the order must be forwarded for acceptance, approval of credit, shipment or billing. For the purposes of this rule, an employee's activities will be attributed to the place of business out of which he works.

Local sales tax should be charged based on the location of the retailer making the sale. This rule applies when the retailer orders something from an out-of-state manufacturer or distributor to be delivered to the retailer's business or when the retailer orders something from an out-of-state manufacturer or distributor to be delivered to the customer's location.

### **Sales by Kansas software retailer to out-of-state customers**

Sales by a Kansas retailer of computer software to an out-of-state customer would be considered a sale in interstate commerce. K.A.R. 92-19-29 provides:

92-19-29. Sales in interstate commerce. When tangible personal property is sold

within the state and the seller is obligated to deliver it to a point outside the state or to deliver it to a carrier or to the mails for transportation to a point without the state, the retail sales tax does not apply: *Provided*, The property is not returned to a point within this state. The most acceptable proof of transportation outside the state will be:

- (a) A waybill or bill of lading made out to the seller's order calling for delivery; or
- (b) An insurance or registry receipt issued by the United States postal department, or a post office department's receipt; or
- (c) A trip sheet signed by the seller's delivery agent and showing the signature and address of the person outside the state who received the delivered goods.

However, where tangible personal property pursuant to a sale is delivered in this state to the buyer or his agent other than a common carrier, the sales tax applies, notwithstanding that the buyer may subsequently transport the property out of this state.

If computer software sold by a Kansas retailer is delivered to the out-of-state customer in Kansas, then the transaction would be considered a Kansas sale, subject to sales tax. If delivery to the out-of-state customer occurs outside the borders of Kansas, then the transaction would not be considered a Kansas sale and would not be subject to Kansas tax. Computer software delivered to the out-of-state customer electronically and downloaded at the customer's out-of-state location will be considered a sale in interstate commerce, not subject to Kansas sales tax. If delivery outside of Kansas is by the US Postal Service, common carrier such as UPS, or the retailer's or retailer's agent's vehicle, the sale is regarded as taking place in the state of delivery and is not subject to Kansas tax. Delivery in Kansas to a contract carrier makes the sale Kansas taxable when the carrier is acting as the buyer's agent.

### **Sale of Computer Software by Out-of-State Retailer to Kansas Customer**

Sale of computer software by an out-of-state retailer to a customer located in Kansas is subject to Kansas compensating use tax. If the out-of-state retailer has sufficient nexus with Kansas, the out-of-state retailer is obligated to collect the use tax from the customer and report and remit it to the Department. If the out-of-state retailer does not have nexus with Kansas, then the customer is obligated to accrue Kansas use tax on the purchase and report and remit it to the Department.

Nexus refers to the presence or contacts that an out-of-state business has with a state. A state can impose use tax collection duties on an out-of-state business only if the business has sufficient contacts or presence in the state. Presence in the taxing state of owned or leased personal or real property, offices, facilities, or agents, representatives or employees can establish nexus. If the out-of-state business has no property, offices, employees, or agents who operate in Kansas, then it will have no legal duty to collect use tax on sales of computer software to Kansas customers. Nexus would not be achieved if the only activity in Kansas is delivery of software, by shipment of a disk by mail, UPS, common carrier or by downloading from the Internet.

Nexus would be created if the out-of-state business sends employees into Kansas, pays independent contractors or agents to operate here, regularly delivers into Kansas using its own vehicles, appears at trade shows here, employs Kansans to perform service work here, or conducts similar activities here. If an out-of-state business, as lessor, leases computer hardware or software in Kansas, it would have nexus and would be required to collect and remit use tax on

leases to Kansas lessees. See K.S.A. 79-3702(c); K.S.A. 79-3702(g).

### **Computer Software Modification and Maintenance**

K.S.A. 2001 Supp. 79-3603(s), as amended by Section 6 of 2002 Senate Bill 39, imposes sales tax on the sale of services of modifying, altering, updating or maintaining computer software. K.S.A. 79-3603(q) specifies that alteration, repair and maintenance services done to tangible personal property are subject to Kansas sales tax. Computer software is defined as “tangible personal property.” K.S.A. 2001 Supp. 79-3602(f)(1). K.S.A. 79-3603(r) imposes a sales tax upon: “the gross receipts from fees or charges made under service or maintenance agreement contracts for services, charges for the providing of which are taxable under the provisions of subsection (p) or (q). . .” The sale of computer hardware and software maintenance agreements are taxable, pursuant to K.S.A. 79-3603(r).

The services of modifying, altering, updating or maintaining computer software are presumed to be performed at the location of the software being used by the customer at the customer’s premises. Kansas sales tax would apply to such services performed in Kansas. Fees charged to diagnose a computer software problem for a customer are considered part of service of modifying, altering or maintaining the software and are part of the taxable gross receipts.

Software that modifies or alters existing software is considered separate from the existing software and is taxable.



**K A N S A S**

JOAN WAGNON, SECRETARY

DEPARTMENT OF REVENUE  
POLICY AND RESEARCH

KATHLEEN SEBELIUS, GOVERNOR

April 2, 2003

To: Representative John Edmonds, Chair  
House Committee on Taxation

From: Richard Cram

**Re: Research Regarding "Resident Trust" Definitions in Other States**

**Definition of "Resident Trust" in States Bordering Kansas**

You requested a review of the statutory definitions of "resident trust" in states bordering Kansas, and a comparison of those definitions to the Kansas definition (which defines a "resident trust" as one administered in this state).

Colorado, like Kansas, defines a resident trust as one administered in that state (§ 39-22-103(b)(10)).

Missouri, as previously discussed, defines a resident trust as: (1) a trust created by the will of a decedent domiciled in Missouri at the time of death and with at least one income beneficiary being a Missouri resident at the end of the tax year; or (2) a trust created by or consisting of property of a trustor domiciled in Missouri at the time the trust became irrevocable, and the trust has at least one income beneficiary being a Missouri resident at the end of the tax year (§143.331).

Nebraska defines a resident trust as: (1) a testamentary trust created by a decedent domiciled in Nebraska at the time of death, or (2) a trust created by or consisting of property of a person domiciled in Nebraska at the time the trust became irrevocable (77-2714.01; Reg 23-001).

Oklahoma, similar to Nebraska, defines resident trust as: (1) a testamentary trust consisting of property transferred by will of a decedent domiciled in Oklahoma at the time of death, or (2) a trust consisting of property of a person domiciled in Oklahoma at the time the trust became irrevocable.

In summary, Kansas and Colorado use the narrowest definition of "resident trust." Nebraska and Oklahoma use a broader definition. Missouri's definition is in between.

## Definition of "Resident Trust" in Other States

You also requested a review of the definitions of "resident trust" in the other states. Statutory/regulation definitions of the term "resident trust" were not identified in every state. Listed below are descriptions of statutory/regulation definitions of "resident trust" for several states where such definitions were found. In general, the definitions break down into approximately four different groups: (1) definitions very similar to Nebraska's and Oklahoma's (trust created under will of decedent who was a resident of the state at the time of death, or irrevocable trust created by or consisting of property of a resident of the state at the time the trust became irrevocable) (Nine states: Nebraska, Oklahoma, Connecticut, Massachusetts, Minnesota, New Jersey, New York, Pennsylvania, West Virginia); (2) definitions similar to the Kansas definition (trust administered in the state) (Seven states: Georgia, Kansas, Colorado, Arizona, Hawaii, Oregon, South Carolina); (3) definitions similar to Missouri's (the Nebraska/Oklahoma definition with the added requirement that at least one beneficiary be a resident) (Missouri, Rhode Island); and (4) a combination of the above definitions (Delaware, Utah, Louisiana).

This review indicates that most states with statutory/regulation definitions define "resident trust" more broadly than does Kansas.

Arizona defines "resident trust" as a trust of which the fiduciary is a resident of the state (§ 43-1301). This is similar to the Kansas definition.

Connecticut defines a resident trust as: (1) a trust consisting of property transferred by will of a decedent who was a resident of the state at the time of death, or (2) a trust consisting of property of a person who was a resident of the state at the time the property was transferred to the trust and the trust became irrevocable (§ 12-701).

Delaware defines resident trust as: (1) a trust created by the will of a decedent who at death was domiciled in the state; (2) a trust created by, or consisting of property of, a person domiciled in the state; or (3) a trust, the trustee of which is a resident of the state or is an entity having an office conducting trust business in the state, or if the trust has more than one trustee, either half of the individual trustees are residents of the state, or if an entity is a co-trustee, the entity has an office for the conduct of trust business in the state (§ 1601).

Georgia defines a non-resident trust as one administered by a non-resident fiduciary (Regs. §560-7-8-.35).

Hawaii defines resident trust as a trust of which the fiduciary is a resident of the state and the administration is carried on in the state.

Louisiana defines resident trust as: (1) a trust created by the will of a decedent who at death was domiciled in this state, or (2) the trust instrument provides that the trust shall be governed by the laws of Louisiana. If the trust instrument is silent on which law governs, then if the trust is administered in the state, it is considered a resident trust (§ 47:300.10).

Massachusetts defines a resident trust as a trust created under the will of a person who died a resident of the state (§ 62.10.1).

Minnesota defines resident trust as: (1) a trust created by the will of a decedent domiciled in the state at the time of death, or (2) an irrevocable trust, the grantor of which was domiciled in the state at the time the trust became irrevocable.

New Jersey defines a resident trust as: (1) a trust consisting of property transferred by will of a decedent who at death was domiciled in the state, (2) a trust consisting of property of a person domiciled in the state at the time the property was transferred to the trust if the trust was irrevocable or domiciled in the state at the time the trust became irrevocable (§ 54A:1-2).

New York defines a resident trust the same way that New Jersey does.

Oregon defines resident trust as a trust of which the fiduciary is a resident of Oregon, or a trust administered in Oregon.

Pennsylvania defines resident trust as: (1) a trust created by the will of a decedent who at the time of death was a resident of the state, or (2) a trust created by or consisting of property transferred to a trust by a person who was a resident of the state at the time of the transfer or creation of the trust.

Rhode Island defines resident trust as: (1) a trust that becomes irrevocable upon the occurrence of an event terminating a person's power to revoke, if the person with such power was a Rhode Island resident at the time of the event, (2) a trust created by the will of a decedent who at death was a resident of the state, or (3) an irrevocable trust created by or consisting of property contributed by a resident of the state. Also, in order to be considered a resident trust, the trust must have beneficiaries who are Rhode Island residents (§ 44-30-5).

South Carolina defines a resident trust as a trust administered in the state (§12-6-30).

Utah defines resident trust as: (1) a trust consisting of property transferred by will of a decedent who at death was domiciled in the state, or (2) a trust administered in the state (§ 59-10-103(1)(1)).

West Virginia defines a resident trust as: (1) a trust created by will of a decedent who at death was domiciled in the state, or (2) a trust created by, or consisting of property of, a person domiciled in the state.



C. FRANK MILLER  
 REPRESENTATIVE, TWELFTH DISTRICT  
 MONTGOMERY, CHAUTAUQUA, AND  
 ELK COUNTIES  
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TOPEKA

HOUSE OF  
 REPRESENTATIVES

COMMITTEE ASSIGNMENTS  
 MEMBER: EDUCATION  
 HEALTH AND HUMAN  
 SERVICES  
 ETHICS AND ELECTIONS  
 LEGISLATIVE POST AUDIT

Thursday April 3, 2003

House Committee on Taxation  
 Honorable John Edmonds, Chairman  
 Testimony in Support of HB2255

It is my pleasure to come before this committee to testify in support of HB2255. This is truly a simple bill, but much needed so as not to penalize property owners who make routine maintenance investments on their homes.

It is not uncommon for property appraisers on occasions to increase the value of homes, simply because the owner made landscaping improvements, repainted the house or installed new shingles on the roof. Then to the shock of the property owner, he/she finds the appraised value of their property has increased significantly because of their consideration to maintain their home in good condition and be good neighbors in the community. In some cases the property may acquire some increase in sales value, but the basic reason the owner made these changes was to maintain the quality and aesthetic appearance of the home. How often have we experienced or heard of the appraised value of a home being **reduced** because of poor upkeep on the property in question?

This bill makes upkeep of a taxpayer's property not a reason for the appraiser to increase the appraised value of a home. This can be argued, but the underlying need for this bill is to make sure property can be maintained in an attractive manner that enhances the community as a whole. We all like to live next to neighbors that maintain their homes and landscaping in such a manner as to retain or even increase the overall value of our community. If all property in a given community become more saleable then increases in the appraised value of all the homes in that community are eligible for an increase in appraised value. But, this bill will remove specific items of maintenance from that list of reasons to increase the appraised value of a single property.

This bill focuses on maintenance items such as repainting, re-roofing, adding siding, or just planting a new lawn and adding some landscaping. All of these things can be viewed as maintaining the value of a home, and maintaining the aesthetic appearance of a community. Why do we want to discourage this kind of community effort?

I stand for questions, and trust the committee will support HB2255 and pass it out favorably for passage.

Respectfully yours,

Representative Frank Miller

House Taxation  
 Attachment 4  
 Date 4-3-03



# K A N S A S

JOAN WAGNON, SECRETARY

DEPARTMENT OF REVENUE  
DIVISION OF PROPERTY VALUATION

KATHLEEN SEBELIUS, GOVERNOR

Testimony to House Tax Committee  
Mark S. Beck  
Director of Property Valuation

April 3, 2003

House Bill 2255

Chairman Edmonds and Members of the Committee:

Art. 11, § 1 of the Kansas Constitution requires that the legislature provide for a uniform and equal basis of valuation and rate of taxation. The equal basis currently provided by the legislature is "fair market value." *State ex rel. Stephan v. Martin*, 227 Kan. 456, 462, 608 P.2d 880 (1980). "Fair market value" has a generally understood and accepted meaning in our free economy and in case law. "Fair market value" means:

"Fair market value in money shall mean the amount of money that a well informed buyer is justified in paying and a well informed seller is justified in accepting, assuming that the parties thereto are acting without undue compulsion and that the property has been offered at the market place for a reasonable period of time. . . ."

*Mobil Pipeline Co. v. Rohmiller*, 905, 926, 522 P.2d 923 (1974).

The Supreme Court of Kansas has struck down as a violation of art. 11, § 1 of the Kansas Constitution attempts to depart from the mandate of "fair market value" most notably in the early 1980s when legislation was enacted to require farm machinery and equipment to be valued at "average loan value" rather than "fair market value." The Court stated:

[A]rt. 11, § 1 of the Kansas Constitution prohibits favoritism, and requires uniformity in valuing property for assessment purposes so that the burden of taxation will be equal. *Addington v. Board of County Commissioners*, 191 Kan. at 532. *Wheeler v. Weightman*, 96 Kan. at 58; *Hines, et al. v. City of Leavenworth et al.*, 3 Kan. \*186, Syl. ¶ 5. Property taxation is not based upon the owner's ability to pay. Economic distress is no justification for ignoring the constitution.

HB 2255 prohibits the appraiser from considering changes made to a property called "regular maintenance" such as landscaping, planting of trees, flower beds, shrubbery and lawns, removal of trash and overgrowth, painting, reroofing or the addition of new siding or veneer to an existing building or any other similar change to the property. Some of the items herein listed as being "regular maintenance" can, in fact, quite extensively renovate a property depending on its previous condition. If any of these changes are substantial, they may be the very things that make a property more attractive to buyers and thus may result in a higher selling/purchase price. Thus, to prohibit the appraiser from considering them in finding the property's "fair market value" is clearly a violation of the "uniform and equal" provision of the Kansas Constitution.

Besides its constitutional problems, HB 2255 presents significant administrative problems. Does the bill "freeze" value whenever "regular maintenance" is shown? If the property owner, for example, plants a tree, is the value frozen? Since the burden of proof on residential property is on the county appraiser, is it the appraiser's burden to demonstrate that any valuation increase on the property is not attributable to the "regular maintenance"? From an appraisal standpoint how does the appraiser extract value attributable to "regular maintenance"?

CITY OF ROSE HILL TESTIMONY- HOUSE BILL NO. 2263  
MARK DETTER-CITY ADMINISTRATOR

The City of Rose Hill is a bedroom community 20 miles southeast of Wichita. The Rose Hill Community's population grew 43% in the 90's and our assessed valuation doubled in that same time period. The City of Rose Hill opposes HB 2263 due to the following reasons:

- 1) **Constitutional Issues-** Several different sources City officials have contacted question whether this bill passes constitutional scrutiny. It is possible that the passage of this bill could lead to a protracted legal battle, which is something the state should not spend its time and resources defending.
- 2) **Financial impact-** The City of Rose Hill's understands that an in-depth financial analysis has not been performed on this issue to determine the financial impact of this proposed change to the valuation process on state and local governments. During these tenuous economic times it is probably unwise to pass any bill with serious fiscal implications without a clear understanding of the overall impact on state government and local units of government.
- 3) **Equity-** The City of Rose Hill is concerned that this bill as currently written may be inequitable to new homeowners and new business owners. The bill as written would cause new homeowners and new business owners to closely scrutinize the inequitable tax burden placed on a new home and new business construction.

All of these concerns cause the City of Rose Hill to oppose the passage of HB 2263. Further study on the impacts of this bill need to be performed before implementation is considered. A bedroom community like Rose Hill with increasing property values has several policy considerations to examine if the valuation process was restructured in the manner contained in HB 2263.

The City of Rose Hill requests that the House Taxation Committee takes no further action on this study and only considers this bill after a more in depth examination of the fiscal impacts of such a change in the valuation of all property occurs.

**Testimony to the Taxation Committee of the Kansas House of Representatives  
Given by Jeff Bridges, City Administrator, City of Andover  
House Bill 2263  
Thursday, April 3, 2003**

House Bill 2263 is a proposal to limit the growth of the appraised valuation of property by prohibiting an increase in value on existing properties above a set formula. In effect this bill eliminates the entire premise and corner stone of the property appraisal system in Kansas, the equality of taxation, and creates an arbitrary, unfair, and unconstitutional property taxation system.

The Constitution of the State of Kansas Article 11 Section 1 states that "... the legislature shall provide for a uniform and equal basis of valuation and rate of taxation of all property subject to taxation."

HB 2263 eliminates the equality of the current tax system by allowing market value to be the determining factor in property taxation only when the property is sold, reconstructed, or improved. In effect two similar houses built in the same year, requiring the same level of service from local or state government, could have significantly different tax burdens due to something as arbitrary as one owner living there for one year versus an owner that has lived there ten years. The essence of a fair tax system is that like persons, and like properties, share equally the burden of taxation. Under HB 2263 this would not exist and owners would pay disproportionate taxes for the same services. This is arbitrary, unfair, and unconstitutional.

The current system of a market value driven appraisal provides the most equitable way to determine taxable value. Generally speaking, market value is defined as what a willing buyer is will to pay a willing seller. The current system of taxation, not only for property tax, but all taxes is not based upon the particular item, but rather based upon the value of the item. For instance, sales taxes are not based upon the product, the soda pop is not taxed, rather the retail sales transaction is taxed at a set percent. Income taxes are the same. Two doctors are not taxed differently. The value of the income is taxed. Why should property be different?

I ask that this bill not be passed out of committee and that the committee preserve the current market driven valuation process and the practice of dividing the tax burden equally amongst owners of similar property.



League of Kansas Municipalities

Date: April 3, 2003  
To: House Taxation Committee  
From: Larry R. Baer  
Assistant Legal Counsel  
Re: HB 2263 - Testimony in Opposition

Thank you for allowing me to appear before the Committee today on behalf of the League of Kansas Municipalities and its member cities and present testimony in opposition to HB 2263.

As we understand HB 2263, it proposes to place a systematic limit or restriction upon the amount of the annual increases in property valuation. The limitation results because the increase is tied to a percentage or fraction derived from the US Department of Labor's consumer price index.

A limitation or restriction on property valuations has the net effect of creating a state imposed spending lid because the same mill levy will result in less revenue being raised than if property is valued using the fair market value required in K.S.A. 79-503a. Because local spending and taxing decisions are best left to locally elected officials, we oppose this type of legislation.

More critically, we believe that the exceptions contained in HB 2263 violate the "uniform and equal" provision in Article 11, § 1 of the Kansas Constitution. Article 11, § 1 of the Kansas Constitution provides, in part: ". . . , the legislature shall provide for a **uniform and equal** basis of valuation and rate of taxation of all property subject to taxation. . . ."

The Kansas appellate courts have often stated: "Uniformity in taxation implies equality in the burden of taxation, and this equality cannot exist without uniformity in the basis of valuation. Uniformity in taxation does not permit a systematic, arbitrary, or intentional higher [or lower] valuation than that placed on other similar property within the same taxing district."

What does this mean? It means that not just the tax rate must be uniform and equal for a given class of property but, also, that the method of determining the valuation of the property must be uniform and equal. The exceptions contained in HB 2263 result in a method of valuation that does not give uniform and equal results.

For example, assume two houses, side-by-side, identical lots, appraised valuations of \$100,000. Also, assume that the HB 2263 cap is applicable. If we assume that the annual increase is capped at 1% and both properties remain under the same ownership for 3 years, the properties would have an appraised value of \$103,030. At the end of 3 years, one property sells for \$108,000, which we will assume represents a negotiated sale between a willing buyer and a willing seller, i.e. it sells for fair market value. Based upon HB 2263, the appraised valuation of the second property is increased to take into account the sale value, fair market value. The first house continues to be valued at its "capped rate" which has been

systematically, arbitrarily and intentionally limited. This results in nonuniformity in the basis of the valuation. Property one is valued at \$103,030 and property 2 is valued at \$108,000. If both properties are residential properties, the \$103,030 property has an assessed valuation of \$11,845 and the \$108,000 property has an assessed valuation of \$12,420. Regardless of what tax rate you apply, the amount of tax is not uniform and equal. Nonuniformity in the basis of valuation results in nonuniformity in the burden of taxation.

Therefore, the League believes that the changes proposed by HB 2263 likely will not withstand a constitutional challenge. For this reason the League urges the Committee to reject HB 2263.

Even if the changes posed by HB 2263 were not unconstitutional, the League would still oppose it because it does not present sound policy. The long term result in this type of legislation is that the state would end up in a very similar, if not identical, situation that we saw before statewide reappraisal and changes in the appraisal process done some 10 to 15 years ago. That is, older properties without sales would be significantly undervalued compared to newer properties or properties that sold on a regular and recurring basis.

This type of legislation also has the potential for a regressive effect on Kansas economy. Why would you want to purchase property, improve property or construct new facilities if each time you did so the transaction results in the appraised value being increased to fair market value without limitations. Holding old property, without improving it, permits you to be taxed on an artificially low value.

Local governments are faced with unfunded mandates, ADA compliance requirements, groundwater pollution cleanup, wastewater treatment, and the like. In addition, they are also faced with increasing expenses that are beyond their control: health care costs, workers compensation, utilities, fuel, maintenance and parts for equipment. Many of these expenses were met with payments received from demand transfers – dollars that the local governments no longer have – therefore, more dollars need to be generated at the local level, not less.

Appreciation in property value is not a bad thing. Historically, it is the appreciation in property values that allows mill levies to remain nearly flat or to decline. In other words, increases in revenue, as needed, can be generated by the same or lesser mill levies because of property valuation increases which fairly and accurately take into account appreciation and market place factors.

For the above reasons the League of Kansas Municipalities opposes HB 2263.

Thank you for the opportunity to appear and present testimony on HB 2063. I will stand for questions when appropriate.

# LEGISLATIVE TESTIMONY



*The Unified Voice of Business*

835 SW Topeka Blvd. • Topeka, KS 66612-1671 • 785-357-6321 • Fax: 785-357-4732 • E-mail: [kcci@kansaschamber.org](mailto:kcci@kansaschamber.org) • [www.kansaschamber.org](http://www.kansaschamber.org)

## HB 2263

April 3, 2003

KANSAS CHAMBER OF COMMERCE AND INDUSTRY

Testimony before the House Taxation Committee  
By Marlee Carpenter, Director of Taxation and Small Business

Chairman Edmonds and members of the Committee:

My name is Marlee Carpenter and I am the Director of Taxation and Small Business for the Kansas Chamber of Commerce and Industry. The Kansas Chamber has adopted a policy that supports the valuation of all real property, with the exception of agricultural land, be based on fair market value and opposes any caps on fair market value increases. Because of this policy, we must oppose HB 2263.

HB 2263 will limit property valuations to the consumer price index published by the federal department of labor. The Consumer Price Index (CPI) is not an adequate indicator of the fluctuations in the value of real property. The CPI represents all goods and services purchased for consumption by the reference population. The CPI does not represent the fluctuations in the values of real property.

The Kansas Chamber believes that any proposal that limits a fair valuation will cause a shift in the property tax burden. Additionally, the limits on the valuation of property will force local units of government to raise the mill-levy at an increased rate. Commercial property, which is assessed at 25%, machinery and equipment, which are assessed at 25%, and utilities, which are assessed at 33%, will bear the brunt of this increased mill-levy and the property tax burden. Residential property owners, who are assessed at 11.5%, will get substantially more tax relief.

The Kansas Chamber of Commerce and Industry believes that the best tax policy is to value property at

House Taxation  
Attachment 9  
Date 4-3-03



its fair market value. Any proposal that limits a fair valuation will shift the tax burden and place it on commercial property, machinery and equipment, and utilities. This practice is inherently unfair. We urge you to not pass HB 2263.

**About the Kansas Chamber of Commerce and Industry**

The Kansas Chamber of Commerce and Industry (KCCI) is the leading broad-based business organization in Kansas. KCCI is dedicated to the promotion of economic growth and job creation and to the protection and support of the private competitive enterprise system.

KCCI is comprised of nearly 2,000 businesses, which includes 200 local and regional chambers of commerce and trade organizations that represent more than 161,000 business men and women. The organization represents both large and small employers in Kansas. 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.



# K A N S A S

JOAN WAGNON, SECRETARY

DEPARTMENT OF REVENUE  
DIVISION OF PROPERTY VALUATION

KATHLEEN SEBELIUS, GOVERNOR

Testimony to House Tax Committee  
Mark S. Beck  
Director of Property Valuation

April 3, 2003

House Bill 2263

Chairman Edmonds and Members of the Committee:

Art. 11, § 1 of the Kansas Constitution requires that the legislature provide for a uniform and equal basis of valuation and rate of taxation. The equal basis currently provided by the legislature is "fair market value." *State ex rel. Stephan v. Martin*, 227 Kan. 456, 462, 608 P.2d 880 (1980). "Fair market value" has a generally understood and accepted meaning in our free economy and in case law. "Fair market value" means:

"Fair market value in money shall mean the amount of money that a well informed buyer is justified in paying and a well informed seller is justified in accepting, assuming that the parties thereto are acting without undue compulsion and that the property has been offered at the market place for a reasonable period of time. . . ."

*Mobil Pipeline Co. v. Rohmiller*, 905, 926, 522 P.2d 923 (1974).

The Supreme Court of Kansas has struck down as a violation of art. 11, § 1 of the Kansas Constitution attempts to depart from the mandate of "fair market value" most notably in the early 1980s when legislation was enacted to require farm machinery and equipment to be valued at "average loan value" rather than "fair market value." The Court stated:

[A]rt. 11, § 1 of the Kansas Constitution prohibits favoritism, and requires uniformity in valuing property for assessment purposes so that the burden of taxation will be equal. *Addington v. Board of County Commissioners*, 191 Kan. at 532. *Wheeler v. Weightman*, 96 Kan. at 58; *Hines, et al. v. City of*

*Leavenworth et al.*, 3 Kan. \*186, Syl. ¶ 5. Property taxation is not based upon the owner's ability to pay. Economic distress is no justification for ignoring the constitution.

*State ex rel. Stephan v. Martin*, 227 Kan. 456, 468, 608 P.2d 880 (1980).

HB 2263 amends K.S.A. 79-503a to limit valuation increases based on the consumer price index. Such value caps require an amendment to our constitution in order to pass constitutional muster. Generally, higher valued and newer construction increases in value at a faster rate than lower valued and older construction. The effect of value caps is to shift the property tax burden from newer, more expensive properties to older, less expensive properties. Value caps violate the very concept of "uniform and equal" taxation and, therefore, violate art. 11, § 1 of the Kansas Constitution.

Besides HB 2263's constitutional problems, the bill has significant administrative problems. The value cap imposed by this bill does not apply to improvements undertaken and authorized by building permits. However, there conceivably are jurisdictions which do not require building permits; thus, would the value cap would apply in those jurisdictions notwithstanding the new improvements? Likewise, would the value cap not apply in those situations where the improvement is undertaken in violation of the requirement to obtain a building permit?

The value cap is also not applicable when there has been a sale, but only when a "certificate of value", or what is now statutorily called a "real estate sales valuation questionnaire" has been filed. The issue that arises here is that filing the questionnaire is not mandatory. The filing of a real estate sales validation questionnaire is only a prerequisite to the recordation of a deed or affidavit of equitable interest. Thus, arguably the purchaser of the property could avoid a value increase by not recording the deed.

Assuming the issues with building permits and questionnaires can be resolved and the cap does not immediately apply to those properties, they will be valued at market value creating instant non-uniform treatment of select properties. Thus again we confront serious constitutional issues.

## CONCEPT

- Annually identifying market value but limiting the increases in the value of real property to no more than the increase in the Consumer Price Index. For purposes of this illustration, we have used the Consumer Price Index for all Urban Consumers (CPI-U) for the Kansas City area acquired from the U.S. Department of Labor, Bureau of Labor Statistics.
- Following are properties from Johnson and Wyandotte counties. The samples consist of residential properties that are increasing in value, remaining relatively stable and properties that are declining in value. The properties include a brief description and a graph depicting the relationship between the annual market changes and the change based on the CPI-U. The examples given make the assumption that any property value decreasing will not be limited by the defined percentage. In the calculations to follow a base maximum percent used was 3%. The CPI-U is shown below for the year developed and the tax year applied against.

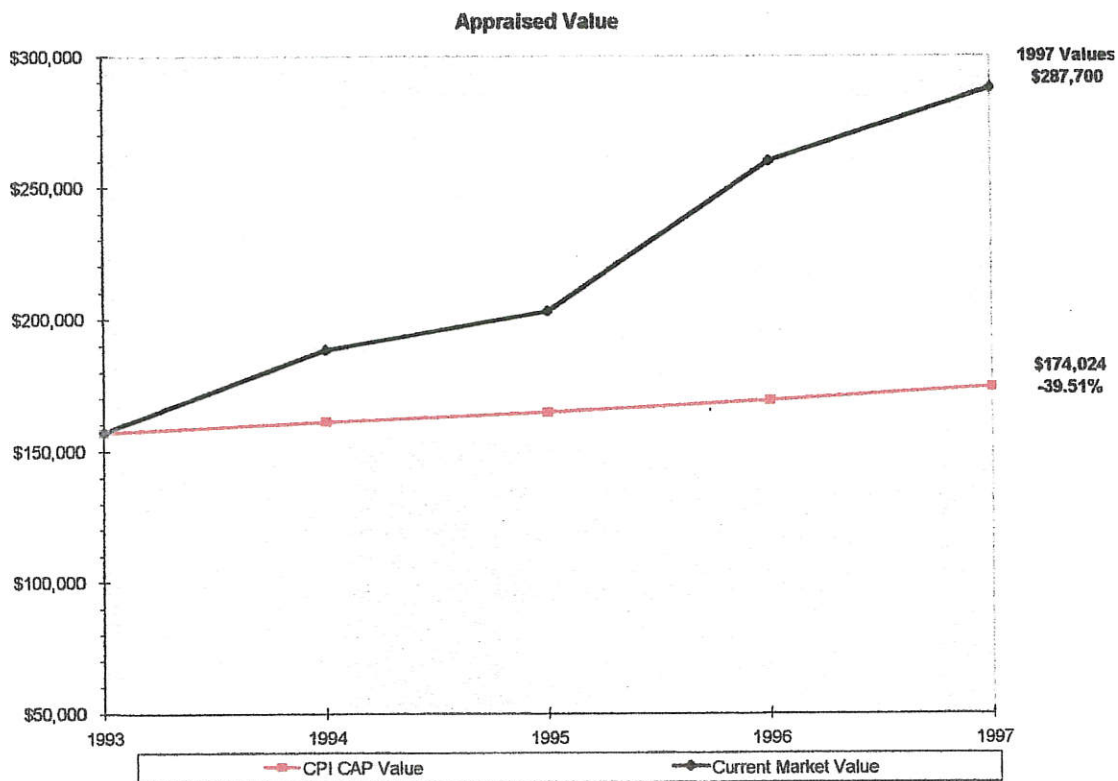
Tax Year	CPI-U Housing KC.	Year Developed
1994	2.5%	1993
1995	2.1%	1994
1996	2.7%	1995
1997	4.2% (3% cap)	1996



16501 Horton St.  
046-7P1-40-0-00-00-00.17

This property is a five bedroom, three and one-half bath, full basement Conventional Style home with a two car garage. The home contains 3,760 square feet of living area and is located on a 141 ft. x 305 ft. lot. This home was built in 1976 and is considered a B grade.

- Value comparison of current market value to CPI CAP value.
- Appreciating neighborhood.

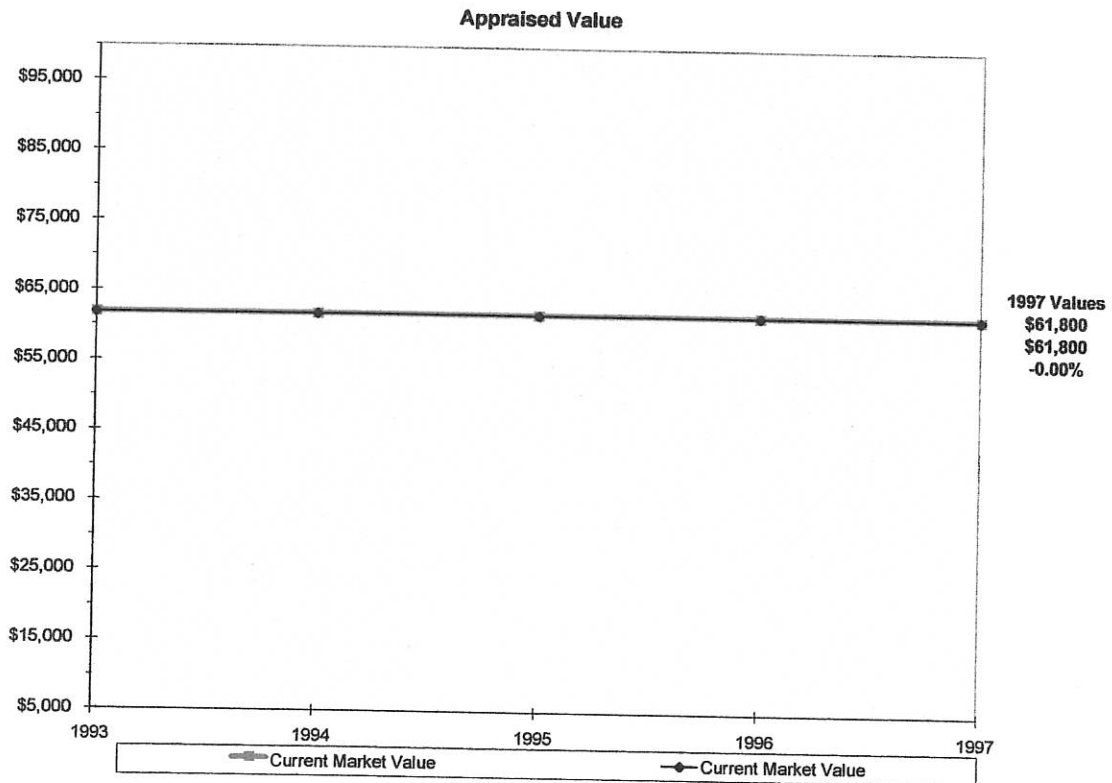




7322 Lafayette Lane  
105-022-00-0

This property is a three bedroom, two bath, full basement Bilevel Style home with a two car basement garage. The home contains 1702 square feet of living area and is located on a 85 ft. x 150 ft. lot. This home was built in 1963 and is considered a C grade.

- Value Comparison of current market value to CPI CAP value.
- Static neighborhood.



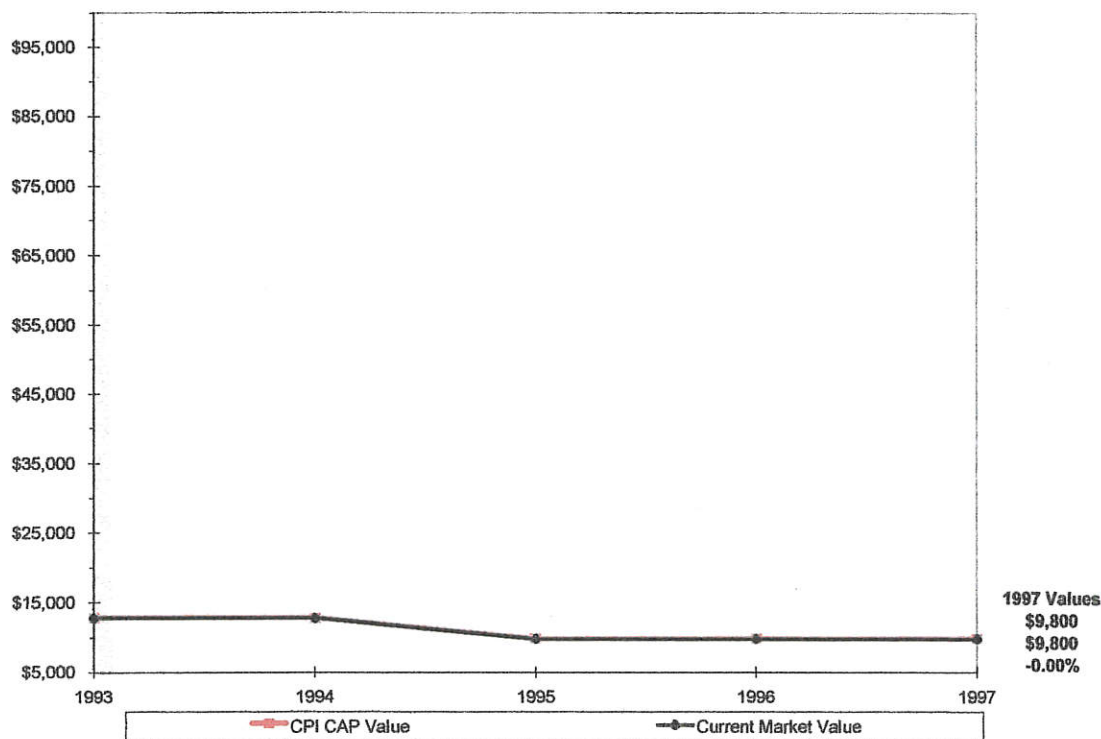


1118 Argentine Boulevard  
105-072-55-9

This property is a two bedroom, one bath, partial basement Bungalow Style home with no garage. The home contains 967 square feet of living area and is located on a 25 ft. x 115 ft. lot. This home was built in 1920 and is considered a D grade.

- Value Comparison of current market value to CPI CAP value.
- Declining neighborhood.

Appraised Value



# Tax Shift Comparison

1992 CPI 1.4%    1993 CPI 2.5%    1994 CPI 2.1%    1995 CPI 2.7%    1996 CPI 4.2% (3% cap)

Total Taxes needed  
\$270,250.00

## Neighborhood A (Appreciating 8% per year)

Valuation Year	Market Value				CPI CAP Value			
	Total Value	Total Assessed Value	Mill Levy	Tax Dollars	Total Value	Total Assessed Value	Mill Levy	Tax Dollars
1993	\$15,000,000	\$1,725,000	100.000	\$172,500.00	\$14,083,333	\$1,619,583	104.059	\$168,532.29
1994	\$16,200,000	\$1,863,000	95.335	\$177,608.52	\$14,435,417	\$1,660,073	102.685	\$170,465.38
1995	\$17,496,000	\$2,012,040	90.744	\$182,580.76	\$14,738,560	\$1,694,934	101.558	\$172,133.60
1996	\$18,895,680	\$2,173,003	86.243	\$187,405.82	\$15,136,502	\$1,740,698	100.045	\$174,147.72
1997	\$20,407,334	\$2,346,843	81.844	\$192,074.43	\$15,590,597	\$1,792,919	98.341	\$176,316.86

## Neighborhood B (Static)

Valuation Year	Market Value				CPI CAP Value			
	Total Value	Total Assesse Value	Mill Levy	Tax Dollars	Total Value	Total Assesse Value	Mill Levy	Tax Dollars
1993	\$6,000,000	\$690,000	100.000	\$69,000.00	\$6,000,000	\$690,000	104.059	\$71,800.74
1994	\$6,000,000	\$690,000	95.335	\$65,780.93	\$6,000,000	\$690,000	102.685	\$70,852.98
1995	\$6,000,000	\$690,000	90.744	\$62,613.43	\$6,000,000	\$690,000	101.558	\$70,074.80
1996	\$6,000,000	\$690,000	86.243	\$59,507.51	\$6,000,000	\$690,000	100.045	\$69,030.90
1997	\$6,000,000	\$690,000	81.844	\$56,472.18	\$6,000,000	\$690,000	98.341	\$67,855.08

## Neighborhood C (Declining 2% per year)

Valuation Year	Market Value				CPI CAP Value			
	Total Value	Total Assesse Value	Mill Levy	Tax Dollars	Total Value	Total Assesse Value	Mill Levy	Tax Dollars
1993	\$2,500,000	\$287,500	100.000	\$28,750.00	\$2,500,000	\$287,500	104.059	\$29,916.97
1994	\$2,450,000	\$281,750	95.335	\$26,860.55	\$2,450,000	\$281,750	102.685	\$28,931.63
1995	\$2,401,000	\$276,115	90.744	\$25,055.81	\$2,401,000	\$276,115	101.558	\$28,041.60
1996	\$2,352,980	\$270,593	86.243	\$23,336.66	\$2,352,980	\$270,593	100.045	\$27,071.39
1997	\$2,305,920	\$265,181	81.844	\$21,703.39	\$2,305,920	\$265,181	98.341	\$26,078.07



# Summary

Valuation Year	Neighborhood A			Neighborhood B			Neighborhood C		
	Market Taxes	CPI CAP Taxes	% Difference	Market Taxes	CPI CAP Taxes	% Difference	Market Taxes	CPI CAP Taxes	% Difference
1993	\$172,500.00	\$168,532.29	-2.30%	\$69,000.00	\$71,800.74	4.06%	\$28,750.00	\$29,916.97	4.06%
1994	\$177,608.52	\$170,465.38	-4.02%	\$65,780.93	\$70,852.98	7.71%	\$26,860.55	\$28,931.63	7.71%
1995	\$182,580.76	\$172,133.60	-5.72%	\$62,613.43	\$70,074.80	11.92%	\$25,055.81	\$28,041.60	11.92%
1996	\$187,405.82	\$174,147.72	-7.07%	\$59,507.51	\$69,030.90	16.00%	\$23,336.66	\$27,071.39	16.00%
1997	\$192,074.43	\$176,316.86	-8.20%	\$56,472.18	\$67,855.08	20.16%	\$21,703.39	\$26,078.07	20.16%

The three neighborhoods A, B, and C consist of the following:

Neighborhood A - 100 homes with an average value of \$150,00 each

Neighborhood B - 100 homes with an average value of \$60,000 each

Neighborhood C - 100 homes with an average value of \$25,000 each

Neighborhood A is appreciating at the rate of eight percent per year, neighborhood B is static, and neighborhood C is declining at the rate of two percent per year. The three neighborhoods combined must raise \$270,250 in tax revenue. For purposes of this illustration, we have used the same total tax revenue for all five valuation years.

## Concerns

### Appeals

- Current appeal statutes will require amendment to clarify just what is appealable. Would only the current year's market value, forming the basis for it's taxable value with the growth limit applied, be appealable?
- If the previous years taxable or market values are allowed to be challenged, several years of historical market data must be accessible for appeals. This will increase administrative costs by retaining historical market data to be used in appeals.

### Tax

- If tax values do not grow proportionately because of the percent growth limit concept, unless spending is reduced mill levies will change to offset the difference and impose the offsetting burden on all properties.
- If the mill levy must be adjusted as a result of the use of the percent growth limit concept, various class' of property will pick up a disproportional share of the increased levies.

### Concept

- This process would benefit the property owners in affluent subdivisions with increasing markets. Property owners in older, slow growth areas of the inner city and low income residents in declining neighborhoods, as well as most rural property owners, will see little or no benefit. Ultimately, property owners in slow growth areas will be paying property taxes at a higher percentage of taxes to market value.
- The growth limit percent concept may lead to annual increases in taxable value, even when there is no current increase in market value.

## Administrative Process

- The growth limit percent concept will create a number of unique problems for public utility real property. The market value of a public utility is, by statute, developed on a "unitary basis".
- Legislation would be necessary to determine how the growth limit percent concept would be applied or influenced when a property is "split or combined".
- Legislation would be necessary to determine how the growth limit percent concept would be applied or influenced when property changes use and/or class.
- Legislation would be necessary to determine how the growth limit percent concept would be applied or influenced when a property sustained additions, demolition or damage due to natural disaster.
- The current Kansas CAMA system does not have an historical file. Software enhancements to administer the additional years data would be required.
- The current hardware used to operate the CAMA system on the AS400 is sized and configured for storage to handle the current software. Additional storage would be required to hold the additional historical data and resultant appeal computations.

**WRITTEN TESTIMONY**  
concerning HB 2263  
Limiting Growth in Appraised Valuation of Real Estate  
House Taxation Committee  
Submitted by Randall Allen, Kansas Association of Counties  
April 3, 2003

Thank you, Chairman Edmonds and members of the committee, for the opportunity to submit written testimony on Representative Patterson's proposal to limit the growth (with certain exceptions) in the appraised valuation of real estate from one year to the next to the growth in the Consumer Price Index (CPI).

We at the Kansas Association of Counties object to the proposal for two basic reasons:

1) Except for the 1.5 mill levy for state building projects and the mandatory state-wide mill levy for public schools, limiting the growth in appraised valuation of real estate to a cap of a certain percentage growth from the prior year would in no way guarantee lower taxes. If values are normally increasing and are not allowed to increase at a rate suggested by market forces, county clerks would merely set higher levies (expressed in mill levy rates) to compensate for the relatively lower aggregate property values based on counties' legally adopted budgets – all other factors being equal. There is a common misperception that county commissioners and other locally elected officials set tax rates. In reality, local governing bodies adopt budgets and county clerks set tax rates. If a goal of imposing a cap on growth in appraised value is to somehow limit taxes or spending in the aggregate, this proposal does not accomplish this goal.

2) The second concern about this proposal is the inequity that it seems to create between and among parcels. If the fair market value of one property increases from \$100,000 to \$108,000 in a year's time (or an 8% increase) while a property across town increases from \$100,000 to only \$102,000 in a year's time (or a 2% increase), and assuming that a cap is imposed based on a 3% growth in the CPI, why should the owner of the second property pay taxes at an inevitably higher mill levy rate resulting from the artificial cap on the growth in appraised values, when that burden should be borne by the first taxpayer and all other taxpayers who are in the same circumstances?

House Taxation  
Attachment 11  
Date 4-3-03

After experiencing years of neglect in our property tax administration system in the 1960s, 70s, and 80s, county commissioners and state officials expended the fiscal and political capital to make our system better. It is not perfect, but it is infinitely better than it was before property values were revisited on an annual basis. I urge the committee to refrain from imposing an artificial cap on annual changes in appraised property values. Let the values reflect reality as nearly as possible. Thank you.

The Kansas Association of Counties, an instrumentality of member Counties under K.S.A. 19-2690, provides legislative representation, educational and technical services and a wide range of informational services to its member counties. Inquiries concerning this testimony should be directed to the KAC by calling (785) 272-2585.