

MINUTES OF THE HOUSE TAXATION COMMITTEE

The meeting was called to order by Chairman Kenny Wilk at 9:00 A.M. on January 23, 2007 in Room 519-S of the Capitol.

All members were present except: Representative Nile Dillmore

Committee staff present:

Chris Courtwright, Legislative Research Department
Martha Dorsey, Legislative Research Department
Gordon Self, Office of Revisor of Statutes
Richard Cram, Department of Revenue
Rose Marie Glatt, Committee Secretary

Conferees appearing before the committee:

Ian Staples, KU Student Senate

Others attending: See attached list.

The Chairman asked for bill introductions.

Ian Staples, KU Student Senate, requested a bill be introduced that would amend the Kansas Retailers' Sales Tax Act, eliminating taxes of college textbooks. Representative Owens moved the introduction, seconded by Carlson. The motion carried.

The Chairman called for a continuation of staff briefings on the interim study reports.

2006 Interim Topics

Motor Fuel Taxation along the Kansas Border

Martha Dorsey, Legislative Research Department, distributed an outline on the final report on Motor Fuel Taxation (Attachment 1). She referred to page 2-12 in the 2006 Interim studies booklet, that had previously been distributed. She reviewed the background on motor fuel tax rates between Kansas and neighboring states and explained legislative efforts with the introduction of **HB 2822** in 2006. That bill would have allowed an alternative motor fuel tax rate at retailers in border communities meeting certain requirements. She briefly reviewed Committee activities and concluded with the Committee recommendation that a study be conducted, such as was originally requested of Kansas, Inc. in September 2006. At that time the Committee Chairperson requested a broad-based examination of fiscal impacts of border zone taxes in general. Discussion followed regarding the rationale and disparity between diesel and gasoline taxes. Staff agreed to provide a multi-state table reflecting those tax rates.

Residential Property Tax Valuation Cap

Chris Courtwright, Legislative Research Department, provided background on **HCR 5027**, a constitutional amendment proposed during the 2006 session, which subsequently led to the LCC charge for further study (Attachment 2). He briefed the Committee on Property Tax Constitutional Amendments since 2000 as well as other approaches to Property Tax relief, including the details on **HCR 5027**. Committee activities were given, and he explained the Committee's Conclusions and Recommendations: 1) The residential valuation cap would tend to shift property taxes away from real estate where values are increasing rapidly and on to other real estate where values are not increasing at the rate of the cap. This could be onerous for young families entering the home market ; 2) Noted that their conclusions were strikingly similar to those made by the 1999 Special Committee on Assessment and Taxation; and 3) The Committee declined to reintroduce a proposed valuation cap constitutional amendment for consideration in 2007. Discussion followed regarding various options that would provide personal property tax relief.

The meeting was adjourned at 10:30 a.m. The next meeting is January 24, 2007.

Special Committee on Assessment and Taxation

MOTOR FUEL TAXATION ALONG THE KANSAS BORDER

CONCLUSIONS AND RECOMMENDATIONS

The Committee recommends a study be conducted as was originally requested of Kansas, Inc. in September 2006, when the Committee Chairperson requested a broad-based examination of fiscal impacts of border zone taxes in general.

Proposed Legislation: None.

BACKGROUND

The Legislative Coordinating Council has authorized the Committee to review the concept for those retailers or communities along the state border of imposing a motor fuels tax that is no more than \$0.01 above the motor fuel tax in the adjoining state; study recent similar legislation in Arkansas and 2006 HB 2822; and study the economic impact of encouraging the purchase of motor fuels in Kansas as opposed to those purchases being made in adjoining states.

Comparison of Motor Fuel Tax Rates: Kansas and Neighboring States

In Kansas communities that border other states, some business owners have complained that motor fuel business is lost because prices at the pump are lower in the bordering states. A primary reason for this cost differential is a difference in motor fuel tax rates.

A review of state motor fuel tax rates in and around Kansas shows Kansas' rates are higher than three of its four border states. The following table depicts these states' motor fuel tax rates as of January 1, 2006.

State	Gas/Gasohol Rate	Diesel Rate
Kansas	\$0.24*	\$0.2600
Missouri	\$0.1755	\$0.1755
Oklahoma	\$0.1700	\$0.1400
Colorado	\$0.2200	\$0.2050
Nebraska	\$0.2700	\$0.2700

* Kansas E85 tax rate as of January 1, 2007 - \$0.17 (pursuant to Laws 2006, Ch. 81, Sec. 2).

Source: Federation of Tax Administrators, "Motor Fuel Excise Tax Rates: January 1, 2006."

Legislative Efforts: 2006 HB 2822; Other States

The 2006 Legislative Session saw the introduction of HB 2822, which would have allowed an alternative motor fuel tax rate at retailers in border communities that meet the following requirements:

- The retailer must be located within 3,000 feet of a state line; or
- The retailer must be located within the city limits of a Kansas city that adjoins the state line.

(Note: The bill's sponsor had drafted an amendment to allow also those retailers located within the city limits of a Kansas city if the city limits are within 3,000 feet of the state line. The amendment also would have controlled for annexation with respect to cities near the state line.)

**HS TAXATION COMMITTEE
1-23-2007
ATTACHMENT 1**

Motor Fuel Taxation along the Kansas Border

Outline of Final Report of the
Special Committee on Assessment and Taxation
to the 2007 Kansas Legislature

1. Framing the border tax issue
 - a. Kansas' tax rate
 - b. Border state rates
 - c. Border retailers' complaint
2. Last year's HB 2822
3. Other states: Arkansas
4. Constitutional Issues
 - a. Violations of equal protection, due process, and abridgement of the privilege and immunities provisions in the state and U.S. Constitutions
 - (1) Arkansas Supreme Court upheld constitutionality of Arkansas' law
 - (2) Determination in Kansas would depend on the specifics of the statute (if enacted) as well as the Kansas Constitution and case law
 - b. Unlawful delegation of legislative authority - could be avoided depending on the way the measure was written
5. Options Considered
 - a. Request a scope statement to study the issue of border taxes
 - (1) Broader issue of border taxes in general - including cigarettes, food, etc.
 - (2) Narrow issue of fuel tax (all the way to just gasoline tax)
 - b. Establish a pilot program specific to gasoline-only border tax, naming specific border communities
6. Conclusions and Recommendations
 - a. Conduct a study of the broader issue of border taxes in general (not just motor fuel taxes).
 - (1) Fiscal impacts related to border communities and Kansas communities near the border communities
 - (2) The state's current and future tax revenue collections if a border zone tax were authorized
 - b. Ask the Secretary of Revenue to work with Kansas, Inc. on how best to accomplish the study and report progress to the House Committee on Taxation in January 2007

The alternative tax rate would have been 0.1 cent per gallon above the lawful rate charged in the adjoining state on motor-vehicle fuel or special fuels, not to exceed the regular Kansas rate. It would have applied only to retail sales to actual consumers. The bill as drafted included diesel as well as gasoline products.

HB 2822, which was heard in the House Transportation Committee but went no further, was modeled generally after an existing law in Arkansas. The Arkansas law, which has been in existence for at least 28 years, allows a lower tax rate on gasoline sold in "cities, incorporated towns, or planned communities" that border on a state line, sold within 800 feet of the shore line of a navigable lake where the opposite shore line is beyond the Arkansas state line, or sold within 800 feet of the Arkansas terminal of a bridge, the center of which is the state line. The lower tax rate cannot be more than 0.1 cent per gallon above the adjoining state's rate.

Allowing alternative motor fuel tax rates at a state's borders appears to be uncommon. The Federation of Tax Administrators (FTA) conducted an electronic-mail survey of states in August 2006. In that survey, the states were asked whether they possessed a different motor vehicle fuel or special fuel tax rate along their borders. Of the 22 states, plus Quebec, that responded to the survey as of the end of August, only one state (Arkansas) and Quebec reported having a border zone tax. The other states responding include Alaska, California, Colorado, Florida, Georgia, Idaho, Illinois, Louisiana, Maryland, Mississippi, Missouri, Montana, Nebraska, Nevada, New Jersey, New York, North Carolina, Texas, West Virginia³, Wisconsin, and Wyoming.

³ A similar proposal was reportedly introduced in a recent West Virginia legislative session, but it did not pass.

COMMITTEE ACTIVITIES

At the September meeting, staff provided a background briefing on the issue. Representatives of Kansas' motor fuels retailing industry, who lived near the border of a state with lower motor fuels taxes, testified in favor of HB 2822. An official from the Arkansas Oil Marketers Association provided information about the Arkansas law and its implementation. The Secretaries of Revenue and Transportation appeared in opposition to the bill. The Committee discussed the potential effects of a motor fuels border tax, as well as border tax differentials for other items such as cigarettes and food. The Committee Chairperson requested that Kansas, Inc. develop a scope statement to study the broader issue of border taxes in general.

At the October meeting, the First Assistant Revisor summarized the constitutional issues involved in the motor fuels border tax issue. His comments included the following:

- A border tax law which provides for a lower motor fuel tax rate for fuel sold in the border zone, in some relationship to motor fuel sold across the border, raises several constitutional questions in relation to retailers in the home state whose businesses lie outside the border zones. Arkansas has long had such a law. The Arkansas Supreme Court upheld the constitutionality of the law. Arguments were raised as to violations of the equal protection, due process, and abridgement of the privilege and immunities provisions in the Arkansas and United States Constitutions. If the Kansas border tax law were written in a manner largely similar to the Arkansas law, and if the Arkansas Supreme Court decision would be valid precedent upon which the Kansas Supreme Court could rely in an action challenging a Kansas border tax law on similar grounds, the border tax law would be upheld. However, any determination of

constitutional issues in Kansas would first involve an analysis of the specific language proposed and involve the specifics of Kansas Constitutional law, case law and statutory law.

- In addition, an additional Kansas Constitutional issue of an unlawful delegation of legislative authority would be raised with regard to any automatic changes in Kansas motor fuel tax rates which do not involve a specific legislative action by the Kansas Legislature. HB 2822 contemplated such automatic changes but could be written in a different manner to avoid such constitutional concerns at the expense of a slower response in motor fuel tax rates in Kansas when the motor fuel tax rate of the adjoining state is changed.

Also at the October meeting, staff provided a copy of the letter that had been written to Kansas, Inc. on behalf of the Committee Chairperson, as well as the initial response provided by Kansas, Inc., which reported the organization's progress to date on the scope statement and projected a scope statement completion date in November (for the final Committee meeting). The President of Kansas, Inc. appeared and responded to questions and concerns. During the discussion, some members noted their concern that the study was too broad as originally conceived. The Committee Chairperson revised the request for the scope statement to include only studying the issue of gasoline tax at the border. The

original sponsor of HB 2822, Representative Virgil Peck, voiced his preference for a pilot program for a gasoline border tax, and he offered the two pilot locations of Coffeyville and Atchison.

Finally, testimony on potential administrative and legal issues was supplied by Richard Cram, Director of Policy and Research for the Kansas Department of Revenue.

At the November meeting, the Committee discussed policy options and recommendations.

CONCLUSIONS AND RECOMMENDATIONS

The Committee recommends that a study be conducted as broadly as was originally requested of Kansas, Inc. in September 2006. The study should determine (a) the fiscal impacts related to border communities, and Kansas communities near the border communities, if a border tax were authorized in Kansas border communities; and (b) the state's current and future tax revenue collections if a border zone tax were authorized. The study is to cover not only motor fuels taxes, but rather address all such border taxes, including those for cigarettes and food sales. The Committee recommends the Secretary of Revenue continue to work with Kansas, Inc. on how best to accomplish the study. The Secretary of Revenue is requested to report the entities' progress to the House Committee on Taxation in January 2007.

Special Committee on Assessment and Taxation

RESIDENTIAL PROPERTY TAX VALUATION CAP

CONCLUSIONS AND RECOMMENDATIONS

The Committee finds that a residential valuation cap would tend to shift property taxes away from real estate where values are increasing rapidly and on to other real estate where values are not increasing at the rate of the cap. The Committee further finds that a property tax system with a valuation cap could be especially onerous for young families entering the housing market for the first time.

Proposed Legislation: None.

BACKGROUND

Among the constitutional amendments under consideration by the House Taxation Committee in 2006 was HCR 5027, a measure that would have limited the annual property valuation increases for most residential parcels to the rate of inflation. The House Committee and Chairperson Wilk asked the Legislative Coordinating Council (LCC) to refer the issue for further study.

The LCC subsequently charged the Special Committee with reviewing the policy implications of 2006 HCR 5027 and making whatever recommendations are deemed appropriate to the 2007 Legislature. Specifically, the Special Committee is asked to recommend whether the proposed amendment or something similar should be reintroduced for consideration in 2007.

Property Tax Constitutional Amendments Since 2000

Section 1 of Article 11 of the *Kansas Constitution* directs the Legislature to provide for a uniform and equal basis of valuation and rate of taxation of all property subject to taxation. Decisions of the Kansas Supreme Court have equated this taxation provision with the equal protection doctrine contained in our Bill of Rights. In this state, uniform and equal basis of valuation is

expressed by the adoption of fair market value in valuation of property for tax purposes. Exceptions to this uniform and equal basis of valuation must be contained in the Constitution. Attempts by the Legislature to provide exceptions to the uniform and equal basis of valuation through statutory means would likely be constitutionally invalid. The Constitution does provide for exceptions to such basis of valuation and grants the authority of the Legislature to provide for exceptions to such valuation basis for recreational vehicles, motor vehicles, mineral products, money, mortgages, notes and other evidence of debt, and grain.

Specified limitations on valuation growth or the grant of authority for the Legislature to prescribe limitations on valuation growth need to be contained in amendments to the Constitution. Any such propositions to amend the Constitution should be expressed as exceptions to the uniform and equal basis of valuation and are often expressed as exceptions to fair market value. Numerous such proposed constitutional amendments have been introduced in the Senate and House, especially since 2000.

These proposed amendments may be grouped into two basic categories. The first category involves general authority granted

to the Legislature to exercise such authority upon its own volition; and the second category involves a constitutional directive to the Legislature to enact legislation with some specificity written into the Constitution.

With regard to the first category, these propositions would add language to the Constitution to grant the Legislature authority to statutorily limit increases in valuation of property. (No specific limitations would be written into the Constitution.) Examples in this category are:

- (1) Authority for the Legislature to place limitations upon increases in valuation of any class or subclass of real property. (2000 HCR 5031 by Tanner and others; 2001 HCR 5026 by Glasscock and others; and 2002 HCR 5045 by Edmonds); and
- (2) Authority for the Legislature to place limitations upon increases in valuation of real property used for residential purposes. (2004 HCR 5031 by Gatewood and Faber; 2004 SCR 1620 by Umbarger and others).

The second category of proposed amendments provide specific language to be written into the Constitution that would require the Legislature to enact legislation to: provide limitations on increases of valuation of certain property owned by certain taxpayers; provide limitations on increases of valuation measured against various consumer price indexes; or specify requirements as to determination of valuation of certain real property. To a large extent, all of these constitutional amendments constitute exceptions to the uniform and equal basis of valuation through modification of the fair market value standard contained in law. Examples in this category are:

- (1) Amendments to require the Legislature to provide by law to limit the increase in valuation of single-family residential real

property with a valuation of < \$250,000 when owned and the principal residence of a Kansas resident 65 years of age or older on January 1 of any tax year. The Legislature is granted authority to enact adjustments in the age and valuation requirements (2004 HCR 5032 by Tafanelli, Wilk and others). A similar variation places the residence valuation limitation at < \$100,000 and is otherwise identical (2005 HCR 5008 by Huff and others). Finally, a 2005 SCR contained the same provisions as 2004 HCR 5032, except there was no valuation ceiling. Residential property of any value would qualify for the valuation limitation. This proposed constitutional amendment did require that the residential property owner must have owned the subject property for at least 10 years (2005 SCR 1605 by Haley).

- (2) There were two variations of constitutional limitations of specific increases in valuation. Rather than prescribing a percentage expressed in the Constitution or requiring the percentage to be provided by statute, such limitations are to be measured against consumer price indexes. The first proposed amendment limited percentage increases in valuation of all real property to the increase in the consumer price index – real estate (2000 HCR 5035 by House Committee on Federal and State Affairs). The other proposed amendment limited percentage increases in valuation of real property used for residential purposes to the average increase of the consumer price index – urban (2006 HCR 5027 by House Committee on Taxation).
- (3) There were two proposed constitutional amendments that provided that the Legislature shall enact legislation to require that the appraised valuation of real property used for residential purposes is to be adjusted to an amount equal to the average of the appraised value of such real property when sold

and the sales price of such real property when sold (2004 HCR 5042 by House Committee on Taxation; 2005 HCR 5009 by F. Miller).

Other Approaches to Property Tax Relief

The Legislature in recent years also has analyzed a number of other mechanisms designed to provide property tax relief to certain classes of property or targeted at selected groups of taxpayers. Among the other forms of property tax relief discussed include increased state aid to local units of government (restoration of demand transfers); expansion of Homestead Property Tax Refund Program (subject of another 2006 interim study); whether some form of the tax lid law should be reimposed on local units of government (subject of another 2006 interim study); property tax deferral programs; and whether the \$20,000 "homestead" exemption from the mandatory school district general fund property tax levy should be expanded or extended to all property taxes.

As to the latter two issues, the National Conference of State Legislatures (NCSL) reports that 24 states and the District of Columbia have property tax deferral programs, with many of them targeted specifically to benefit elderly taxpayers. Legislation was approved by the Kansas House but not the Senate in 1990 that would have established a Kansas deferral program for certain low income taxpayers who were age 65 and above. The issue was subsequently studied by the 1990 Special Committee on Assessment and Taxation, which made no recommendations on the proposal. NCSL also reports that 33 states (including Kansas) and the District of Columbia have some form of "homestead" program wherein a portion of the valuation of certain residential properties is exempt from property taxation.

2006 HCR 5027

As mentioned previously, HCR 5027 would have limited the annual property valuation increases for most residential parcels to the rate of inflation. Exceptions would have been provided for new or newly improved residential real property (which would have been valued in the initial year based upon the valuation of similar properties); and for residential real property which had been sold in the previous year (which would have been valued at the sales price).

If adopted by the voters, the amendment would have had an indeterminate fiscal impact to the state to the extent that less revenues would have been raised by the 21.5 mills in state property tax levies.

A similar proposal was last studied by the Special Committee in 1999. That Special Committee declined to recommend a constitutional amendment limiting growth in assessed valuation, noting that such a proposal could cause:

- a tax shift away from real estate where values are increasing rapidly and on to other real estate where values are not increasing at the rate of the cap;
- a tax shift which could increase the tax burden borne by young families entering the housing market for the first time; and
- a tax shift away from real estate and on to personal property, especially oil and gas and commercial and industrial machinery and equipment.

HCR 5027 would have been placed on the November 7, 2006, general election ballot, had it been approved by the necessary two-thirds majority of both legislative chambers. Had it been subsequently adopted by the voters, it would have been effective beginning in tax year 2007. One set of policy decisions the

Committee would need to consider before reintroducing a similar amendment would relate to the revised date of election and potential implementation date.

COMMITTEE ACTIVITIES

At the October meeting, staff reviewed a number of constitutional amendments considered since 2000 that would have provided exceptions to uniform and equal valuation of certain real estate.

Staff also compared and contrasted those proposals with HCR 5027 and with other property tax relief mechanisms under consideration in Kansas and in other states.

The Director of Property Valuation explained to the Committee how local property taxes and budgets are set; and how property taxes tend to shift when the tax base is narrowed or when certain classes or subclasses of property are granted tax-favored treatment.

During the public hearing, no proponents appeared to request the

reintroduction of HCR 5027. Opponents included the League of Kansas Municipalities and Kansas Association of Counties.

CONCLUSIONS AND RECOMMENDATIONS

The Committee finds that a residential valuation cap such as the one proposed in 2006 HCR 5027 would tend to shift property taxes away from real estate where values are increasing rapidly and on to other real estate where values are not increasing at the rate of the cap. The Committee further finds that a property tax system with a valuation cap could be especially onerous for young families entering the housing market for the first time.

The Committee notes that these conclusions are strikingly similar to those made by the 1999 Special Committee on Assessment and Taxation.

The Committee therefore declines to reintroduce a proposed valuation cap constitutional amendment for consideration in 2007.