

MINUTES OF THE SENATE ASSESSMENT AND TAXATION COMMITTEE

The meeting was called to order by Chairperson David Corbin at 10:45 a.m. on February 13, 2003, in Room 519-S of the Capitol.

All members were present except: Senator Haley

Committee staff present: Chris Courtwright, Legislative Research Department
Gordon Self, Revisor of Statutes Office
Shirley Higgins, Committee Secretary

Conferees appearing before the committee: Nancy Schmidt Roush, Attorney at Law
Martin Dickinson, Professor of Law
Jim Weisberger, Kansas Department of Revenue
T.C. Anderson, Kansas Society of Certified Public Accountants
Allie Devine, Kansas Livestock Association
Richard Cram, Kansas Department of Revenue
Senator Derek Schmidt

Others attending: See attached list.

Senator Corbin called the Committee's attention to the minutes of the February 11 meeting. Senator Goodwin moved to approve the minutes of the February 11, 2003, meeting, seconded by Senator Buhler. The motion carried.

SB 94—Repealing inheritance or succession tax

SB 148—Enacting the Kansas Estate Tax Act

Nancy Schmidt Roush, an attorney from Overland Park, testified in support of **SB 148**, noting that she was a member of the group which drafted the proposed Kansas Estate Tax Act. She discussed the following concerns regarding the existing death taxes in Kansas, including the existing Kansas estate tax and Kansas succession tax: (1) Increased cost, complication, and confusion to Kansans who are planning their estates dealing with the death of a family member, and (2) Difficulty for the Department of Revenue to effectively enforce and collect the taxes. She contended that the proposed Kansas Estate Tax Act would solve significant problems and give Kansas a workable and enforceable death tax. She went on to discuss related information under the headings in her written testimony, "Summary of Kansas Estate Tax Act" and "Problem Areas in Kansas Death Taxes." (Attachment 1)

In response to a question from Senator Clark regarding the significant difference in the fiscal note for **SB 148** and **SB 94**, Richard Cram, Kansas Department of Revenue, explained that the Department discovered after **SB 148** was published that the rate schedule was too low. The Department's intent is to develop a fiscally neutral, stand-alone estate tax. Ms. Roush added that **SB 148** would retroactively repeal the succession tax back to June 6, 2002, and the new Kansas estate tax would be in effect from January 1, 2003.

Martin Dickinson, a professor of law at the University of Kansas, testified in support of **SB 94** and **SB 148**, noting that he worked with Ms. Roush and others to draft the proposed Kansas Estate Tax. He discussed the problem inherent in basing Kansas taxation on federal law, emphasizing that Kansas must "decouple" and move to a free standing Kansas estate tax that can operate efficiently and assure adequate revenue, regardless of what Congress may do in the future. He noted that the tax rate structure in Section 3 of **SB 148** can be modified to produce whatever revenue is desired. (Attachment 2)

Jim Weisberger, Kansas Department of Revenue, testified in support of **SB 148**. He said, currently, the Department has two separate tax structures in the estate tax and in the succession tax which it cannot administer. The Department's primary focus is to develop a tax structure that works and is revenue neutral.

CONTINUATION SHEET

MINUTES OF THE SENATE ASSESSMENT AND TAXATION COMMITTEE at 10:45 a.m. on February 13, 2003, in Room 519-S of the Capitol.

The bill replaces both the current "pick-up" tax and the succession tax and creates a stand-alone Kansas estate tax which is workable. For the Committee's information, he called attention to a brief outline of the sections of the bill attached to his written testimony. ([Attachment 3](#))

T.C. Anderson, Kansas Society of Certified Public Accountants (KSCPA), stood in support of **SB 148** and the testimony given by previous conferees. He explained that a KSCPA task force reviewed the proposed Kansas Estate Tax Act and adopted it as part of its legislative platform for 2003. ([Attachment 4](#))

Mr. Cram informed the Committee that the Department of Revenue will recommend technical amendments to **SB 148** in the near future. In this regard, he called attention to a suggested amendment to the rate schedule outlined in the written testimony provided by Mr. Weisberger. He went on to explain data in the tables entitled, "Comparison of Adjusted Kansas Estate Tax Rates," for years 2003 through 2006 and the data in a table on the estimate for the Kansas Estate Tax for fiscal years 2003 through 2010. He also noted that the Department recommends that Section 54 be amended to provide that any refunds of previously paid Kansas succession tax shall be paid without interest.

Allie Devine, Kansas Livestock Association (KLA), testified in opposition to **SB 148** and in support of **SB 94**. With regard to **SB 148**, she explained that KLA members are adamantly apposed because they view death taxes as an obstacle to the survival of ranching and farming operations, small businesses, and the preservation of a family legacy. She pointed out that, while the federal government is moving away from estate taxes, the bill resurrects them in Kansas. Although KLA members understand that the bill seeks to address administrative problems with the current Kansas law tied to the federal law, they are not convinced that a free standing estate tax will decrease the complications. She urged the Committee to take the time to develop good information on the issues before proceeding. With regard to **SB 94**, Ms. Devine stated that KLA members philosophically support the bill because they want to assure that no one is precluded from continuing the family business operation. ([Attachment 5](#))

Senator Corbin called the Committee's attention to written testimony in support of **SB 94** and **SB 148** submitted by Marlee Carpenter, Kansas Chamber of Commerce and Industry, ([Attachment 6](#)) and written testimony in support of **SB 94** but questioning the benefits of **SB 148** submitted by Leslie Kaufman, Kansas Farm Bureau ([Attachment 7](#)). There being no other persons wishing to testify on **SB 148**, Senator Corbin closed the hearing and called upon the sponsor of **SB 94**, Senator Derek Schmidt, for further testimony.

Senator Schmidt discussed the following reasons he believes that the succession tax enacted last year should be repealed retroactively: (1) It is not significantly helping to balance the state budget, (2) It constitutes triple taxation by the state, (3) It is unfair on its face, (4) It is exceptionally confusing, and (5) It is a tax on honesty. He emphasized the succession tax was bad public policy when it was enacted, and it has proven to be worse public policy in practice. In conclusion, he strongly recommended that the succession tax be abolished before it does any more harm. ([Attachment 8](#)) With this, the hearing on **SB 94** was closed.

Chris Courtwright, Kansas Legislative Research Department, distributed a memorandum to the Committee regarding the fiscal impact of various death tax provisions ([Attachment 9](#)) and a report on the extent to which the 50 states conform to the estate tax provision of the new federal law ([Attachment 10](#)).

The meeting was adjourned at 11:40 a.m.

The next meeting is scheduled for February 14, 2003.

SENATE ASSESSMENT AND TAXATION COMMITTEE GUEST LIST

DATE: February 13, 2003

NAME	REPRESENTING
Jim Weisgenher	KDOR
Richard Cram	KDOR
Ann Duskes	DOB
Trista Curzydlo	KS Bar Assn
Nancy Kovsh	KS Bar Assn
MARTIN DICKINSON	NONE
Natalie Bright	WIBA
Malle Carpenter	KCET
Leslie Kaufman	KS Farm Bureau
Alli Quinn	KCA
Mark Leonard	Kansas, Inc.
Larry Hoobler	KS Farm Bureau
Chris Van Gyle	KS Farm Bureau
Bill Brady	KS Gov't Consulting
Whitney Damron	KS Bar Assn.
Kathy Oken	KS Bankers Assn.
Ron Seiber	Hein Law Firm
Pam Scott	KS Funeral Directors Assn
Hal Hudson	NEFB/KS

**KANSAS ESTATE TAX ACT
SENATE BILL No. 148**

**Written Testimony
by
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February 13, 2003

I am an attorney and I have practiced in the areas of estate tax planning and probate in Kansas for over 20 years. I am a member of the executive committees (and past president) of both the Real Estate, Probate and Trust Section and Tax Section of the Kansas Bar Association.

I am one of the group who drafted the proposed Kansas Estate Tax Act set out in Senate Bill No. 148. Other drafters are Martin Dickinson, a professor of law at KU Law School, Tim O'Sullivan and Terry Fry, both practicing attorneys in Wichita, and Jim Weisegerber, the death tax specialist at the Kansas Department of Revenue. I have attached a summary I prepared of the proposed Act.

There are significant problems with the existing death taxes in Kansas (which includes the existing Kansas estate tax and Kansas succession tax). The attached outline describes those problem areas in detail. The problems created by the existing death taxes have two consequences:

(i) increased cost, complication, and confusion to Kansans who are planning their estates dealing with the death of a family member;

(ii) difficulty for the Department of Revenue to effectively enforce and collect the taxes.

I have been contacted by numerous Kansas attorneys and accountants, whose practice involves planning for death taxes and preparation of death tax returns. They have been unanimous regarding the urgent need for a solution to this problem. The Kansas Bar Association Board of Governors has endorsed the proposed Kansas Estate Tax Act.

Given the need for a revenue-neutral solution, I believe the proposed Kansas Estate Tax Act would solve significant problems and give Kansas a workable and enforceable death tax.

SUMMARY OF KANSAS ESTATE TAX ACT

**Senate Bill No. 148
2003 Legislative Session**

**Prepared by Nancy Schmidt Roush
February 2003**

Effective Dates and Repeal of Prior Law

Currently Kansas has an estate tax that imposes a tax equal to the state death tax credit on the federal estate tax return (referred to as a "pick-up" tax). This tax is "anchored" in the old federal estate tax law, however. This means that for decedents dying after January 1, 2002, a "pretend" federal estate tax return must be prepared based on the old federal filing limits and estate tax exemption in order to calculate the Kansas tax, and the Kansas tax may bear no relationship to the actual federal credit. The proposed Kansas estate tax would be effective January 1 of 2003, and would repeal the existing Kansas estate tax on that date. Therefore the "disconnect" between the Kansas pick-up tax on the federal tax would occur only for decedents dying in 2002.

Currently Kansas also has a succession tax for decedents dying on or after June 6, 2002. This tax is fraught with problems because it is unclear when the tax is imposed, who is responsible for paying the tax, and when the tax is due. The proposed Kansas estate tax would repeal the succession tax retroactively.

Connection to the Federal Estate Tax

The proposed Kansas estate tax is a "free-standing" tax, and is not connected to the old, new or future (if any) federal estate tax. Although concepts such as the gross estate, taxable estate and marital deduction are similar to the existing federal estate tax, the proposed Kansas estate tax would be determined independently of any calculation of the federal tax, or any allocations or elections made for federal purposes.

If the state death tax credit allowed on the decedent's federal estate tax return exceeds the tax owed Kansas under the proposed Kansas estate tax, however, Kansas would impose an additional tax equal to that excess. (The state death tax credit is being phased out and will be eliminated at the federal level in 2005.)

Calculation of Gross Estate and Taxable Estate

The concept of the gross estate is similar to the federal gross estate and generally includes all property in which the decedent had an interest or certain powers at the time of death. Unlike the federal estate tax, which is backed up by a gift tax, there is no Kansas gift tax. Therefore all transfers or relinquishment of powers within one year of death are included in the Kansas gross estate except "annual exclusion" gifts.

The concept of the taxable estate is also similar to the federal taxable estate and generally allows deductions for debts and expenses, and for gifts to a spouse or charity. There

are two important differences. First, a deduction is allowed for any federal estate tax imposed on the estate. Second, there are two alternatives for deducting the spouse's interest in a trust. One alternative is based on the federal "QTIP" concept, which means that the full value of the trust can be deducted, but the full value of what remains in the trust on the spouse's death is included in the spouse's gross estate. The other alternative is based on the old Kansas inheritance concept of deducting the value of the spouse's interest in the trust, but not the remainder interest; as a result nothing is included in the spouse's gross estate.

Filing Threshold and Rates

The proposed Kansas estate tax is intended to be revenue neutral. The proposed filing threshold is \$750,000. This means if the decedent's gross estate is \$750,000 or less (calculated before any deductions), no return is required and no tax is due. If the taxable estate is \$750,000 or less, no Kansas estate tax would be due. The proposed rates above that threshold start at 3.5% and reach 21% for taxable estates over \$10 million.

Kansas and Non-Kansas Property

If the estate has property with a Kansas tax situs and property subject to another jurisdiction, the tax is prorated based on the value of property in the gross estate with a Kansas tax situs.

Due Date and Responsibility for Filing

Like the current Kansas estate tax, the return must be filed and the tax is due nine months after the date of death. The Department of Revenue can grant extensions for the filing deadline.

The "personal representative" is responsible for filing the return, and if there is more than one personal representative they are each responsible for filing a return and reporting the property in their possession. A "personal representative" includes an executor or administrator of a Kansas probate estate, or anyone else who is in possession of property with a Kansas tax situs (such as a joint tenant or pay-on-death beneficiary).

Who bears the burden of the tax would be determined by the provisions of any applicable will or trust, or if none then the Kansas apportionment act.

PROBLEMS AREAS IN KANSAS DEATH TAXES

BY

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January 2003

Federal Estate Tax Changes

Before the 2001 changes, the estate tax calculation was straightforward – calculate the tax, apply the credit, and the result was the total estate tax. In Kansas, a pure “pick-up” states, the state death tax credit was applied to determine the amount owed to the state, with the rest owed at the federal level.

The 2001 tax changes affect state death taxes in several ways as follows:

*Increase in the estate tax applicable exclusion (“EE”): \$1,000,000 in 2002 & 2003; \$1,500,000 in 2004 & 2005, \$2,000,000 in 2006 - 2008, \$3,500,000 in 2009; repeal in 2010. If the state law conforms to this change, then no state return (and thus no state tax) is required if no federal return is required.

*Reduction in the amount of state death tax credit (“SDTC”): 75% in 2002; 50% in 2003; and 25% in 2004. If state law conforms to this change, this has the effect of lowering the tax owed to the state, but still allows a full deduction against the federal tax for what is paid at the state level. This in effect shifts some of the tax away from the state to the federal level.

*Change in the SDTC to a deduction: Beginning in 2005, the SDTC becomes a deduction. If state law conforms to this change, this has the effect of eliminating the state tax entirely beginning in 2005. If state law does not conform to this change, then there will still be a state tax, and that will reduce the federal tax, but not by as much as a credit would. For example, if the taxable estate is \$2,000,000, and the federal tax would otherwise be \$435,000 (45% bracket), a credit of \$100,000 saves \$100,000 in federal tax, but a deduction saves only \$45,000.

Kansas Estate Tax

The Kansas estate tax does not “conform” to the federal tax. A bill to conform in significant aspects was introduced in the 2002 legislative session, but did not pass. (Clearly any conformity to the federal tax is a revenue loser for the state.)

Kansas imposes a tax on every estate required by law to file a federal estate tax return. The amount of the tax is the maximum credit under IRC 2011 against the tax imposed by IRC 2001. The Kansas act says that references to the IRC are to the '86 Code as it existed on 12/31/97. (Kansas law is found at KSA Section 79-15,101 et seq.)

Requirement of Filing Federal Return.

Since the first provision imposing tax does not reference the IRC, presumably it is not “anchored” to the old estate tax law. This means that as the exemption equivalent (“EE”) rises, estates below the EE will not have to file a return and thus will not have to pay Kansas tax. This also means that if and when the estate tax is repealed, no one would be required to file a federal estate tax return, and thus repeal of the federal tax will repeal the Kansas tax. The Kansas Department of Revenue is taking the position, however, that the filing provision is anchored also. If that position is found to be correct, someone dying in 2002 with an estate over \$700,000, but not over \$1 million, would have to file a “pretend” federal return in Kansas and will owe Kansas tax equal to the SDTC calculated as though the federal law had not changed. It will be extraordinarily difficult for the Department of Revenue to enforce the filing of Kansas estate tax returns under these circumstances.

Assuming the filing threshold is not anchored, however, the federal filing requirement creates other issues. A federal estate tax return must be filed for all estates whose gross estate, plus adjusted taxable gifts and specific exemption, exceed the applicable exclusion. It is important to note that this is not the same as saying “all estates who owe estate tax.” The gross estate is before any reduction for the marital deduction, charitable deduction, or debts, taxes, expenses, and losses.

Example A: 2002 \$1,500,000 gross estate with a \$500,000 debt but no spouse: You still have to file a federal estate tax return, although no federal tax is due, and the SDTC, calculated under the old law (which would allow a \$700,000 EE for a 2002 estate) results in a Kansas tax. Contrast that with a 2002 \$1,000,000 gross estate with no debt or spouse: no Kansas tax. This is a strange result.

Effect of Anchor Under the Old Law.

The calculation of the SDTC under the old law means, presumably, that you use the EE based on the old increasing schedule for the actual year of death and you calculate the taxable estate using the gross estate less deductions, including the actual marital deduction taken on the federal return. The basis for using the old increasing EE would be

that the Kansas law doesn't reference IRC 2010, and old IRC 2011 does float based on changes in the unified credit under 2010.

Example B: 2002 \$2,000,000 gross estate, no deductions and no spouse: The gross estate is reduced by \$60,000 and the tax brackets applied, which means the SDTC (and thus the Kansas tax) is \$99,600. This is no different than before. The federal tax is different – the EE is more, but only 75% of the \$99,600 is allowed as a credit. Thus, the 2001 federal changes result in a net reduction of the overall estate tax, but not as much of a net reduction as would be generally expected.

The example gets more complicated when you have a spouse and a “reduce to zero” marital formula.

Example C: 2002 \$2,000,000 gross estate with no debt/expenses and a spouse with “reduce to zero” formula: A federal return is required, but you get a \$1,000,000 EE and (if \$1,000,000 goes to the spouse under the formula) you get a \$1,000,000 marital deduction, resulting in no federal tax. The Kansas tax calculation will start with the gross estate of \$2,000,000 and (if \$1,000,000 goes to the spouse under the formula) subtract the marital deduction of \$1,000,000, leaving a taxable estate of \$1,000,000. Normally no SDTC would be allowed on a 706 if there was no federal tax due, as the case here. But Kansas would ignore that and assume a federal tax was due since the taxable estate would have been \$300,000 under the old law. The SDTC on a \$1,000,000 taxable estate (and thus the Kansas estate tax) is \$33,200.

Effect of Drafting and Effect on Funding.

In example C, if the document provides that the shelter trust bears the burden of any death taxes, then the Kansas estate tax is paid from the Shelter Trust and the marital deduction is not affected. If the document does not provide that (and it may not if the drafter thought the “reduce-to-zero” formula would eliminate death tax if the spouse survived), then you would have a circular calculation which would increase the tax due.

In example C, the marital formula can make a difference also. Which way do we want our marital formula to work? Using example C, is it better to (i) pay \$33,200 in Kansas estate tax on the first death, but leave the shelter trust at \$1 M or (ii) pay no Kansas tax and have the shelter trust be \$700,000? The answer obviously varies depending on the facts. For example, if the surviving spouse is likely to die before 2004, the federal tax on the additional \$300,000 is around \$125,000, and it would be better to pay \$33,200 in Kansas estate tax now. If the survivor is likely to live longer and doesn't have additional assets, you probably would not want to pay any Kansas estate tax on the first death.

There may be many different marital formulas in use, with varying results. What is the impact of the following formula: “the largest amount that can pass free of federal estate tax under this section by reason of any credits, deductions, or exclusions allowable to my estate for the purposes of computing the federal estate tax, except for those which, if used, would increase the estate or other death taxes payable to any jurisdiction”?

Arguably, using the EE of the full \$1,000,000 increases the tax due to Kansas, since if the marital deduction amount was \$1,300,000, no Kansas tax would be due, and therefore puts \$700,000 in the shelter trust. What is the impact of this formula: "the largest amount that can pass free of federal estate tax under this section by reason of the state death tax credit, except if use of that credit would increase the death taxes payable to any state"? This probably puts \$1,000,000 in the shelter trust, but incurs Kansas tax even though the spouse survives.

If the formula would lower the shelter trust to \$700,000, then you can modify this after death with a disclaimer by the spouse, if the document was drafted so that any of the marital gift/trust disclaimed by the spouse went to the shelter trust. The disclaimer could presumably be a formula disclaimer of whatever additional property was required to fund the shelter trust to the current EE.

Regarding future drafting, the use of disclaimers, or a "one-lung" QTIP should allow the needed flexibility to decide at the time of the first death how you want the formula to work.

Kansas Succession Tax

The 2002 Kansas legislature passed, at the 11th hour, a succession tax. This tax is "supplemental" to the Kansas estate tax, and is effective for estates of decedents dying on or after June 6, 2002.

The tax is imposed on any "relative or stranger in the blood" receiving property subject to Kansas jurisdiction who is not one of the following: spouse, sibling, ancestor, descendant, step-parent, step-child, spouse of a child or step-child. The tax is calculated as follows: 10% of the first \$100,000, 12% of the next \$100,000, and 15% of amounts over \$200,000.

The press surrounding the bill indicated that it was intended to put back the inheritance tax on "class c" beneficiaries. The bill is very short and ambiguous, however, and raises more questions than it answers. For example:

*Are the brackets are calculated separately for each individual?

*Is a trust for a spouse (or other "exempt" relative) the same as the spouse (or other "exempt" relative) and thus not taxed?

*Is a charity a "stranger in the blood"? (The Department of Revenue at one time apparently took the position that the tax was imposed on charities, but now has reversed that position.)

*Does the individual or the estate bear the burden of the tax? (Although traditionally an inheritance tax is imposed on the individual receiving the property, this tax is styled a "succession" tax.)

*Is the tax due 9 months after death?

*How will the Department of Revenue collect or enforce this tax? (The provisions of the probate code that required an inheritance tax closing letter in order to close the estate have been repealed for estates of decedents dying after July 1, 1998, and no new provision has been made. What about the \$1,000 owed on the \$10,000 bank account payable on death to a niece living in another state?)

A standard tax clause that says to pay all death taxes from the residue may no longer be appropriate if there are gifts to more distant relatives. A formula which gives the EE to more distant relatives and the residue to the spouse, and pays the tax from the residue, will result in a significant distortion of the estate plan.

SENATE COMMITTEE ON ASSESSMENT AND TAXATION

February 13, 2003

Written Testimony of Martin Dickinson regarding SB 94 and SB 148

Committee Members:

SB 94 would repeal the succession tax adopted in 2002 (KSA 79-15,127). SB 148 would adopt a new Kansas estate tax, replacing the existing "pick-up" tax (KSA 79-15,100 et seq.). I believe adoption of both bills would be good for Kansas, and I respectfully offer the following suggestions for your consideration:

1. The succession tax adopted in 2002 is impractical and may prove difficult to enforce. It should be repealed retroactively.
2. Congressional enactment of the Economic Growth and Tax Relief Reconciliation Act of 2001 destroyed the premise on which the current pick-up tax is based—the provision of a full federal credit for taxes paid to Kansas. Because the Kansas pick-up tax is imposed in the amount of the federal credit, the phaseout of the federal credit has the effect of directly reducing, and eventually eliminating, the Kansas tax. The only way to prevent this is to tie the Kansas tax to prior federal law. The current Kansas law does exactly that, imposing a Kansas tax in the amount of the federal credit that was allowed under federal law as it existed on December 31, 1997. This requires that the executor of a decedent's estate be a historian and determine what the Internal Revenue Code said five years ago. The executor must then prepare a "phantom" federal return using 1997 law, and this return determines the tax owed to Kansas. In addition, if the estate is currently subject to federal tax, the executor must prepare a "real" federal return, using current law.
3. This illustrates the problem inherent in basing Kansas taxation on federal law. Kansas should "decouple" and move to a freestanding Kansas estate tax that can operate efficiently and assure adequate revenue, regardless of what Congress may do in the future.
4. The discarded inheritance tax regime was cumbersome and expensive, requiring computation of the exact dollar value of property going to each and every recipient. An estate tax is far preferable, lowering costs for both taxpayers and the Department of Revenue.
5. I believe that the SB 148 estate tax provides a sound solution to the problem of assuring an efficient and dependable revenue source.
 - A. The "gross estate" is determined using well established principles that have been developed at the federal level over 75 years of experience.

*Senate Assessment & Taxation
2-13-03
Attachment 2*

- B. A marital deduction is allowed for all transfers to a surviving spouse. Beyond this, there is no need to compute the exact amount each beneficiary will receive.
- C. The gross estate is reduced in the amount of any federal estate tax payable. As a result, the executor does not have to pay tax on dollars that actually go to the United States.
- D. SB 148 includes comprehensive provisions designed to enhance collection and enforcement.
- E. The tax rate structure in Section 3 of SB 148 can be modified to produce whatever revenue is desired. I suggest a couple of thoughts that may be relevant:
 - (1) Because the federal estate tax will be deductible in determining the Kansas tax, the cost of the Kansas tax to larger estates will be smaller than it might appear to be. For example, if the top federal rate is 45% and the top Kansas rate is 16%, the top combined rate will not be 61% of the estate, but only 54%. (Beginning in 2005 there will be a federal deduction for state death taxes. This will have the effect of further reducing the cost of the Kansas tax.)
 - (2) Legislatures throughout the nation are wrestling with this problem. The federal credit for state death taxes had the benefit of largely preventing competition among the states to attract older residents by providing lower death tax rates. That competition will now be restored. Setting the Kansas rates too high might prove counterproductive in the sense of driving prosperous oldsters to establish formal residence in other states, thereby depriving Kansas of any tax at all.

Although I am a member of the faculty of the School of Law of the University of Kansas, the views above are mine alone, and I do not speak for either the School of Law or the University.

Respectfully submitted,

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K A N S A S

JOAN WAGNON, ACTING SECRETARY

DEPARTMENT OF REVENUE
POLICY AND RESEARCH

KATHLEEN SEBELIUS, GOVERNOR

TESTIMONY REGARDING SENATE BILL 148

Before the Senate Assessment and Taxation Committee
February 13, 2003

Background

Problems with the current estate and succession tax were presented to this Committee on January 14, 2003. At that time, the Committee indicated it was aware of the activities of a working group that was preparing legislation to address those problems, and granted leave for the introduction of this legislation. Senate Bill 148 is the result.

Senate Bill 148

Senate Bill 148 creates a stand-alone Kansas estate tax. It will be replace both the current "pick-up" tax and the succession tax. It is designed to be revenue neutral (although the rates set forth in the Bill must be adjusted to achieve this result). The bill has support from many practitioner groups, and from the Department of Revenue.

The structure of the tax is based on current (December 31, 2002) federal law, but it is independent of federal law. If federal law changes, the major components of the Kansas law will not change. All calculations made in determining the tax (including the size and valuation of the gross estate, deductions, computation of the taxable estate, and calculation of the tax) are made independently under Kansas law.

The bill also addresses two problems with current law:

First, the bill recognizes current federal law with regard to the calculation of the "pick-up" tax (i.e. the federal credit for state death taxes). In other words, the bill recognizes the planned increases in the federal filling threshold (which means few and fewer estates will have to make the computation). And, the bill recognizes the percentage phase-out of the credit (which means the amount of the credit is reduced even for those estates paying it).

Second, the bill repeals the succession tax, retroactively. The succession tax, which was intended to re-impose the inheritance tax on Class C heirs, became effective for estates of decedents dying on or after June 6, 2002. However, many believe the law is fatally flawed and that the best way to address the problem is to repeal the law.

A brief outline of the various sections of the Bill, and their effect, follows:

Section 1 is the citation of the act. The act shall be known and may be cited as the Kansas estate tax act.

Section 2 defines terms used in the act. Among other definitions, this section provides that any reference to the Internal Revenue Code means the provisions of the Internal Revenue Code of 1986, as such code exists on December 31, 2002.

Section 3 provides for the imposition of tax and establishes the rates of tax. No estate tax is imposed unless the taxable estate exceeds \$750,000. Rates start at 2.5% for estates of less than \$1,000,000. The top rate of 11.5% applies to estates in excess of \$10,000,000.

Section 4 provides for the imposition of tax equal to the maximum credit for state death taxes. This is the "pick-up" tax. The section provides that if the estate tax does not equal the amount of the federal credit for state death taxes, and additional tax up to that amount is due.

Section 5 provides that if no estate tax is imposed, an amount equal to the maximum credit for state death taxes will be imposed.

Section 6 provides for the proration of tax. The tax is to be multiplied by a percentage determined by dividing the value of property in Kansas by the value of all the property in the estate.

Section 7 defines the gross estate. It provides that the gross estate shall include the value of all property to the extent provided in sections 8 through 17.

Section 8 provides that all property in which a decedent had an interest is to be included in the gross estate.

Section 9 provides that property transferred by the decedent within one year of the date of death is to be included in the gross estate.

Section 10 provides that property transferred by the decedent in which the decedent retained a life estate is to be included in the gross estate.

Section 11 provides that property transferred by the decedent in which the decedent retained the right to revoke the transfer is to be included in the gross estate.

Section 12 provides that annuities or other payments that are receivable by a beneficiary be reason of the death of the decedent are to be included in the gross estate.

Section 13 provides that property held in joint tenancy with the decedent, or as tenants in entirety between the decedent and spouse, is to be included in the gross estate.

Section 14 provides that property in respect to which the decedent had a general power of appointment is to be included in the gross estate.

Section 15 provides that life insurance proceeds are to be included in the gross estate.

Section 16 provides that transfers made by the decedent for insufficient consideration are to be included in the gross estate.

Section 17 provides that property for which a marital deduction was previously allowed is to be included in the gross estate.

Section 18 defines the taxable estate. It provides that the taxable estate shall be determined by deducting from the gross estate the deductions provided for in sections 19 through 24.

Section 19 provides deductions for funeral expenses, administration expenses, and claims against the estate.

Section 20 provides a deduction for casualty losses.

Section 21 provides a deduction for property that is specifically exempt by state or federal law.

Section 22 provides a deduction for estate taxes paid to the federal government.

Section 23 provides a deduction for transfers for public, charitable, and religious uses.

Section 24 provides a deduction for transfers to a surviving spouse.

Section 25 provides that certain deductions made in computing the taxable estate are not allowed as deductions for Kansas income tax purposes.

Section 26 defines who has responsibility for filing the estate tax return.

Section 27 provides that the time for filing the return shall be within 9 months of the decedent's death.

Section 28 provides for extensions of time to file the return when good cause exists, and that tax remains due and payable by the due date.

Section 29 provides all returns shall be filed with the Director of Taxation.

Section 30 provides for signatures on the return, and that the return is filed under penalty of perjury.

Section 31 provides for filing of the return by disclosure of information.

Section 32 provides rules for the treatment of fractional dollar amounts shown on the return.

Section 33 provides for the preservation and confidentiality of the return, and that performance of certain activities by administrative personnel are unlawful and subject to penalty.

Section 34 provides that the estate tax shall be paid by the personal representative.

Section 35 provides that the tax shall be paid within 9 months of the date of death of the decedent.

Section 36 provides for the imposition of penalty and interest if the tax is not paid in a timely fashion.

Section 37 provides the duties of the Director of Taxation include the examination of returns, the refund of excess tax paid, the assessment of additional tax, and the conducting of informal conferences.

Section 38 provides for the issuance of jeopardy assessments by the Director of Taxation, and for review of those assessments.

Section 39 provides for the personal representative's request for a determination of tax and discharge from liability.

Section 40 provides for a tax lien to aid in the enforcement and collection of tax.

Section 41 provides the filing of notice of the tax lien.

Section 42 provides for the issuance of tax warrants.

Section 43 provides for actions for collection by the Director of Taxation.

Section 44 provides for the release of the lien imposed by Section 40.

Section 45 provides for the issuance of proof and notice of release of the lien.

Section 46 provides for the issuance of a closing letter.

Section 47 provides for the disposition of revenue to the state general fund.

Section 48 creates the estate tax abatement fund and provides for the payment of abatements and refunds of interest.

Section 49 provides for the imposition of fees for services, and for the disposition of proceeds to the state general fund.

Section 50 creates a statute of limitations, and requires the personal representative notify the Director of Taxation of adjustments by the internal revenue service.

Section 51 provides the Secretary of Revenue shall adopt rules and regulations necessary to carry out the purposes of the act.

Section 52 provides the act shall apply to the estates of all decedents dying after December 31, 2002, and that prior acts (other than the succession tax act) shall apply to deaths occurring prior to that date.

Section 53 provides a severability clause.

Section 54 provides for the retroactive repeal of the succession tax, and establishes a procedure for the claiming of refunds.

Section 55 repeals the existing estate and succession tax statutes.

Section 56 provides that the act shall be effective and in force upon publication in the statute book (July 1).

It is suggested that the rate schedule in Senate Bill 148, as introduced, be amended as set forth below, in order to obtain fiscal neutrality in FY 04 (i.e., replace the revenue expected in FY 03 and FY04 from the Kansas succession tax, if it is retroactively repealed by Senate Bill 148, and replace the revenue expected in FY 04 from the existing Kansas estate tax under current law):

Sec. 3. (a) A tax is hereby imposed on the taxable estate of every resident decedent, and every nonresident decedent who owned real, personal or intangible property with a tax situs in Kansas.

(b) The tax imposed by this section shall be computed in accordance with the following schedule:

If the taxable estate is:	The tax is:
Not over \$750,000	Zero
Over \$750,000 but not over \$1,000,000	3.25% of excess over \$750,000
Over \$1,000,000 but not over \$5,000,000	\$8,125 plus 13% of excess over \$1,000,000
Over \$5,000,000 but not over \$10,000,000	\$528,124 plus 17% of excess over \$5,000,000
Over \$10,000,000	\$1,403,125 plus 21% of excess over \$10,000,000

It is further recommended that Section 54 of Senate Bill 148, as introduced, be amended to provide that any refunds of previously paid Kansas succession tax shall be paid without interest.

Estate Tax Filing Thresholds

Current Kansas Estate Tax Filing Thresholds:

2003: \$700,000

2004: \$850,000

2005: \$950,000

2006 and thereafter: \$1 million

Federal Estate Tax Filing Thresholds:

2003: \$1 million

2004: \$1.5 million

2005: \$1.5 million

2006-08: \$2 million

2009: \$3.5 million

2010: repeal, which sunsets in 2011, reverting to Federal Estate Tax law prior to 2001

Proposed Filing Threshold for Stand-alone Kansas Estate Tax in Senate Bill 148:

All years: \$750,000

Year 2003 – Comparison of Adjusted Kansas Estate Tax Rates

<u>Taxable Estate</u>	If Kansas Conformed to Federal (Federal Pick-Up Tax)	Current Law (State Pick-Up Tax)	Proposed Revenue Neutral Rates (State Estate Tax)
\$700,000	\$0	\$0	\$0
\$1,000,000	\$0	\$33,200	\$8,125
\$1,500,000	\$32,200	\$64,400	\$73,125
\$2,000,000	\$49,800	\$99,600	\$138,125
\$3,500,000	\$114,600	\$229,200	\$333,125
\$5,000,000	\$195,800	\$391,600	\$528,124
\$7,500,000	\$352,600	\$705,200	\$953,124
\$10,000,000	\$533,800	\$1,067,600	\$1,403,125

Note: Federal Estate Tax Filing Threshold for 2003 is \$1,000,000

Year 2004 – Comparison of Adjusted Kansas Estate Tax Rates

<u>Taxable Estate</u>	If Kansas Conformed to Federal (Federal Pick-Up Tax)	Current Law (State Pick-Up Tax)	Proposed Revenue Neutral Rates (State Estate Tax)
\$700,000	\$0	\$0	\$0
\$1,000,000	\$0	\$33,200	\$8,125
1,500,000	\$16,100	\$64,400	\$73,125
2,000,000	\$24,900	\$99,600	\$138,125
3,500,000	\$57,300	\$229,200	\$333,125
\$5,000,000	\$97,900	\$391,600	\$528,124
\$7,500,000	\$176,300	\$705,200	\$953,124
\$10,000,000	\$266,900	\$1,067,600	\$1,403,125

SB 148

Note: Federal Estate Tax Filing Threshold for 2004 is \$1,500,000

Year 2005 – Comparison of Adjusted Kansas Estate Tax Rates

<u>Taxable Estate</u>	If Kansas Conformed to Federal (Federal Pick-Up Tax)	Current Law (State Pick-Up Tax)	Proposed Revenue Neutral Rates (State Estate Tax)
\$700,000	\$0	\$0	\$0
\$1,000,000	\$0	\$19,500	\$8,125
1,500,000	\$0	\$64,400	\$73,125
2,000,000	\$0	\$99,600	\$138,125
3,500,000	\$0	\$229,200	\$333,125
\$5,000,000	\$0	\$391,600	\$528,124
\$7,500,000	\$0	\$705,200	\$953,124
\$10,000,000	\$0	\$1,067,600	\$1,403,125

Note: Federal Estate Tax Filing Threshold for 2005 is \$1,500,000

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Year 2006 – Comparison of Adjusted Kansas Estate Tax Rates

<u>Taxable Estate</u>	<u>If Kansas Conformed to Federal (Federal Pick-Up Tax)</u>	<u>Current Law (State Pick-Up Tax)</u>	<u>Proposed Revenue Neutral Rates (State Estate Tax)</u>
\$700,000	\$0	\$0	\$0
\$1,000,000	\$0	\$0	\$8,125
1,500,000	\$0	\$64,400	\$73,125
2,000,000	\$0	\$99,600	\$138,125
3,500,000	\$0	\$229,200	\$333,125
\$5,000,000	\$0	\$391,600	\$528,124
\$7,500,000	\$0	\$705,200	\$953,124
\$10,000,000	\$0	\$1,067,600	\$1,403,125

Note: Federal Estate Tax Filing Threshold for 2006 is \$2,000,000, increasing to \$3,500,000 in 2009. The Federal Estate Tax is repealed effective 2010, but the repeal sunsets in 2011, and the Federal Estate Tax Law effective prior to 2001 would go back into effect (\$1,000,000 Federal Estate Tax Filing Threshold).

Fiscal Estimate—Kansas Estate Tax

	Current Kansas Estate Tax							
	FY03	FY04	FY 05	FY06	FY07	FY08	FY09	FY10
Estimated Revenue (\$millions):	50	50	50	50	50	50	50	50

	Current Kansas Succession Tax							
	FY03	FY04	FY 05	FY06	FY07	FY08	FY09	FY10
Estimated Revenue (\$millions):	5	10	10	10	10	10	10	10
Total	55	60	60	60	60	60	60	60

Senate Bill 148 Proposed Stand-alone Kansas Estate Tax (at rates in introduced bill) and
Retroactive Repeal of Succession Tax

Estimated Revenue (\$millions):	25	25.8	26.5	27.3	28.1	29	29.9
Difference from Current Law:	(40)	(34.2)	(33.5)	(32.7)	(31.9)	(31)	(30.1)

Senate Bill 148 Proposed Stand-alone Kansas Estate Tax (at FY04 revenue neutral rates) and
Retroactive Repeal of Succession Tax

Estimated Revenue (\$millions):	65	66.9	69	71	73.2	75.3	77.6
Difference from Current Law:	0	6.9	9	11	13.2	15.3	17.6



Kansas Society of Certified Public Accountants

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February 13, 2002

Senator Corbin, members of the Senate Assessment and Taxation Committee:

On behalf of the 2,600-member Kansas Society of Certified Public Accountants, I want to thank you for the opportunity to appear before you today in support of SB 148, the Kansas Estate Tax Act.

I am T.C. Anderson, Executive Director of the Kansas Society.

At the request of the drafters of this proposed legislation, the KSCPA appointed a task force to review and comment on it. Following that review, a recommendation was forthcoming that the Kansas Society adopt as a part of its legislative platform for 2003 support of the Kansas Estate Tax Act.

Thank you. I'd be happy to stand for questions.

*Senate Assessment + Taxation
2-13-03
Attachment 4*



Since 1894

Testimony

To: Senate Committee on Assessment and Taxation

From: Allie Devine, Vice President and General Counsel

Re: Senate Bill 94 and Senate Bill 148

Good morning. My name is Allie Devine. I am representing the Kansas Livestock Association (KLA). KLA is a trade organization that represents all segments of the livestock industry and has over 6,000 members.

We appreciate the opportunity to comment on both of these bills. Before addressing the specifics of these bills please let me provide a context for our positions. At the federal level, the National Cattlemen's Beef Association (NCBA) has been a leader in organizing the efforts of small businesses to repeal the federal death tax. One year ago at the NCBA convention President Bush stood before a crowd of 5,000 ranchers, tipped his cowboy hat and called for the permanent repeal of death taxes. The crowd was ecstatic.

For over 20 years, KLA has supported the repeal of death taxes because there is nothing more sacred to our members than the land they leave for their heirs. To quote President Bush, "the repeal of death taxes will allow families to pass our assets on from one generation to the next."

Death taxes are often one of the reasons, ranches and farming operations split. Death, unlike other taxable events such as the sale of a product, produces no revenue. This is why it becomes a burden on the heirs. The heirs must generate the revenue to pay the tax. At a time when we are searching for ways to maintain our farms and ranches, and encourage young farmers and ranchers, we cannot afford to undercut them with this type of tax policy. Ranching and farming are capital intensive. It takes many years to accumulate a sustainable size operation. Our members want to preserve and pass their work onto their families. We view death taxes as an obstacle to the survival of ranching and farming operations, small businesses and the preservation of a family legacy.

We are philosophically opposed to the implementation of a state estate tax like what is proposed in SB 148. While the federal government is moving away from estate taxes, this bill resurrects them in Kansas. We understand the budget situation. We don't think it can or should be solved with estate taxes. An estate tax is a deterrent to the continuation of businesses that the state needs to generate revenues. What social policy is being furthered by such a tax? Our members view estate taxes as a road to rural decline not development.

*Senate Assessment & Taxation
2-13-03*

We understand that this bill seeks to address administrative problems with the current Kansas law tied to the federal law at a point in time. We appreciate the information the Department of Revenue has provided to explain this complicated issue. However, we are not convinced that a freestanding estate tax will decrease the complications. There will be costs to the state to implement these provisions. There will be larger costs and burdens to taxpayers as they plan and rework their estates.

We ask that you think carefully and act very slowly in this area. Philosophically we are opposed to estate taxes. Practically, we know they will be considered as the state tries to address its budget concerns. We are asking you to take the time to develop good information on these issues before you proceed. A side by side comparison, outlining short and long term provisions, of current state law, SB 148, and current federal law is needed so that we can discuss in detail the effects of this proposal. We will be discussing this in detail with agricultural estate planners and our members next week.

Regarding SB 94, we understand that the succession tax was designed to capture revenue from Class C heirs. While these heirs may be distant, they may be the only parties interested in continuing the ranching or farming operation. Philosophically we support SB 94, because we want to assure that no one is precluded from continuing the family, extended or otherwise, business operation.

Thank you for your time. We are committed to working with you on this important issue.

LEGISLATIVE TESTIMONY



The Unified Voice of Business

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SB 94 and SB 148

February 13, 2003

KANSAS CHAMBER OF COMMERCE AND INDUSTRY

Testimony before the Senate Assessment and Taxation Committee

By Marlee Carpenter, Director of Taxation and Small Business

Chairman Corbin and members of the Committee:

I am Marlee Carpenter with the Kansas Chamber of Commerce and Industry testifying on both bills today. KCCI is in favor of SB 94. We have had a long-standing policy to repeal all death taxes. Last session the "class C" inheritance tax was reinstated on "class C heirs", nieces, nephews, charities, etc. KCCI did not support this re-imposition. KCCI supports SB 94, which would abolish the inheritance tax that was re-imposed last session.

KCCI also supports the reduction in the rate schedule listed in SB 148. A family-owned business stands to lose 55% of all its assets when it passes from one generation to the next. KCCI supported the pick-up estate tax changes made in the late 1990's. SB 148 creates a stand-alone Kansas estate tax and will replace both the current "pick-up" tax and the succession tax. We have policy that encourages Kansas to repeal that state estate tax and conform with the federal phase out. SB 148 would reduce the top rate from 16% to 11.5% and reduces the estate tax burden in the state. KCCI supports this rate reduction. However, we are concerned whether this bill meets the intent of the drafter. We hope these issues can be addressed while maintaining a reduced rate reduction.

Senate Assessment & Taxation
2-13-02
Attachment 6

KCCI supports the repeal of the succession tax in SB 94 and rate reduction in SB 148. KCCI believes that in order to keep Kansas competitive, the inheritance tax needs to be repealed and the estate tax rate should be phased down or eliminated all together. Thank you for your time and I will be happy to answer any questions.

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.



Kansas Farm Bureau

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PUBLIC POLICY STATEMENT

SENATE COMMITTEE ON ASSESSMENT & TAXATION

**Re: SB 94 -- repealing the succession tax
and
SB 148 – modifying the estate tax**

**February 13, 2003
Topeka, Kansas**

**Presented by:
Leslie J. Kaufman, State Director
KFB Governmental Relations**

Chairman Corbin and members of the Committee, thank you for the opportunity to present comments regarding the succession and estate taxes. I am Leslie Kaufman, the State Director of Governmental Relations for Kansas Farm Bureau (KFB). As I am sure you are aware, KFB is the state's largest general farm organization. We represent agricultural producers through the 105 county Farm Bureau Associations across Kansas.

Farm Bureau policy, on both the state and national levels, has long opposed any form of "death tax". We are supportive of repealing the succession tax, from a policy perspective, but also know that, as a practical matter, repeal also serves to eliminate a now confusing area of tax law.

As we have said, we philosophically oppose the estate tax, but realize from an estate planning perspective that there could be ways to improve our state process. We still have many questions regarding SB 148:

- How will it actually function;
- How does it compare to the current Kansas estate tax;
- How does it interplay with the federal estate tax, now and as the federal tax changes over the next few years; and
- How will it impact our members?

Without answers to these questions, we are unable to determine, at this time, if our members benefit overall with these changes as compared to the current law. We will continue to study the issue and look forward to further dialog. Thank you.

Senate Assessment & Taxation
2-13-02
Attachment 7

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Senator Derek Schmidt
15th District

Committee Assignments
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During Session

**Testimony in Support of Senate Bill 94
Repealing the Kansas Inheritance Tax
By Senator Derek Schmidt
February 13, 2003**

Mr. Chairman, thank you for allowing me to testify in support of Senate Bill 94, which would repeal the Kansas Inheritance Tax that was re-enacted last year and would refund any tax paid to date.

These are reasons we should repeal this tax now before it causes any more harm:

- This tax is not significantly helping to balance the state budget. The whole purpose of enacting this tax last year was to help the state balance its budget. At the time, we were told that this new tax would generate \$15 million per year for state coffers. Now, the Department of Revenue has lowered that estimate for this year to \$5 million, and it is my understanding that to date the new tax has generated only about \$1 million for the state.
- This tax constitutes triple taxation by the State of Kansas. Yes, triple taxation. Imagine an estate valued at more than \$1 million which is left to Class C heirs. The money was taxed once by the State of Kansas during the decedent's lifetime when it was earned (income tax). It is then taxed twice upon death – that portion of the estate exceeding \$700,000 is subject to the Kansas Estate Tax and the entire estate is subject to the Kansas Inheritance Tax. This is absurd.
- This tax is unfair on its face. What is the public policy rationale for taxing an estate left to a loving and helpful niece, nephew, or neighbor who lives in town but not taxing the same estate if it is left to an estranged son or daughter who lives in, say, California? There is none.

*Senate Assessment + Taxation
2-13-03
Attachment 8*

- This tax is exceptionally confusing. Despite honest efforts by the Department of Revenue to paint this ugly pig as a cuddly puppy, it is still an ugly pig. For example, I heard from two attorneys in my district in the past week who remain under the impression that the new tax applies to estates left to charities, including churches. Although the Department of Revenue has attempted to clarify that charities are not Class C heirs within the meaning of this new law, significant confusion remains – even among professionals in the field.
- This tax is a tax on honesty. In tax-assistance circles, the new Inheritance Tax is collected only haphazardly at best. The truth is, if you are a person subject to paying the tax, and if both you and your tax advisor are honest to a fault, you will pay. But if any person involved is less than fully forthcoming, this tax is readily avoided. There is no enforcement mechanism.

Mr. Chairman, this tax was bad public policy when it was enacted last year, and it has proven to be worse public policy in practice. “Fixing” the mechanics of this tax will not remedy its fundamental flaws. On behalf of the sponsors of Senate Bill 94 and on behalf of the citizens I represent, I urge this committee to advance this legislation. We should abolish this tax before it does any more harm. We should do so retroactively by refunding any taxes paid to be fair to those who were so unfortunate as to have been caught in this nightmare.

Thank you for your time, and I would be glad to stand for questions.

MEMORANDUM

February 10, 2003

To: Various Legislators
From: Chris W. Courtwright
Re: Fiscal Impact of Various Death Tax Provisions

This memo responds to a number of questions which have come up with regard to various proposals to amend the Kansas succession and estate taxes.

Repeal of Succession Tax

The Department of Revenue now believes that the succession tax which was imposed by 2002 legislation is expected to raise \$5 million in FY 2003 and \$10 million in FY 2004. (At the time the legislation was adopted, expectations were that the tax would raise \$15 million annually.) By way of reference, consider that the March 2002 Consensus estimate for FY 2003 receipts was \$49 million. With the addition of the succession tax, the total death tax estimate was increased at the conclusion of the 2002 session to \$64 million. When the Consensus group reconvened in the fall and received the revised estimates from the Department of Revenue, the FY 2003 estimate was reduced to its current \$55 million; and the first FY 2004 estimate was set at \$60 million.

Thus, a prospective repeal of the tax would reduce FY 2004 receipts by \$10 million; and a retroactive repeal to the date of the tax's imposition would reduce receipts by \$15 million.

Full Conformity to Federal Law

The Department also estimates that full conformity to the new federal estate tax law - including that portion that wipes out state death tax credits by 2005 - would reduce receipts by an additional \$25 million in FY 2004; by \$39.4 million in FY 2005; and by \$55.1 million in FY 2006.

Partial Conformity to Federal Law

Conforming to the new federal law with respect to the exemption thresholds and other provisions effective for estates of decedents dying on and after January 1, 2003, (but NOT to that part of the federal law wiping out the state death tax credits) would reduce receipts by \$2.8 million in FY 2004; \$6.9 million in FY 2005; and \$9.0 million in FY 2006.

The following table compares the exemption thresholds under current Kansas law (which is tied to the federal law in effect on December 31, 1997) and the 2001 federal law:

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	<u>Kansas Exemption Amount</u> <u>(1997 federal law)</u>	<u>New Federal</u> <u>Exemption Amount</u>
2002	\$700,000	\$1,000,000
2003	\$700,000	\$1,000,000
2004	\$850,000	\$1,500,000
2005	\$950,000	\$1,500,000
2006	\$1,000,000	\$2,000,000
2007	\$1,000,000	\$2,000,000
2008	\$1,000,000	\$2,000,000
2009	\$1,000,000	\$3,500,000
2010	\$1,000,000	tax repealed
2011	\$1,000,000	\$1,000,000

MEMORANDUM

January 29, 2003

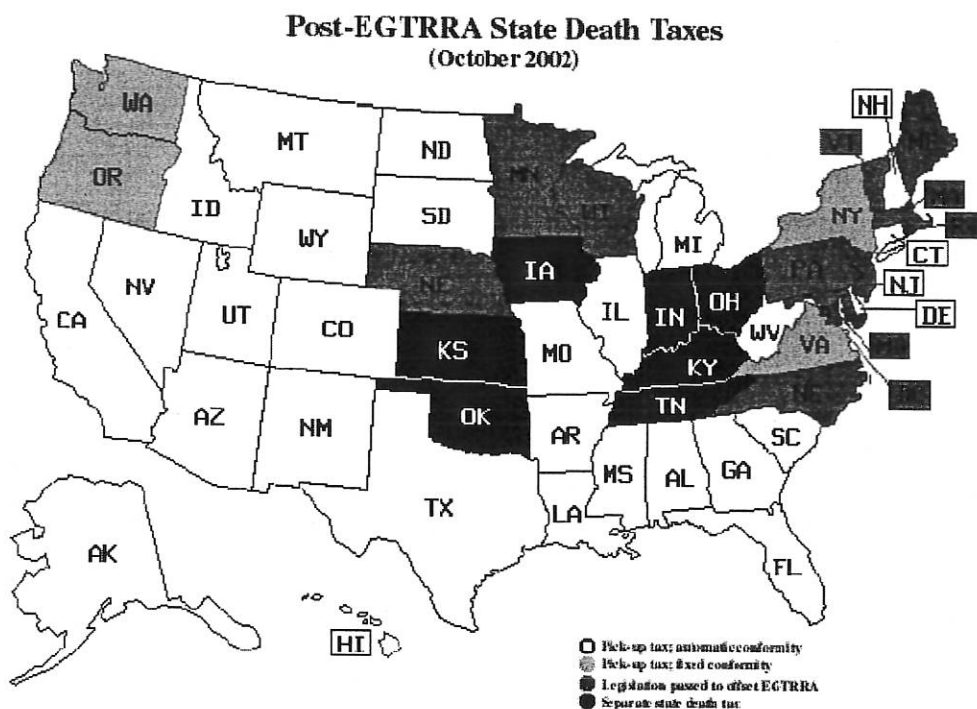
To: Rep. John Edmonds, Rep. Bruce Larkin
From: Chris W. Courtwright
Re: State Estate Tax Provisions

Attached you will find a report on the extent to which the 50 states conform to the estate tax provisions of the new federal law (EGTRRA of 2001). As you know, some states conformed prospectively to those provisions; others, like Kansas, did not conform prospectively; and others have stand-alone estate, inheritance, or succession taxes.

*Senate Assessment & Taxation
2-13-03
Attachment 10*

State Responses to Estate Tax Changes Enacted as Part of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA)

[\[more detail\]](#) [\[summary table\]](#)



B-23/02
October 24, 2002

State Responses to Estate Tax Changes Enacted as Part of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA)

Summary

The Economic Growth and Tax Relief Reconciliation Act of 2001 phases out the state death tax credit allowed against the federal estate tax in 25 percent increments between 2002 and 2005. This bulletin presents the results of a survey regarding legislative action taken in 2002 to offset the impact of EGTRRA on state death taxes. The survey findings are: (1) Prior to EGTRRA, 38 states relied on solely on a pick-up estate tax, i.e., a state estate tax equal to the maximum state death tax credit allowed under federal law. In all but four states the conformity to the federal code was on an automatic or rolling basis. (2) The other 13 states had a free-standing state death tax, but incorporated the state death tax credit as either a minimum tax or supplemental tax; (3) Twelve states took legislative action to offset some or all of the revenue impact of EGTRRA; (4) Under current state law, there will be 30 states

that have no state death tax in 2005, when the federal law phases-out fully the state death tax credit; (5) The state revenue impact of the phase-out of the death tax credit exceeds \$4.0 billion annually. Survey results are discussed further below and presented in the attached table.

Background

1. The Economic Growth and Tax Relief Reconciliation Act (EGTRRA) repeals the federal estate tax effective in 2010. Between 2002 and 2010, EGTRRA also reduces the estate tax rates somewhat and increases the exemption level for the tax. In addition, EGTRRA provides that the amount of state death tax credit that may be taken against the federal estate tax is reduced by 25 percent for deaths occurring in 2002, 50 percent for deaths in 2003, 75 percent for deaths in 2004 and by 100 percent for deaths occurring in 2005 and thereafter. Beginning in 2005, a deduction is allowed for state death taxes paid in computing the taxable estate for federal purposes.
2. The state death tax credit had been a permanent feature of the federal estate tax since it was enacted in 1926. When enacted, it was intended to reduce federal revenues and to place a floor under state death taxes to reduce interstate tax competition. The rates of the credit (maximum of 16 percent) have been unchanged since 1926 when they were set at an amount equal to 80 percent of the federal tax rates.
3. The effect of the death tax credit phase-out, of course, is to reduce state revenues in cases where the state death tax is tied on an automatic basis to the federal death tax credit and there is no countervailing legislative action taken. This is true regardless of whether the state relies on the pick-up tax as its only death tax or as a supplemental tax (in which case the entire tax will phase-out) or uses the pick-up tax as a minimum tax (in which case, the state will lose revenue in those cases where the death tax credit available exceeded the tax under the state stand-alone tax).
4. The effect of the phase-out was also to transfer revenue from states to the federal government during the period of the phase-out, thus allowing greater federal tax reductions than would otherwise have been possible.

Pre-EGTRRA State Death Taxes

5. Since its enactment in 1926, all states and the District of Columbia have taken steps to coordinate their state death taxes in some fashion with the state death tax credit. Prior to the enactment of EGTRRA in 2001, 37 states and D.C. relied solely on a "pick-up tax" in which the state death tax was simply an amount equal to the maximum amount of state death tax credit allowed under federal law. In five states (New York, North Carolina, Oregon, Virginia and Washington), the state pick-up tax was tied to the federal estate tax as of a particular date prior to the enactment of EGTRRA. In the remaining cases, the state pick-up tax was tied to the federal code on an automatic or rolling basis, meaning that the pick-up tax would phase-out in these states unless the state enacted legislation to the contrary.
6. The remaining 13 states -- Connecticut, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maryland, New Hampshire, New Jersey, Ohio, Oklahoma, Pennsylvania and Tennessee -- also coordinated their death taxes (a stand-alone inheritance or estate tax) with the state death tax credit. In these states, the state death tax credit acted as a minimum tax for the stand-alone tax (i.e., the estate was liable for the greater of the death tax credit or the separately computed state tax) or as a supplemental state death tax (i.e., an amount equal to the allowable death tax credit was owed in addition to a state-computed liability). Of

10-3

these thirteen states, all except Kansas were tied to the federal code on an automatic or rolling basis prior to the enactment of EGTRRA. In addition, Ohio takes the position that its incorporation of the state death tax credit into its estate tax is not affected by the passage of EGTRRA.

Post-EGTRRA Legislative Action

7. Since the enactment of EGTRRA, 12 states have taken legislative action to offset all or a part of the impact of the death tax credit phase-out. This includes nine states (D.C., Maine, Massachusetts, Minnesota, Nebraska, North Carolina, Rhode Island, Vermont and Wisconsin) that took legislative action to preserve their pick-up tax. In addition, Maryland, New Jersey and Pennsylvania enacted legislation to tie their use of the death tax credit as a supplemental or minimum tax to the death tax credit as it existed prior to the passage of EGTRRA.

8. In most cases, the legislative change was accomplished simply by conforming the state law references to the state death tax credit to the federal law at some point prior to the passage of EGTRRA. There were three exceptions:

- Nebraska enacted a free standing estate tax tied to the federal definitions of the estate tax base, a \$1 million exemption and a rate schedule identical to that of the state death tax credit.
- Vermont tied its law to the death tax credit as it existed as of 1/1/2001, but adopted the other estate tax provisions of EGTRRA, including the increased exemptions.
- North Carolina updated their reference date to conform to the federal estate tax (including increased exemptions) as of May 7, 2001, but provided (for deaths occurring prior to January 1, 2004) that the amount of the state pick-up tax is to be computed without regard to the phase-out of the credit contained in federal law.

9. In Oregon where the pick-up tax is tied to the federal code as April 28, 1997, the legislature passed a law that would adopt the federal exemption amounts for 2002-2004, but phase out the pick-up tax in 2005. Governor Kitzhaber has not yet signed or vetoed this legislation. Similarly, New Hampshire repealed its separate inheritance tax effective in 2003.

10. If there is no further state legislative action between now and 2005 (when the federal allowance of a state death tax credit is terminated), there will be at that time 10 states with a straight pick-up tax:

D.C.	Massachusetts	Minnesota
Nebraska	New York	Rhode Island
Vermont	Virginia	Washington
Wisconsin		

There will be five states -- Kansas, Maryland, New Jersey, Ohio and Pennsylvania -- that have a stand-alone state death tax that incorporates the death tax credit (with a fixed conformity date) as a minimum tax or a supplemental tax. There will also be 6 other states -- Connecticut, Indiana, Iowa, Kentucky, Oklahoma and Tennessee -- that have a stand-alone state death tax that does not include any reference to the state death tax credit, although the Connecticut succession tax will be repealed fully in 2006.

The remaining 30 states will have no death tax in place at that time (including Louisiana where a separate state death tax is scheduled to expire in 2004, Maine and North Carolina where the decoupling legislation is effective only for deaths occurring prior to 2003 and

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2004, respectively, New Hampshire which repealed its separate inheritance tax effective for deaths occurring in 2003, and Oregon unless the governor vetoes a measure passed in 2002 that will phase-out the pick-up tax in 2005.)

Revenue Effects

11. When enacted, it was estimated that the phase-out of the death tax credit could reduce state revenues by \$19-\$23 billion between FY 2003 and 2007, unless states took contrary state legislative action. In FY 2001, state death taxes of all types amounted to \$7.5 billion. Equally as frustrating to states as the revenue loss was the fact that it came with no consultation and at a time when state (and federal) revenues were beginning to show the effects of a slowing economy.

12. The FTA survey of states indicates that states that do not tie their relationship to the state death tax credit as of a fixed date will see their revenues reduced by about \$4.2 billion on an annual basis in FY 2007 when the effects of the phase-out should be fully reflected. In addition, it is likely that the state legislative actions noted above have offset an additional \$0.5 billion in revenue reductions. The FY 2004 (next budget cycle) costs of the EGTRRA phase-out will be roughly \$2.1 billion. The FY 2003-2007 costs will total about \$13-\$14 billion.

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State Death Taxes After the Passage of The Economic Growth and Tax Relief Reconciliation Act of 2001

State	Type of Tax/ Relationship to Federal Credit	State Law Change Passed	Fiscal Impact (\$ Millions)		
			FY 2003	FY 2004	FY 2007
Alabama	Pick-up/Auto	No	-\$20.0	-\$33.0	-\$48.0
Alaska	Pick-up/Auto	No	-\$0.3	-\$1.0	-\$3.0
Arizona	Pick-up/Auto	No	-\$18.8	-\$38.1	-\$73.0
Arkansas	Pick-up/Auto	No	-\$4.7	-\$10.9	-\$25.0
California	Pick-up/Auto	No	-\$386.5	-\$762.2	-\$1,300.0
Colorado	Pick-up/Auto	No	-\$14.3	-\$35.7	-\$73.7
Connecticut	Stand-alone/Auto*	No	NA	NA	NA
Delaware	Pick-up/Auto	No	-\$7.6	-\$16.3	-\$34.7
District of Columbia	Pick-up/Fixed*	Yes	-	-	-
Florida	Pick-up/Auto	No	-\$153.2	-\$361.6	-\$930.3
Georgia	Pick-up/Auto	No	-\$24.0	-\$56.0	-\$129.0
Hawaii	Pick-up/Auto	No	-\$9.0	-\$14.1	-\$24.2
Idaho	Pick-up/Auto	No	-\$2.0	-\$2.0	-\$2.0
Illinois	Pick-up/Auto	No	-\$150.0	-\$250.0	-\$400.0
Indiana	Stand-alone/Auto	No	-\$7.4	-\$17.6	-\$21.4
Iowa	Stand-alone/Auto	No	-\$15.2	-\$26.1	-\$45.6
Kansas	Stand-alone/Fixed*	No	-	-	-

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Kentucky	Stand-alone/Auto	No	-\$11.3	-\$23.4	-\$55.8
Louisiana	Stand-alone/Auto*	No	-\$5.4	-\$11.5	-\$24.0
Maine	Pick-up/Auto*	Yes*	-\$3.6	-\$16.2	-\$32.3
Maryland	Stand-alone/Fixed*	Yes	-	-	-
Massachusetts	Pick-up/Fixed*	Yes	-	-	-
Michigan	Pick-up/Auto	No	-\$67.0	-\$99.6	-\$155.0
Minnesota	Pick-up/Fixed*	Yes	-	-	-
Mississippi	Pick-up/Auto	No	-\$13.0	-\$20.0	-\$30.0
Missouri	Pick-up/Auto	No	-\$30.0	-\$72.0	-\$182.0
Montana	Pick-up/Auto	No	-\$0.9	-\$2.7	-\$3.9
Nebraska	Pick-up/Fixed*	Yes*	-	-	-
Nevada	Pick-up/Auto	No	-\$14.0	-\$23.0	-\$39.0
New Hampshire	Stand-alone/Auto*	No	-\$7.0	-\$9.4	-\$31.0
New Jersey	Stand-alone/Fixed*	Yes	-	-	-
New Mexico	Pick-up/Auto	No	-\$7.5	-\$12.0	-\$20.0
New York	Pick-up/Fixed*	No	-	-	-
North Carolina	Pick-up/Fixed*	Yes*	-	-	-\$129.0
North Dakota	Pick-up/Auto	No	-\$0.2	-\$1.5	-\$5.5
Ohio	Stand-alone*	No	-	-	-
Oklahoma	Stand-alone/Auto	No	-\$4.6	-\$10.3	-\$11.5
Oregon	Pick-up/Fixed*	No	-	-	-\$46.0
Pennsylvania	Stand-alone/Fixed*	Yes	-	-	-
Rhode Island	Pick-up/Fixed*	Yes	-	-	-
South Carolina	Pick-up/Auto	No	-\$12.0	-\$24.0	-\$48.0
South Dakota	Pick-up/Auto	No	NA	NA	NA
Tennessee	Stand-alone/Auto	No	-\$4.5	-\$8.3	-\$16.6
Texas	Pick-up/Auto	No	-\$81.0	-\$159.0	-\$253.0
Utah	Pick-up/Auto	No	-\$3.0	-\$8.0	-\$16.0
Vermont	Pick-up/Fixed*	Yes*	-	-	-
Virginia	Pick-up/Fixed*	No	-	-	-
Washington	Pick-up/Fixed*	No	-	-	-
West Virginia	Pick-up/Auto	No	-\$5.0	-\$9.0	-\$16.0
Wisconsin	Pick-up/Fixed*	Yes*	-\$29.0	-	-
Wyoming	Pick-up/Auto	No	-\$5.1	-\$7.7	-\$10.3
Total			-\$1,117.1	-\$2,142.2	-\$4,234.8

Definitions:

Pick-up: State has death tax equal to the state death tax credit provided for under federal estate tax.

Stand-alone: State has a free-standing death tax (inheritance or estate) and uses the death tax credit provided for under federal law as either a minimum tax or a supplemental additional tax to the state law tax.

Auto: State conforms to the provisions of the state death tax credit on an automatic or rolling basis.

Fixed: State conforms to the provisions of the state death tax credit as of a fixed date prior to the enactment of EGTRRA.

Notes:

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- Connecticut Connecticut had earlier passed legislation to repeal its separate succession tax and move solely to a pick-up tax in 2006. No legislative changes were made in 2002; the pick-up tax will expire for deaths occurring after 1/1/2005.
- D.C. D.C. passed legislation in July 2002 to provide that the pick-up tax will be equal to the amount computed under the state death tax credit as it existed on January 1, 2001.
- Kansas Kansas has an estate tax and a succession tax; they are separate taxes that are not alternative minimums. The estate tax is equal to the state death tax credit allowed under federal law as of 12/31/1997 without regard to the EGTRRA phase-out.
- Louisiana Under prior state law, Louisiana was transitioning to a pure pick-up tax. The state inheritance tax will expire for deaths occurring after June 30, 2004; the pick-up tax will expire for deaths after 12/31/2004. The revenue impacts reflect only the phase-out of the pick-up tax.
- Maine For deaths occurring in 2002, the Maine tax is equal to the state death tax credit allowed as of 12/31/2001. In subsequent years, the Maine tax is equal to the credit allowed under federal law; it will phase-out barring further legislation.
- Maryland Maryland passed legislation in 2002 to tie the pick-up tax to the state death tax credit as it existed prior to 1/1/2001. Maryland also imposes an inheritance tax on non-lineal heirs.
- Massachusetts Massachusetts passed legislation in 2002 providing that the state tax is the credit computed under the federal law as of December 31, 2000. The new law is unclear on the treatment of the new federal exemption levels. Corrective legislation is under consideration.
- Minnesota Minnesota law provides that the state pick-up tax is tied to the federal estate tax as of 12/31/2000. Legislation passed in 2002 to clarify this intent.
- Nebraska Nebraska converted its pick-up tax to a separate estate tax with a rate schedule identical to the rate schedule of the state death tax credit as it existed on 12/31/2001. The rate applies to the adjusted estate minus \$1 million.
- New Hampshire New Hampshire also imposes an 18 percent inheritance tax on non-lineal heirs. Legislation was passed in 2002 to repeal the inheritance tax for deaths occurring after January 1, 2003. Revenue impacts are for the pick-up tax only.
- New Jersey New Jersey has both an inheritance tax and an estate tax. Legislation passed in 2002 provides that the estate tax is equal to the credit allowed as of 12/31/01.
- New York The New York estate tax is tied to the federal estate tax and death tax credit as in effect in July 1998.
- North Carolina Legislation passed in 2002 ties the state pick-up tax to the federal code as of May 7, 2002 except that the amount of the state pick-up tax is to be computed without regard to the phase-out of the death tax credit. For deaths occurring on or after 1/1/2004, however, the state pick-up tax will be equal to the state death tax credit allowed under federal law as of the date of death.
- Ohio Ohio has a stand-alone estate tax. Where the state death tax credit exceeds the Ohio liability, the amount of the death tax credit is owed; Ohio takes the position that this provision is not affected by the phase-out contained in EGTRRA.
- Oregon The Oregon pick-up tax is tied to the federal estate tax as of April 28, 1997. Legislation passed in 2002 would adopt the federal exemption amounts for 2002-2004 (but not the phase-out) and would repeal the tax for deaths occurring in 2005 and after. As of this writing, the Governor has neither signed nor vetoed the bill.
- Pennsylvania Pennsylvania enacted in legislation in 2002 to tie the state estate tax to the federal death tax credit as of 6/1/2001.
- Rhode Island Passed legislation in 2002 providing that state death tax is equal to the amount available under state death tax credit as it existed on 12/31/2001.

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- Vermont Legislation passed in 2002 conform state law references to the state death tax credit as in effect on 1/1/2001. The law, however, incorporated all other estate tax features of EGTRRA, including the higher exemption amounts.
- Virginia Prior Virginia law tied the state estate tax to the death tax credit as it existed on Jan. 1, 1978.
- Washington Prior Washington law tied the pick-up tax to the death tax credit in effect on Jan. 1, 2001.
- Wisconsin Legislation passed in 2001 provides that for deaths occurring from 10/1/2002 through 12/31/2007, the state pick-up tax is computed under federal law in effect on 12/31/2000. Effective for deaths occurring after 12/31/2007, the state tax is tied to federal law in effect at that time.

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