

MINUTES OF THE SENATE JUDICIARY COMMITTEE.

The meeting was called to order by Chairman John Vratil at 9:30 a.m. on February 4, 2003 in Room 123-S of the Capitol.

All members were present.

Committee staff present: Mike Heim, Kansas Legislative Research Department
Lisa Montgomery, Office of the Revisor of Statutes
Dee Woodson, Committee Secretary

Conferees appearing before the committee:

Terri Roberts, Tobacco Free Kansas Coalition
Ron Pope, Kansas Trial Lawyers
Ed Larson, Kansas Judicial Council
Melissa Wangemann, Secretary of State's Office
Hal Hudson, National Federation of Independent Business

Others attending: see attached list

Chairman Vratil called for bill introductions. Senator Gilstrap asked that a bill be introduced which is requested by an Assistant District Attorney in Wyandotte County, pertaining to forensic laboratory services rendered by Kansas City, Kansas Community College. Senator Gilstrap made a motion that this bill be introduced, seconded by Senator Allen, and the motion carried.

SB 48 - appeal bonds in litigation involving signatories or successors of the tobacco litigation agreement

The Chair reopened the hearing on **SB 48**. Conferee Roberts testified in opposition to the proposed legislation. She stated that **SB 48** appears to give special considerations/protections to certain tobacco companies in court cases in which there is an unfavorable court decision and the case is then appealed by the tobacco company. Ms. Roberts said that the bill imposes a \$25,000,000 statutory cap on an appeal bond in such cases, and only those tobacco companies that are part of the MSA would benefit from this proposed statute change; no other commercial, public or privately held corporations. She added that limiting the appeal bond amount for one type of industry would set a precedent that other industries might seek. (Attachment 1)

Conferee Pope testified in opposition of **SB 48** as it sets a dangerous precedent for other industries to seek similar protections while eliminating the rights of individuals. He stated that it was not true that the MSA payments could be in jeopardy. He said that these types of verdict amounts are extremely rare in Kansas, and was not aware of any situation in Kansas where posting an appeal bond was a problem for any judgments that have been entered. He explained that a limit of \$25 million is insufficient in cases where individuals have suffered major injuries or death by powerful corporations. Mr. Pope added that the tobacco companies are well-diversified with the financial capability of paying and posting the bond, and are not at risk of bankruptcy. (Attachment 2)

After brief discussion, the Chair closed the hearing on **SB 48**.

SB 37 - receipts from an interest in minerals and other natural resources pursuant to the uniform principal and income act

Chairman Vratil opened the hearing on **SB 37**. Conferee Larson testified in support of **SB 37** for the Kansas Judicial Council. He explained that the change which is suggested by **SB 37** is to adopt the current depletion allowance under the federal income tax code (15% of gross receipts in case of a royalty, shut in well payment, take or pay payment, bonus or more than nominal delay rental and 15% of the net amount received from a working interest) as the amount to be credited to principal and balance (85%) to be allocated to income. He said the suggested change simply strikes the "90" from lines 25 and 28 of the existing act and inserts in its place "15". Mr. Larson stated that the change is consistent with the approach taken by surrounding states with a substantial oil and gas industry when they adopted the 1997 version of the Uniform Principle and Income Act. (Attachment 3)

CONTINUATION SHEET

MINUTES OF THE SENATE JUDICIARY COMMITTEE on February 4, 2003 in Room 123-S of the Capitol.

After brief Committee questions and discussion, the Chair closed the hearing on **SB 37**.

SB 38 - annual report, filing of certain documents, franchise tax and business activities of certain business entities

Chairman Vratil opened the hearing on **SB 38**. Conferee Wangemann explained the changes requested by the Secretary of State's office. In her written testimony (Attachment 4) she outlined the recommended amendments to the bill involving filing procedures, extensions, business trust annual reports, definition of "doing business" for foreign entities, agricultural information on annual reports, third-party agent for Certificates of Good Standing, and franchise tax calculation. She noted there would be a fiscal impact on state general funds regarding the franchise tax amendment involving parent entities that own net worth in subsidiaries and are being taxed twice. Ms. Wangemann stated that the Secretary of State believes the amendment promotes fairness and equity in taxing Kansas business entities.

Question was asked about how much revenue would be lost in allowing the subsidiaries not to pay the tax. Ms. Wangemann replied that the Secretary of State's Office and the Department of Revenue do not track companies by the parent/subsidiary relationship, so they are unable to estimate the effect currently.

Copies of the fiscal note for **SB 38** were distributed to Committee members. (Attachment 5) Committee discussion continued regarding the loss of revenue involving the franchise tax issue. The Chair asked if the Secretary of State's Office could furnish some additional information and possible estimates on this issue.

Written testimony was submitted in opposition to **SB 38** by Hal Hudson, State Director for the National Federation of Independent Business (NFIB). He asked that the bill be amended on page 2, lines 5 through 8, and elsewhere in the bill where reference is made to payment of \$1 per \$1,000 or net worth, with a minimum of \$40 and a maximum of \$5,000. With Mr. Hudson's written testimony was attached a copy of Kenneth Daniels' testimony before the House Taxation Committee on January 29, 2003 in regard to **HB 2025**. (Attachment 6)

After brief discussion, the Chairman closed the hearing on **SB 38**.

Final Action on:

SB 21 - nomination and selection of justices and judge

SB 28 - professional corporation law of Kansas

SB 29 - corporation code amendments

Chairman Vratil briefly reviewed **SB 21**, and explained that it was cleanup legislation. Senator Oleen moved to pass SB 21 out favorably, seconded by Senator O'Connor, and the motion carried.

The Chair reviewed **SB 28** and the technical amendments submitted by the Secretary of State's Office. Senator Goodwin made a motion to accept the amendments to the bill, seconded by Senator Donovan, and the motion carried.

Senator Oleen moved that the Committee report SB 28 out favorably as amended, seconded by Senator Goodwin, and motion carried.

Chairman Vratil reviewed **SB 29**, and reminded the Committee that the Secretary of State's Office recommended that the franchise tax provision regarding parent/subsidiaries corporations, which also appears in **SB 38**, should either be left in both bills or taken out of both bills for conformity.

Final action on **SB 29** was postponed after Committee discussion and request for additional information from the Secretary of State's Office.

The meeting adjourned at 10:30 a.m. The next scheduled meeting is February 5, 2003.

SENATE JUDICIARY COMMITTEE GUEST LIST

DATE: Feb. 4, 2003

NAME	REPRESENTING
Fariba Pouraryan	S.O.S.
Trista Curzydlo	KS Bar Assn.
Jesse Boston	S.O.S.
Melissa Wangeman	S.O.S.
Mary Jane Stettelman	KGFA / KARA
SCOTT SCHNEIDER	KADC
Mary Beth Lidd	Jewele Jesta Anthony
Wanda M. Hays	KAPA-KRINCA
Lark Bradford	Inter-Faith Ministries
ADAM GASSER	SEN. ADKINS
Diane Albert	KDOR
Kyle Kenler	DOB
Aui Hyten	JUDICIAL BRANCH
Christina Collins	KMS
John C. Gottenberg	Alpha Group



Contact: Terri Roberts J.D., R.N.
 Kansas State Nurses Association
 1208 SW Tyler
 Topeka, Kansas 66612-1735
 Phone 785.233.8638/ troberts@ksna.net

Tobacco *Free* Kansas Coalition, Inc.

S.B. 48 APPEAL BONDS IN LITIGATION; CAP OF \$25,000 FOR TOBACCO COMPANIES IN MSA

February 3, 2003

Senator Vratil and members of the Senate Judiciary Committee, my name is Terri Roberts, the Immediate Past-President, here today representing the TOBACCO FREE KANSAS COALITION. S.B. 48 on its face appears to give special considerations/ protections to certain tobacco companies in court cases in which there is an unfavorable court decision and the case is then appealed by the tobacco company. The bill imposes a \$25,000,000 statutory cap on a appeal bond in such cases. Only those tobacco companies part of the Master Settlement Agreement would benefit from this proposed statute change, no other commerical, public or privately held corporations.

From a public policy perspective we cannot support this special provision singling out tobacco companies by providing a special benefit. While we don't anticipate that tobacco companies would be unscrupulous with their financial holdings during a 1-2 year time frame while a verdict is being appealed, as a matter of fair public policy, we support that the policy in place for setting the appeal bond amount be retained to protect the citizen or citizens for whom the verdict was rendered. Limiting the appeal bond amount for one type of industry (and narrowing it even more to those participating in the MSA) sets a precedent that other industries might seek.

The appeal bond if set too low would encourage frivolous appeals by companies not prevailing at the trial court level. Appeal bonds are designed to protect the plaintiff and ensure that the resources are available to pay the amount awarded by the court in civil actions.

We strongly urge this committee to reject S.B. 48.

Senate Judiciary
 2-4-03
 Attachment 1-1



Tobacco *Free* Kansas Coalition, Inc.

Tobacco Free Kansas Coalition Organization Members 2002-03

Barber County Health Department
 Barton County Health Department
 Big Brothers & Big Sisters of Kansas
 Boys and Girls Club of Manhattan
 Butler County Health Department
 Cloud County Health Department
 Coffey County Health Department
 Community Awareness Team
 Cowley County Health Department
 Kansas D.A.R.E.
 Dickinson County Health Department
 Gray County Health Department
 Harvey Co. Partnership/Communities in Schools
 Jefferson County Health Department
 Johnson County Health Department
 KAHPERD
 Kansas Department of Health and Environment/Office of Rural and Local Health
 Kansas Academy of Family Physicians
 Kansas Area Agency on Aging Assoc.
 Kansas Association of Local Health Departments
 Kansas Dental Association
 Kansas Department of Health and Environment/Bureau of Health Promotion
 Kansas Family Partnership
 Kansas Hospital Association
 Kansas Public Health Association
 Kansas School Nurse Organization
 Kansas State Nurses Association

Leavenworth County Health Department
 Manhattan/Riley County Health Department
 Marion County Health Department
 McPherson County Health Department
 Meade County Health Department
 Montgomery County Health Department
 Osborne County Health Department
 Pawnee County Health Department
 Pottawatomie County Health Department
 Regional Prevention Center of Northwest Kansas (Hays)
 Regional Prevention Center of Northwest Kansas (Colby)
 Regional Prevention Center of Johnson, Leavenworth, and Miami Counties
 Regional Prevention Center of Northeast Kansas
 Regional Prevention Center of Southeast Kansas
 Rooks County Health Department
 Salina Tobacco Use Prevention Program
 School of Pharmacy - University of Kansas
 Shawnee County Prevention and Recovery Services
 Thomas County Health Department
 Trego County Health Department
 USD 470, Arkansas City Public Schools
 University of Kansas Medical Center
 Via Christi Research, Inc.
 Wabaunsee County Health Department
 Wichita/Sedgwick County Health Department
 Wichita/Sedgwick County Regional Prevention Center

Charter Members

American Cancer Society, Kansas Division
 American Heart Association, Kansas Division
 American Lung Association of Kansas

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TOBACCO FREE KANSAS COALITION, INCORPORATED OFFICERS

Kevin Walker

ADVOCACY DIRECTOR
 AMERICAN HEART ASSOCIATION
 HEARTLAND AFFILIATE



Stephanie Sharp

ADVOCACY DIRECTOR
 AMERICAN CANCER SOCIETY
 HEARTLAND DIVISION



Joan Smith

HEALTH EDUCATOR
 RILEY COUNTY/MANHATTAN HEALTH DEPARTMENT

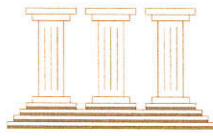
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Topeka Office

4300 SW Drury Lane
 Topeka, Kansas 66604

Phone 785-272-8396

Fax 785-272-9297



KANSAS TRIAL LAWYERS ASSOCIATION

Lawyers Representing Consumers

TO: Members of the House Judiciary Committee

FROM: Ron Pope
Kansas Trial Lawyers Association

RE: 2003 SB 48

DATE: February 3, 2003

Chairman Vratil and members of the Senate Judiciary Committee. I am Ron Pope, KTLA president elect of the Kansas Trial Lawyers Association. We are a statewide, nonprofit organization of lawyers who represent consumers and advocate for the safety of families and the preservation of the civil justice system. I appreciate the opportunity to appear before you today in opposition to SB 48.

KTLA opposes SB 48, which places limitations on appeal bonds. This amendment applies an appeal bond limit of \$25 million on judgments. This is special legislation sought by the tobacco industry which sets a dangerous precedent for other industries to seek similar protections while eliminating the rights of individuals. A limit of \$25 million is insufficient in cases where individuals have suffered major injuries or deaths by powerful corporations.

What is the problem to be solved with this legislation? In reality, these types of verdict amounts are extremely rare in Kansas. I am not aware of any situation in Kansas where posting an appeal bond was a problem for any judgments that have been entered. However, a verdict in Kansas of this amount would reflect major injuries and damages to individual Kansans by a very powerful corporate wrongdoer. This industry continues to profit heavily, both in the United States and abroad, from the sale of their dangerous product. These are well-diversified companies with the financial capability of paying and posting the bond. They are not at risk of bankruptcy.

R.J. Reynolds, on its website, admits that the company "has been subject to significant litigation for many decades; however, the volume of litigation against Reynolds Tobacco and the tobacco industry has remained manageable...Accordingly, the company's ability to defend these cases remains solid and intact." (http://www.rjrt.com/TI/TIlitigation_cover.asp)

SB 48 benefits **only** the tobacco industry. Keep in mind that Kansas citizens were among those harmed by the tobacco industry. As a result of that harm, the tobacco industry was required by the Master Settlement Agreement to reimburse Kansas for the costs of providing health care to Medicaid recipients. And now, that same industry is asking for special consideration should the industry be found responsible for future damages and misconduct in excess of \$25 million.

Terry Humphrey, Executive Director

Fire Station No. 2 • 719 SW Van Buren Street, Suite 100 • Topeka, Ks 66603-3715 •

E-Mail: triallaw@ink.org

Senate Judiciary

2-04-03
Attachment 2-1

SB 48 sets a dangerous precedent in Kansas. Amending our state policy to benefit the tobacco industry not only jeopardizes possible future cases brought by individual Kansans, but also opens the door for other industries and corporations to seek similar special protection. The costs of these corporate benefits are then born by individual Kansas consumers.

In addition, Kansans who have suffered these catastrophic injuries and damages may find themselves facing needless delays without the assurance that they will be fairly compensated when the appeal process is over. The provisions within SB 48 would encourage frivolous appeals by the tobacco industry. Currently, Kansas law includes statutory procedures for delays and enforcement of judgments that afford reasonable and timely protections to a party for obvious errors or modifications that need to be made to a judgment.

Under K.S.A. 60-262(a), all judgments, except injunctions and receiverships are automatically stayed following entrance of judgment for 10 days. In its discretion, the Court may stay the execution of any judgment pending a motion for new trial; to alter or amend the judgment; for relief from the judgment or order; for judgment as a matter of law; or for amendment to the findings of fact. Otherwise, a judgment is the final determination of the rights of the parties in an action. A judgment becomes effective when it is entered pursuant to K.S.A. 60-258. Obviously then a judgment is "effective" before appeal.

The bond requirements as specified in SB 48 are insufficient. Currently, Kansas law requires bond to be set at/or greater than the amount of judgment. Reducing the bond limit for tobacco companies sends the wrong message to wrongdoers.

Decreasing bond requirements will also result in:

- (a) A delay of payment of judgment rather than deciding a legitimate issue of law that needs to be decided on appeal;
- (b) Increasing the leverage of a wrongdoer. A victim may feel forced to settle for a lesser amount, fearing the consequences of delays that are necessarily caused by appeals. This fear would be perpetuated because the wrongdoer is not been required to post a bond for the full value;
- (c) Possibly allowing for evasion of judgment responsibilities by disposal of assets. This statute puts the onus on the victim to prove that the wrongdoer is in fact wrongfully disposing of assets;
- (d) Discouraging settlements on the part of the wrongdoer unless it is for a much smaller amount. Since the wrongdoer does not have to immediately utilize its assets for payment of the judgment, the wrongdoer gets the benefit of the time value of money, which could easily outpace the amount of interest accruing on the judgment.

Thank you for the opportunity to express KTLA's opposition to SB 48. This bill sets the policy precedent of rewarding a corporate wrongdoer with special protections at the risk of the individual rights of Kansans. It removes current judicial discretion and statutory protections to victims against needless or unreasonable delays and imposes an insufficient bond limit, which unfairly benefits the wrongdoer. We respectfully request the committee to vote against passage of SB 48.



KANSAS JUDICIAL COUNCIL

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Kansas Judicial Center
301 S.W. Tenth Street, Suite 262
Topeka, Kansas 66612-1507

Telephone (785) 296-2498
Facsimile (785) 296-1035

Judicial.Council@ksjc.state.ks.us
www.kscourts.org/council

RANDY M. HEARRELL
EXECUTIVE DIRECTOR
NANCY J. STROUSE
RESEARCH ATTORNEY
JANELLE L. WILLIAMS
ADMINISTRATIVE ASSISTANT
MARIAN L. CLINKENBEARD
ADMINISTRATIVE ASSISTANT

MEMORANDUM

TO: House Judiciary Committee
FROM: Kansas Judicial Council -Edward Larson
DATE: February 4, 2003
RE: 2003 SB 37

My name is Edward Larson and I appear today as a member of the Judicial Council Probate Law Advisory Committee, in support of Senate Bill No. 37 which amends K.S.A. 58-9-411. Members of the Probate Law Advisory Committee are:

Gerald L. Goddell, Chair, Topeka
Cheryl C. Boushka, Overland Park
Judge Same K. Bruner, Overland Park
Tim Carmody, Overland Park
Michael L. Clutter, Topeka
Peter A. Cotorceanu, Topeka
Martin B. Dickinson, Jr. Lawrence
Jack R. Euler, Troy
Senator Greta Goodwin, Winfield
Mark Knackendoffel, Manhattan
Justice Edward Larson, Topeka
Phillip D. Ridenour, Cimarron
Willard B. Thompson, Wichita

When the 1997 revision of the Uniform Principal and Income Act was adopted by the 2000 Kansas Legislature (HB 2501), it was not reviewed section by section by the Probate Law Advisory Committee or the Judicial Council. One of the provisions substantially changed our previous law in Kansas, KSA 58-909 (a) (3), relating to how gross receipts from oil or gas royalty are apportioned between principal and income.

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Under the provisions of the law prior to the 2000 amendments, twenty two percent (22%) of the gross receipts were to be added to the principal as an allowance for depletion with the balance of the gross receipts, after payment therefrom of all expenses, considered income and payable to a life tenant.

The 2000 amendments essentially reversed the allocation and provided that 90 percent (90%) of the gross receipts must be allocated to principal and the balance ten percent (10%) is to be received by the life tenant as income. Copies of both provisions are attached to my testimony as Exhibits A & B.

While well drafted instruments, whether they be deeds establishing life estates, a provision in a will granting a life estate and remainder interest, or a revocable trust where the income for life is granted to a beneficiary often provide that all of the gross receipts from oil or gas production is to be treated as income, the statutory division must be applied to new production in the absence of specific directions in the applicable instrument to the contrary. The old doctrines of "open mines" and "closed mines" are specifically abolished by the Uniform Act, (see comment to ¶ 411, 7B Uniform Laws Annotated p. 175) although an almost 40 year old Kansas Supreme Court decision, Kimbark Exploration Co. v. Von Lintel, 192 Kan 791, 391 P. 2d 55 (1964) did not recognize this in our first Uniform Principal & Income Act case.

The change which is suggested by Senate Bill No. 37 is to adopt the current depletion allowance under the federal income tax code (15% of gross receipts in case of a royalty, shut in well payment, take or pay payment, bonus or more than nominal delay rental and 15% of the net amount received from a working interest) as the amount to be credited to principal and the balance (85%) to be allocated to income.

The suggested change which will be made if Senate Bill No. 37 is adopted simply strikes the "90" from lines 25 and 28 of the existing act and inserts in its place "15".

The suggested change which would be made by Senate Bill No. 37 is consistent with the approach taken by surrounding states with a substantial oil and gas industry when they adopted the 1997 version of the Uniform Principle and Income Act.

Oklahoma adopted the current IRS depletion rate of 15% to principal and 85% to income.

New Mexico tied its allocation to that made by the internal revenue code which is currently 15% to principal and 85% to income.

Wyoming substituted 27.5% for 90% throughout the revised Uniform Acts provisions.

We believe this to be in the best interest of life tenants and income trust beneficiaries while still providing realistic protection to remainder men.

EXHIBIT "A" LAW PRIOR TO 2000 AMENDMENTS

58-909. Disposition of natural resources. (a) If any part of the principal consists of a right to receive royalties, overriding or limited royalties, working interests, production payments, net profit interest, or other interests in minerals or other natural resources in, on or under land, the receipts from taking the natural resources from the land shall be allocated as follows:

(1) If received as rent on a lease or extension payments on a lease, the receipts are income.

(2) If received from a production payment, the receipts are income to the extent of any factor for interest or its equivalent provided in the governing instrument. There shall be allocated to principal the fraction of the balance of the receipts which the unrecovered cost of the production payment bears to the balance owed on the production payment, exclusive of any factor for interest or its equivalent. The receipts not allocated to principal are income.

(3) If received as a royalty, overriding or limited royalty, or bonus, or from a working net profit, or any other interest in minerals or other natural resources, receipts not provided for in the preceding paragraphs of this section shall be apportioned on a yearly basis in accordance with this paragraph whether or not any natural resource was being taken from the land at the time the trust was established. Twenty-two percent (22%) of the gross receipts (but not to exceed fifty percent (50%) of the net receipts remaining after payment of all expenses, direct and indirect, computed without allowance for depletion) shall be added to principal as an allowance for depletion. The balance of the gross receipts, after payment therefrom of all expenses, direct and indirect, is income.

(b) If a trustee, on the effective date of this act, held an item of depletable property of a type specified in this section, the trustee shall allocate receipts from the property in the manner used before the effective date of this act, but as to all depletable property acquired after the effective date of this act by an existing or new trust, the method of allocation provided herein shall be used.

(c) This section does not apply to timber, water, soil, sod, dirt, turf, or mosses.

History: L. 1951, ch. 509, § 9; L. 1965, ch. 344, § 9; L. 1972, ch. 211, § 1; July 1.

Research and Practice Aids:

Trusts — 272.

C.J.S. Trusts § 355.

EXHIBIT "B" LAW AS NOW EXISTS UNDER 2000 AMENDMENTS

58-9-411. Minerals, water and other natural resources. (a) To the extent that a trustee accounts for receipts from an interest in minerals or other natural resources pursuant to this section, the trustee shall allocate them as follows:

(1) If received as nominal delay rental or nominal annual rent on a lease, a receipt must be allocated to income.

(2) If received from a production payment, a receipt must be allocated to income if and to the extent that the agreement creating the production payment provides a factor for interest or its equivalent. The balance must be allocated to principal.

(3) If an amount received as a royalty, shut-in-well payment, take-or-pay payment, bonus, or delay rental is more than nominal, 90 percent must be allocated to principal and the balance to income.

(4) If an amount is received from a working interest or any other interest not provided for in subsection (1), (2), or (3), 90 percent of the net amount received must be allocated to principal and the balance to income.

(b) An amount received on account of an interest in water that is renewable must be allocated to income. If the water is not renewable, 90 percent of the amount must be allocated to principal and the balance to income.

(c) This act applies whether or not a decedent or donor was extracting minerals, water, or other natural resources before the interest became subject to the trust.

(d) If a trust owns an interest in minerals, water, or other natural resources on the effective date of this act, the trustee may allocate receipts from the interest as provided in this act or in the manner used by the trustee before the effective date of this act. If the trust acquires an interest in minerals, water, or other natural resources after the effective date of this act, the trustee shall allocate receipts from the interest as provided in this act.

History: L. 2000, ch. 61, § 20, July 1, 2000

RON THORNBURGH
Secretary of State



First Floor, Memorial Hall
120 SW 10th Ave.
Topeka, KS 66612-1594
(785) 296-4564

TESTIMONY OF THE SECRETARY OF STATE
TO THE SENATE JUDICIARY COMMITTEE
ON SB 38

February 4, 2003

Mr. Chairman and Members of the Committee:

The Secretary of State appreciates the introduction and hearing on SB 38, which was requested by our office.

The Kansas Bar Association and the Secretary of State worked jointly this last year to update the Kansas corporate code. A bill containing an amended corporate code has been introduced and heard by this committee. The purpose of SB 38 is to duplicate changes made in the corporate code in the laws relating to all other business entities. Our intent is to create uniformity and consistency among all business entities that file with the Secretary of State. The amendments contained in the bill are outlined below.

1. **Filing Procedures.** The Secretary of State adopted an imaging system in 2000, which replaced our paper filing system. All documents are indexed and maintained on the imaging system and therefore retention of paper documents is no longer necessary. SB 38 directs the Secretary of State to image the original paper document filed by the customer and to return the paper document to the customer as a certified copy. This new procedure reduces our storage needs while providing the customer evidence of the document that was recorded in our office. Our office has checked with the Historical Society and they are satisfied that the Secretary of State's imaging system will adequately preserve our records.

2. **Extensions.** The current statutory language allowing business trusts, limited liability companies and limited partnerships to file an extension (which delays the filing deadline for the annual report) is contained in the corporate code. SB 38 moves these provisions to their respective acts. The corporate code also contains a provision limiting public disclosure of the IRS tax extension filed with the Secretary of State; this provision is likewise moved to the correct statutory section for LLCs, LPs and business trusts.

3. **Business Trust Annual Reports.** The business trust annual report still requires detailed financial disclosure, a fact discovered when I amended the statutory section on annual reports to add the extension provision. Balance sheets were eliminated from all other entity annual reports in 1997. SB 38 strikes this language from the business trust annual report in order to create uniform reporting requirements among all business entities.

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4. **Definition of “doing business” for Foreign Entities.** The definition of “doing business,” which determines when a foreign entity must register with the Secretary of State, is amended for LLCs and LPs to reflect the definition given in the KBA corporate code revision. The new definition is based on Delaware law and the Kansas Revised Uniform Partnership Act. All foreign entities that register with our office will use this uniform definition.

5. **Agricultural Information on Annual Reports.** This amendment would strike the requirement that limited partnerships include the section, range and township when listing agricultural land on the annual report. Several of our customers requested this amendment so that they would not have to track down detailed land descriptions from the Register of Deeds in order to complete the annual report.

6. **Third-Party Agent for Certificates of Good Standing.** Foreign entities that register with the Secretary of State must produce a certificate of good standing from the state of organization. This information is generally obtained from the foreign entity’s filing office, such as the Secretary of State. However, no state filing office is able to produce an electronic version of the certificate. This amendment allows our office to accept certificates of good standing from a reliable third-party vendor approved by our office, who can provide the information in electronic format.

7. **Franchise Tax Calculation.** Business entities pay a franchise tax at the time they file their annual report with our office. The franchise tax is calculated based on net worth; \$2 for each \$1,000 in net worth. Parent entities that own net worth in subsidiaries are therefore taxed twice. SB 38 would allow a parent entity to subtract any net worth reported by the subsidiary entity before computing its franchise tax, thereby eliminating the double taxation. A subsidiary entity is defined as ownership of over 50%, based on recommendations from the Department of Revenue.

This amendment will have a fiscal impact on state general funds; therefore the committee should carefully consider this provision of the bill. The Secretary of State believes the amendment promotes fairness and equity in taxing Kansas business entities; however, we would understand if the committee decides to eliminate this provision of the bill.

I appreciate the opportunity to appear today on SB 38 and would be happy to answer questions.

Melissa A. Wangemann, Legal Counsel
Deputy Assistant Secretary of State

KANSAS

DIVISION OF THE BUDGET
DUANE A. GOOSSEN, DIRECTOR

KATHLEEN SEBELIUS, GOVERNOR

February 4, 2003

The Honorable Stan Clark, Chairperson
Senate Committee on Utilities
Statehouse, Room 449-N
Topeka, Kansas 66612

Dear Senator Clark:

SUBJECT: Fiscal Note for **SB 38** by Senate Committee on ~~Utilities~~ **JUDICIARY**

In accordance with KSA 75-3715a, the following fiscal note concerning SB 38 is respectfully submitted to your committee.

SB 38 would amend the Kansas Corporate Code in six ways. First, the bill would eliminate the balance sheet on business trust annual reports that are filed with the Secretary of State. Balance sheets were removed from all other annual reports in 1997. Second, the bill would move provisions relating to extensions on business trusts and limited liability companies from the general corporate code to the appropriate statutory sections. Third, it would allow the Secretary of State to return the original filing as a certified copy after imaging the document. Fourth it would allow the Secretary of State to obtain a certificate of good standing on a foreign business from a third-party agent. Currently, the certificate must be obtained from the filing officer of the business' home state. Fifth, the bill would define "doing business" so that foreign businesses would be required to register with the Secretary of State and, finally, the bill would allow a parent company to subtract the net worth of a subsidiary before calculating the franchise tax.

SB 38 would reduce State General Fund revenues; however, the full effect cannot be determined currently. According to the Secretary of State's Office, this bill allows a parent company to subtract the net worth of a subsidiary prior to calculating its corporate franchise tax. Because this tax is based on net worth, a parent company that owns all equity in a subsidiary essentially pays the franchise tax twice: once on the value of the parent and the subsidiary and

The Honorable Stan Clark, Chairperson
February 4, 2003
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again for the subsidiary only. The Secretary of State's Office does not track companies by the parent/subsidiary relationship, so it is unable to estimate the effect currently.

The Secretary of State's Office states that other provisions in the bill may affect its operating budget, but any costs would be absorbed within the current budget. Any fiscal effect associated with the passage of SB 38 is not included in *The FY 2004 Governor's Budget Report*.

Sincerely,



Duane A. Goossen
Director of the Budget

cc:

KANSAS

**Statement by Hal Hudson, State Director
National Federation of Independent Business
Before the
Senate Judiciary Committee
On Senate Bill 38
February 5, 2003**

Mr. Chairman and Members of the Committee:

Thank you for allowing me this opportunity to speak to you.

My name is Hal Hudson, and I am the State Director for the National Federation of Independent Business. I appear before you today to oppose enactment of SB 38, without one important amendment. Otherwise, the bill has merit.

We would ask that you amend SB 38 on page 2, lines 5 through 8, and elsewhere in the bill where reference is made to payment of the franchise tax, as follows:

The franchise fee should be \$1.00 per \$1,000 of net worth, with a minimum of \$40.00, and a maximum of \$5,000.

This tax increase, as now is current law, was enacted late in the 2002 session, from a conference committee report, without ever having been heard by a committee or passed by either the Senate or the House as a stand along issue. In fact, when it appeared on the floor as a committee amendment to another bill, the House voted 123-0 to reject the increase.

Current law causes a burden on small businesses who are corporations, and who will pay the majority of this tax increase. NFIB is supporting a measure already in the works in the House to roll back this tax increase, and we hope you would agree to do the same within SB 38.

Thank you for your consideration of our concern.

The National Federation of Independent Business (NFIB) is the nation's largest small-business advocacy group. A nonprofit, nonpartisan organization founded in 1943, NFIB represents the consensus views of its 600,000 members in Washington and all 50 state capitals, including over 6,000 members in Kansas. More information about NFIB is available at www.nfib.com.

1 ~~to be used elsewhere.~~

2 (b) (1) At the time of filing its annual report, the business trust shall
3 pay to the secretary of state an annual franchise tax in an amount equal
4 to ~~\$2~~ for each \$1,000 of its corpus ~~as shown by its balance sheet, or, in~~ \$1.00
5 the case of a foreign business trust, in an amount equal to ~~\$2~~ for each
6 \$1,000 of that portion of its corpus which is located in or which it uses
7 or intends to use in this state ~~as shown by its balance sheet~~, except that
8 in any case no such tax shall be less than \$40 nor more than \$5,000.

9 (2) The failure of any domestic or foreign business trust to file its
10 annual report and pay its annual franchise tax within 90 days from the
11 date on which they are due, as aforesaid, shall work a forfeiture of its
12 authority to transact business in this state and all of the remedies, pro-
13 cedures, and penalties specified in K.S.A. 17-7509 and 17-7510, and
14 amendments thereto, with respect to a corporation which fails to file its
15 annual report or pay its annual franchise tax within 90 days after they are
16 due, shall be applicable to such business trust.

17 (c) *When any business trust that is required to file an annual report*
18 *with the secretary of state, applies for an extension of time for filing its*
19 *annual income tax return with the internal revenue service, the time for*
20 *filing the annual report with the secretary of state shall be extended, cor-*
21 *respondingly, upon filing a copy of the application to income tax author-*
22 *ities with the secretary of state, prior to the due date of its annual report.*
23 *All such copies of applications for extension of the time for filing income*
24 *tax returns shall be maintained by the secretary of state in a confidential*
25 *file and shall not be disclosed to any person except as authorized pursuant*
26 *to the provisions of K.S.A. 79-3234 and amendments thereto, a proper*
27 *judicial order, and subsection (d). All copies of such applications shall be*
28 *preserved for one year and until the secretary of state orders that the*
29 *copies are to be destroyed.*

30 (d) *A copy of such application shall be open to inspection by or dis-*
31 *closure to any person designated by resolution of the trustees of the busi-*
32 *ness trust.*

33 Sec. 2. K.S.A. 2002 Supp. 17-7678 is hereby amended to read as
34 follows: 17-7678. (a) The original signed copy, ~~together with a duplicate~~
35 ~~copy which may be either a signed or conformed copy,~~ of articles of
36 organization or any certificate to be filed pursuant to this act, shall be
37 filed with the secretary of state. A person who executes a certificate,
38 statement or articles as an agent or fiduciary shall not be required to
39 exhibit evidence of the person's authority as a prerequisite to filing. Any
40 signature on any articles or certificate authorized to be filed with the
41 secretary of state under any provision of this act may be a facsimile, a
42 conformed signature or an electronically transmitted signature. Unless
43 the secretary of state finds that any filing does not conform to law, upon

6-2

Presentation to the House Taxation Committee
January 29, 2003

By Kenneth L. Daniel
Chairman and C.E.O., Midway Sales & Distributing, Inc. d/b/a Midway Wholesale
and
2003 Chairman, Kansas Leadership Council,
National Federation of Independent Business

Mr. Chairman and Members of the Committee:

My name is Kenneth Daniel. I am the C.E.O. of Midway Wholesale, a building materials distributor headquartered in Topeka with five branches in other Kansas cities, plus one in Missouri and one in Arkansas. I am also the Chairman of NFIB/Kansas, a volunteer position.

I would like to speak in support of HB2025. The Kansas Franchise Tax is the most aggressively anti-small business of all the business taxes in Kansas. It is extremely regressive. Many small businesses with 15 employees pay the same \$5,000 per year as Goodyear, Boeing, and Sprint.

Of the \$36 million per year this tax raises, about 95% is paid by small businesses.

The tax is levied on the net worth of corporations and limited liability partnerships. The "franchise" in the name of the tax refers to the right to operate in Kansas as a limited liability entity. It is not imposed on sole proprietorships or standard partnerships.

This tax was doubled in 2002. It is now \$2 per \$1000 of net worth with a \$5,000 maximum. Last year about 87,000 Kansas businesses paid the tax, and 2,500 of them paid the maximum tax¹. The 400 richest corporations in Kansas will pay only \$2 million of the \$36 million of franchise taxes.

The franchise tax is a highly unfair tax. It is levied whether a business is profitable or not. Identical businesses, organized differently, will pay widely varying amounts. Businesses that need little capital—doctors, lawyers, and service providers, for instance—will pay little tax. Businesses that require heavy capitalization—banks, medium to large contractors, manufacturers, transportation, and distribution—will pay a lot of tax. For most small business owners, much or all of their personal net worth is invested in their business, so this tax is nothing more than a tax on their life savings.

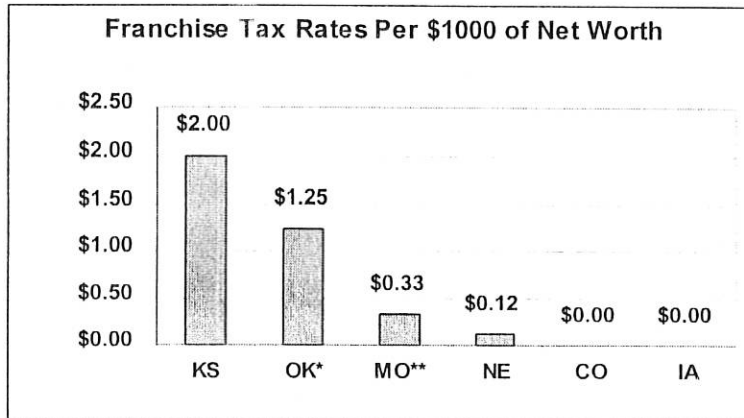
Kansas, at \$2.00 per thousand, has by far the highest tax rate in the region. The tax is 6 times the average rate of the surrounding states (\$.34 per thousand).

The Oklahoma version, at \$1.25 per thousand, is capped at \$20,000 of tax, which equates to a \$16,000,000 net worth. This at least spreads the misery to many large corporations, but it is still a highly regressive tax borne mostly by small businesses.

The Missouri version, at \$.33 per thousand, applies only to the portion of corporate net worth in excess of \$1 million, thereby eliminating this tax for most small businesses. It has no cap. The Missouri version is more of tax on medium and large businesses.

The Nebraska version, at \$.12 per thousand, is capped at \$11,995 of tax (\$15,000 for out-of-state corporations) which equates to \$100,000,000 of net worth, making it the same percentage for almost all businesses in the state, and enabling the rate to be kept very low.

Colorado and Iowa, like many other states across the nation, do not have this tax at all.



* Oklahoma's tax is capped at \$20,000 per year.

** Missouri's tax applies only to the portion of net worth over \$1,000,000.

In NFIB, it is the members, not the leaders, who determine our position on issues. On this issue, they voted, by a 5 to 1 margin, to ask you to roll the rate back to 1% and raise the maximum. I would encourage you to consider keeping the maximum at the present \$5,000 per year until Fiscal Year 2005 to avoid raising taxes on some businesses during these very difficult economic times.

In 2005, the income tax credit on machinery and equipment will increase to 20% from the present 15%. Virtually the same companies that would have to pay more franchise tax with a \$10,000 cap will be getting a much larger tax break from the higher M&E credit.

Please support HB2025 and help small business, the only sector of the Kansas economy that is growing, to create jobs for Kansans.

Thank you. I will be happy to answer any questions.

¹ Per Carol Crupper of the Hutchinson News, June 18, 2002, citing information obtained from the Kansas Secretary of State's office: From July 1, 2001 through June 17, 2002 (11 1/2 months), 86,737 entities had paid the franchise tax. 2,472 paid the maximum amount.