

Approved: 1/29/09  
Date

## MINUTES OF THE SENATE ASSESSMENT AND TAXATION COMMITTEE

The meeting was called to order by Chairman Les Donovan at 10:30 a.m. on January 21, 2009, in Room 535-N of the Capitol.

All members were present except:  
Senator Derek Schmidt- excused

Committee staff present:  
Chris Courtwright, Kansas Legislative Research Department  
Gordon Self, Office of the Revisor of Statutes  
Virginia Fett, Office Assistant

Conferees appearing before the committee:  
Whitney Damron

Others attending:  
See attached list.

Chairman Donovan welcomed everyone to the committee. He opened the meeting with bill introductions.

Richard Cram spoke on behalf of the Governor introduction of a bill to amend KSA 79-41a03 and repeal 79-41a04 and 79-41a05 so that starting the fiscal year 2010 the liquor drink tax revenues currently going to local governments would, instead, be deposited and stay in State General Fund. Sen. Brownlee asked if doing this would impact local governments. Yes, it would. Chairman Donovan asked if there were any objections to accepting the bill. Seeing none, he said he would get the bill drafted. (Attachment 1)

He also had two bill requests on behalf of the Department of Revenue. First would clarify the income tax refund statute of limitations by amending 79-3230 in paragraphs C, F, and G. The other request is to add language to the Liquor Enforcement Tax Act that would require that retail licensees file and pay the taxes as required. The amendment is requested to clarify. That will not impact local government. Motion was made to accept the request to make bills to do this was made by Sen. Lynn; Sen. Holland seconded the motion. Motion passed. (Attachment 2)

Sen. Barnett explained Lyon County residents passed a one cent sales tax, however they exceeded their authority and need to add them to a list of other counties who have also done this. Sen. Colyer moved the bill be accepted; Sen. Apple seconded the motion. The motion passed.

Whitney Damron requested another bill. SB 487 from last year was passed. This request would clarify that bill. Sen. Brownlee moved the motion to accept; Sen. Apple seconded. Motion carried. (Attachment 3)

No other people were present to request other bills.

Chris covered the subjects in the interim committee. He distributed all ten committee reports from that committee. The topics studied were: Slider Formula; Sales Tax – Telecommunications; Property Tax Relief for Seniors; Taxation of Watercraft; Coalbed Methane; Local Bonded Indebtedness; Gas Severance Tax; Mill Levy Issues; Aerospace Engineer Credits; and Net Operating Loss Carrybacks. (Attachment 4)

Chairman Donovan closed this meeting and advised the committee to watch their Journals for scheduling of the next meeting. He will schedule it when the bills are printed and available.

The meeting was adjourned at 11:24 a.m.







Kathleen Sebelius, Governor  
Joan Wagnon, Secretary

www.ksrevenue.org

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Senate Committee on Assessment and Taxation

Joan Wagnon

January 21, 2009

**Request for Introduction of Governor's Proposal**

Senator Donovan, Chair, and Members of the Committee:

On behalf of the Governor, the Department respectfully requests introduction of a bill amending K.S.A. 2008 Supp. 79-41a03 and repealing K.S.A. 79-41a04 and 79-41a05 so that, effective beginning in fiscal year 2010 and thereafter, all liquor drink tax revenue currently being distributed to local governmental entities would instead be deposited and remain in the State General Fund.

OFFICE OF THE SECRETARY  
DOCKING STATE OFFICE BUILDING, 915 SW HARRISON ST., TOPEKA  
Voice 785-296-3041 Fax 785-296-7928 <http://www.k>

Senate Assessment and Taxation  
JANUARY 21, 2009  
Attachment 1

Senate Committee on Assessment and Taxation

Richard Cram

January 21, 2009

**Request for Introduction of Department Legislative Proposals**

Senator Donovan, Chair, and Members of the Committee:

The Department respectfully requests introduction of the following bills:

Clarification of the Income Tax Refund Statute of Limitations

The Department proposes amendments to K.S.A. 2008 Supp. 79-3230 to make clear the statutory deadlines for filing income tax refund claims. Recent opinions issued by the Court of Appeals, *In re Appeal of Lemons*, Docket No. 98,468 (filed September 19, 2008) and the Court of Tax Appeals, *In re Appeal of McColley*, Docket No. 2008-957-DT (filed September 24, 2008), have created confusion in identifying the appropriate statute of limitations for income tax refund claims. Under these interpretations, taxpayers ignoring statutory deadlines are actually better off than taxpayers who complied with them. The Department seeks the amendments to eliminate the compliance disincentive and confusion now existing for the taxpayer, tax practitioners, and the Department, as a result of these 2 opinions.

Add Provision Requiring Timely Payment of Liquor Enforcement Tax

The Department seeks to add specific statutory language to the Liquor Enforcement Tax Act requiring that retail licensees timely file and pay their liquor enforcement taxes as required by K.S.A. 79-4101. That would make it clear that failure to file or pay the taxes would be a violation of the Act subject to administrative action (fine, suspension or revocation) by the Director of Alcohol Beverage Control.



**REQUEST FOR BILL INTRODUCTION**

TO: The Honorable Les Donovan, Chair  
And Members of the Senate Committee on Assessment and Taxation

FROM: Whitney Damron  
On Behalf of:

- Flint Oak, LLC
- Kansas Sport Hunting Association
- 

RE: Sales Taxes on Hunting & Fishing Guide Services, Leases and Game Birds

DATE: January 21, 2009

Good morning Chairman Donovan and Members of the Senate Committee on Assessment and Taxation. My name is Whitney Damron and I appear before you today to request introduction of legislation clarifying the application of sales tax collections on guide services and land leases utilized for hunting and fishing and the retail sale of game birds for hunting purposes.

Flint Oak, LLC is a world-class hunting and shooting facility located in Elk County, Kansas approximately 80 miles east of Wichita.

[www.flintoak.com](http://www.flintoak.com)

The Kansas Sport Hunting Association is a non-profit association of hunting service professionals and game bird producers working together to promote sport hunting, shooting sports and game bird production in our state.

[www.huntkansas.org](http://www.huntkansas.org)

Those of you who were in the Senate last year may recall SB 487 that proposed similar clarifications of tax law in our state. Although that bill was not approved by the Legislature, it was adopted by both the Senate (40-0) and the House, although in separate pieces of legislation. In the end, the contents of SB 487 were not included in the House and Senate Tax Conference Committee Report.

However, the Secretary of Revenue subsequently issued Notice 08-01 effectively staying the imposition of a sales tax on charges for participation in guided and non-guided hunts and the sale of game birds for a period of one year to allow the Legislature to revisit this matter in 2009. Notice 08-01 is scheduled to expire on May 6, 2009 (copy attached).

The Kansas Sport Hunting Association and Flint Oak both believe this legislation is clarifying in nature, rather than substantive. For our 2009 proposal, we have deleted the reference to any exemption for clay target shooting and instead focused our proposal specifically on the issues that led to this legislation in the first place: Whether guide services, hunting and fishing leases and game bird sales consumed in hunts were subject to state and local sales taxes.

Attached to this request is a copy of the pertinent pages from SB 487 from the 2008 session.

On behalf of Flint Oak, LLC and the Kansas Sport Hunting Association, we thank you for your consideration of our request and look forward to providing additional testimony during the committee hearing process.

WBD  
Attachment

May 7, 2008

Notice 08-01

**Sales Tax Treatment of Charges for Participation in Guided and Non-guided  
Hunting and Retail Sale of Game Birds**

**This notice is to advise that the Department is currently reviewing its interpretation on the sales tax treatment of charges for guided and non-guided hunts, and on the retail sale of game birds. Effective May 7, 2008 through May 6, 2009, the Department is suspending enforcement of collection of sales tax on charges for participation in guided or non-guided hunts, and on the retail sale of game birds.**

In Revised Notice 07-08 dated February 4, 2008, the Department stated its interpretation that the gross receipts derived from the participation in guided and non-guided hunts are subject to Kansas retailers' sales tax, pursuant to K.S.A. 79-3603(m). During the 2008 Legislative Session, legislation was introduced that would exempt such gross receipts from sales tax. Although no such legislative was enacted, the Department is in the process of reviewing its interpretation. During such review and effective May 7, 2008 through May 6, 2009, subject to any legislative action taken during the 2009 Legislative Session, the Department will not enforce collection of sales tax on the gross receipts derived from the participation in guided and non-guided hunts, and on the retail sale of game birds. Any sales tax on such gross receipts already collected or remitted to the Department as of May 6, 2008 shall be deemed lawfully paid and shall not be refunded.

Taxable sales of meals, tangible personal property and lodging do not fall within the Department's forbearance on enforcement, and collection and remittance of applicable sales tax on those items should continue.

Questions concerning this notice may be directed to Policy & Research, telephone number 785-296-3081.



*As Amended by Senate Committee*

Session of 2008

**SENATE BILL No. 487**

By Committee on Assessment and Taxation

1-28

10 AN ACT concerning sales taxation; relating to imposition of tax; hunting  
11 **and fishing** and sale of game birds; amending K.S.A. 2007 Supp. 79-  
12 3603 and 79-3606 and repealing the existing sections.

13

14 *Be it enacted by the Legislature of the State of Kansas:*

15 Section 1. K.S.A. 2007 Supp. 79-3603 is hereby amended to read as  
16 follows: 79-3603. For the privilege of engaging in the business of selling  
17 tangible personal property at retail in this state or rendering or furnishing  
18 any of the services taxable under this act, there is hereby levied and there  
19 shall be collected and paid a tax at the rate of 5.3%. Within a redevelop-  
20 ment district established pursuant to K.S.A. 74-8921, and amendments  
21 thereto, there is hereby levied and there shall be collected and paid an  
22 additional tax at the rate of 2% until the earlier of the date the bonds  
23 issued to finance or refinance the redevelopment project have been paid  
24 in full or the final scheduled maturity of the first series of bonds issued  
25 to finance any part of the project upon:

26 (a) The gross receipts received from the sale of tangible personal  
27 property at retail within this state;

28 (b) the gross receipts from intrastate, interstate or international tel-  
29 ecommunications services and any ancillary services sourced to this state  
30 in accordance with K.S.A. 2007 Supp. 79-3673, and amendments thereto,  
31 except that telecommunications service does not include: (1) Any inter-  
32 state or international 800 or 900 service; (2) any interstate or international  
33 private communications service as defined in K.S.A. 2007 Supp. 79-3673,  
34 and amendments thereto; (3) any value-added nonvoice data service; (4)  
35 any telecommunication service to a provider of telecommunication serv-  
36 ices which will be used to render telecommunications services, including  
37 carrier access services; or (5) any service or transaction defined in this  
38 section among entities classified as members of an affiliated group as  
39 provided by section 1504 of the federal internal revenue code of 1986, as  
40 in effect on January 1, 2001;

41 (c) the gross receipts from the sale or furnishing of gas, water, elec-  
42 tricity and heat, which sale is not otherwise exempt from taxation under  
43 the provisions of this act, and whether furnished by municipally or pri-

1 dyeing and laundry services except laundry services rendered through a  
2 coin-operated device whether automatic or manually operated;

3 (j) the gross receipts from the rendering of the services of washing  
4 and washing and waxing of vehicles;

5 (k) the gross receipts from cable, community antennae and other sub-  
6 scriber radio and television services;

7 (l) (1) except as otherwise provided by paragraph (2), the gross re-  
8 cepts received from the sales of tangible personal property to all con-  
9 tractors, subcontractors or repairmen for use by them in erecting struc-  
10 tures, or building on, or otherwise improving, altering, or repairing real  
11 or personal property.

12 (2) Any such contractor, subcontractor or repairman who maintains  
13 an inventory of such property both for sale at retail and for use by them  
14 for the purposes described by paragraph (1) shall be deemed a retailer  
15 with respect to purchases for and sales from such inventory, except that  
16 the gross receipts received from any such sale, other than a sale at retail,  
17 shall be equal to the total purchase price paid for such property and the  
18 tax imposed thereon shall be paid by the deemed retailer;

19 (m) the gross receipts received from fees and charges by public and  
20 private clubs, drinking establishments, organizations and businesses for  
21 participation in sports, games and other recreational activities, but such  
22 tax shall not be levied and collected upon the gross receipts received from:

23 (1) Fees and charges by any political subdivision, by any organization  
24 exempt from property taxation pursuant to paragraph *Ninth* of K.S.A. 79-  
25 201, and amendments thereto, or by any youth recreation organization  
26 exclusively providing services to persons 18 years of age or younger which  
27 is exempt from federal income taxation pursuant to section 501(c)(3) of  
28 the federal internal revenue code of 1986, for participation in sports,  
29 games and other recreational activities; ~~and~~ (2) entry fees and charges for  
30 participation in a special event or tournament sanctioned by a national  
31 sporting association to which spectators are charged an admission which  
32 is taxable pursuant to subsection (e); ~~and~~ (3) *fees and charges for partic-*  
33 *ipation in guided and non-guided hunts and fees and charges for sporting*  
34 *clays fishing expeditions and excursions, ~~clay shooting sports and~~*  
35 *hunting or fishing leases;*

36 (n) the gross receipts received from dues charged by public and pri-  
37 vate clubs, drinking establishments, organizations and businesses, pay-  
38 ment of which entitles a member to the use of facilities for recreation or  
39 entertainment, but such tax shall not be levied and collected upon the  
40 gross receipts received from: (1) Dues charged by any organization ex-  
41 empt from property taxation pursuant to paragraphs *Eighth* and *Ninth* of  
42 K.S.A. 79-201, and amendments thereto; and (2) sales of memberships  
43 in a nonprofit organization which is exempt from federal income taxation

1 (zzz) all sales of tangible personal property purchased by the rotary  
2 club of shawnee foundation which is exempt from federal income taxation  
3 pursuant to section 501 (c)(3) of the federal internal revenue code of  
4 1986, as amended, used for the purpose of providing contributions to  
5 community service organizations and scholarships; ~~and~~

6 (aaaa) all sales of personal property and services purchased by or on  
7 behalf of victory in the valley, inc., which is exempt from federal income  
8 taxation pursuant to section 501 (c)(3) of the federal internal revenue  
9 code, for the purpose of providing a cancer support group and services  
10 for persons with cancer, and all sales of any such property by or on behalf  
11 of any such organization for any such purpose; *and*

12 *(bbbb) all sales of game birds the primary purpose of which is use in*  
13 *hunting.*

14 Sec. 3. K.S.A. 2007 Supp. 79-3603 and 79-3606 are hereby repealed.

15 Sec. 4. This act shall take effect and be in force from and after its  
16 publication in the statute book.

**Report of the  
Special Committee on Assessment and Taxation  
to the  
2009 Kansas Legislature**

**CHAIRPERSON:** Representative Kenny Wilk

**VICE-CHAIRPERSON:** Senator Les Donovan

**RANKING MINORITY MEMBER:** Representative Stan Frownfelter

**OTHER MEMBERS** Senator Pat Apple, Karin Brownlee, Janis Lee, and Derek Schmidt;  
Representative Sydney Carlin, Steve Lukert, John Grange, Jeff King, Bill Light, and Ron  
Worley

**STUDY TOPICS**

- Certain Tax Distributions (“Slider”) for Local Unites of Government.
- Sales Tax Refunds for Certain Telecommunications Machinery and Equipment.
- Review of Existing Programs for Property Tax Relief for Seniors.
- Taxation of Watercraft.
- Coalbed Methane Tax Structure.
- Local Units of Government Bonded Indebtedness.
- Gas Severance Tax.
- Mill Levy Issues for Certain Tax Jurisdictions.
- Attracting Aerospace Engineers.
- Modifying the Net Operating Loss Deduction for Kansas Income Tax Purposes.

*December 2008*

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Senate Assessment and Taxation

JANUARY 21, 2009

Attachment 4

# Special Committee on Assessment and Taxation

## SLIDER FORMULA

### CONCLUSIONS AND RECOMMENDATIONS

While sympathetic to some concerns expressed, the Committee observes that many taxing subdivisions received slider distribution payments in 2008, without any apparent complaints. The Committee asks the standing tax committees to continue to monitor future slider distributions.

The Committee also strongly recommends that the 2009 Kansas Legislature continue to fully fund all slider payments, as well as Local Ad Valorem Tax Reduction Fund (LAVTRF) payments, to local units.

*Proposed Legislation:* None.

### BACKGROUND

#### Machinery and Equipment Exemption and Slider Provisions – 2006

During the 2006 session, the Legislature enacted HB 2583, which provided a property tax exemption for certain pieces of commercial and industrial machinery and equipment; and a formula (the “slider”) designed to reimburse local units of government for a portion of the lost revenues.

The bill provided a property tax exemption for:

- Certain commercial and industrial, railroad, and telecommunications machinery and equipment; acquired by qualified purchase or lease after June 30, 2006 as the result of bona fide transactions not consummated for the purpose of avoiding taxation; and
- Such machinery and equipment transported into the state after June 30, 2006 to expand existing businesses or create new

businesses.

Relative to the slider provisions, the bill created two new funds within the state treasury, the Business Machinery and Equipment Tax Reduction Assistance Fund (BMETRAF); and the Telecommunications and Railroad Machinery and Equipment Tax Reduction Assistance Fund (TRMETRAF). These funds provide a mechanism whereby taxing subdivisions were to be reimbursed beginning in February, 2008 for certain property tax reductions assumed attributable to the exemptions.

The Secretary of Revenue is required to compute for each county an amount equal to the difference in machinery and equipment property taxes levied in tax year 2005 and various future tax years (beginning with tax year 2007). Based upon this computation, county treasurers were to receive 90 percent of the difference for tax year 2007; 70 percent for tax year 2008; 50 percent for tax year 2009; 30 percent for tax year 2010; and 10 percent for tax year 2011. (The transfers

from the state to counties therefore were to be made during FY 2008-2012).

Under the initial provisions of HB 2583, county treasurers would have been required to apportion the BMETRAF and TRMETRAF funds among taxing subdivisions (including the state) relative to their respective shares of property tax levies. (This secondary distribution formula was subsequently amended in 2007 prior to the initial distribution in 2008.)

The Secretary also is required to make an annual report to the standing tax committees on the BMETRAF and TRMETRAF computation methodologies.

#### Slider Provisions Amended – 2007

During the 2007 session, HB 2044 made several amendments to the distribution formula relating to “slider” replacement revenues for local units of government designed to help mitigate the commercial and industrial machinery and equipment property tax exemption enacted in 2006. One amendment provided that the secondary distribution formula, which relates to the amounts that county treasurers distribute to each taxing subdivision, was to be based directly upon the amount of reduced property taxes from commercial and industrial machinery and equipment within each subdivision. (The initial distribution formula, which relates to the amounts distributed from the state to each county, also is based directly on the amount of reduced taxes from this subclass of property within each county.)

Additional language clarified that the amount of current property taxes attributable to property which had been abated or exempted prior to July 1, 2006, would not count against counties for purposes of qualifying for the replacement revenue payments from the state. (An annual report prepared by the Secretary of Revenue also will be required to quantify the impact of this amendment.)

Another provision clarified that the slider formula is to be tied to certifications of commercial and industrial machinery and equipment property taxes made by county clerks on or before November 15 of each tax year. Finally, an additional provision clarified that the formula relates only to changes in machinery and equipment property taxes and not to overall property taxes.

#### Interim Study Request

After the initial slider distributions were made early in 2008, several concerns were expressed, especially in Lyon County, that county treasurers had not necessarily interpreted the provisions of the secondary distribution formula correctly. Senator Barnett requested an interim study, and the Legislative Coordinating Council agreed, charging the Special Committee with reviewing the secondary distribution formula for slider payments by counties to other local units of government; studying whether the proper distribution to local units of government is being made; and recommending if there should be additional state oversight to assure compliance with the statutory formula. The Committee is further charged with reviewing the overall equity of the slider formula and make any recommendations deemed appropriate to the 2009 Legislature.

### COMMITTEE ACTIVITIES

At the September meeting, staff from the Property Valuation Division gave an overview of the slider reimbursements made to the counties for 2007 and the calculations of the payments. The total amount of reimbursements for the first year was \$25,860,360.

A conferee representing the city of Emporia said that officials in that city believed that the distribution formula had created unintended consequences. He argued that slider monies should not be distributed to certain entities

(such as libraries and recreation commissions) which rely on other taxing subdivisions to make property tax levies on their behalf. He also said that the distribution formula should be based upon change in estimated assessed valuation instead of change in property tax levies. Finally, he suggested that the Legislature consider earmarking the slider funds for only those taxing jurisdictions like cities and counties that provide services such as police and fire protection for businesses.

A conferee representing the city of Atchison said that there needed to be additional state oversight to assure compliance with the proper distribution of slider funds within the counties. His review of the slider indicated that the amount of the slider was correctly calculated pursuant to K.S.A. 79-2978(b)(1), but was not distributed pursuant to K.S.A. 79-2978(e)(2). He also said that he would have preferred the Legislature to provide the tax relief via a refundable income tax credit instead of narrowing the property tax base and causing tax shifts on to other classes of property.

The executive director of the Kansas Association of Counties said that it was critical

for the Legislature to continue to make the slider payments, as promised when the machinery and equipment property tax exemptions were enacted by the 2006 Legislature. He also said that the Kansas Association of Counties was not aware of any reason to require additional state oversight of county treasurers' distribution of slider payments.

## CONCLUSIONS AND RECOMMENDATIONS

While sympathetic to some of the concerns expressed by conferees, the Committee observes that many thousands of taxing subdivisions received slider distribution payments in 2008 without any apparent complaints. The Committee asks the standing tax committees to continue to monitor future distributions relative to additional concerns.

The Committee also strongly recommends that the 2009 Kansas Legislature continue to fully fund all slider payments, as well as LAVTRF payments, to local units of government.

# Special Committee on Assessment and Taxation

## SALES TAX—TELECOMMUNICATIONS

### CONCLUSIONS AND RECOMMENDATIONS

The Committee finds that the telecommunications industry is a critical partner in the state's economic development efforts. The Committee believes that authorizing sales tax refunds for certain telecommunications-related purchases will continue to encourage much needed investment.

The Committee therefore recommends introduction of a bill that would phase in the refunds from FY 2012 to FY 2016. The Committee requests that this legislation be introduced as a House bill.

***Proposed Legislation:*** The Committee recommends the introduction of one bill on this topic.

### BACKGROUND

During the 2007 and 2008 session, representatives of the telecommunications industry supported various versions of legislation (HB 2288, HB 2412, HB 2762, and SB 664) that would have provided for refunds of all or a portion of state sales or use taxes paid on certain telecommunications machinery and equipment. One derivative of that proposal ultimately was approved by the Legislature but vetoed by the Governor as part of Senate Sub. for HB 2412, the Economic Stimulus Act of 2008.

Under the provisions relating to telecommunications machinery and equipment, refunds would have been authorized equivalent to 20 percent of such amount paid during FY 2012; 40 percent during FY 2013; 60 percent in FY 2014; 80 percent in FY 2015; and 100 percent in FY 2016 and thereafter. Local sales taxes paid would not have been refunded, and taxpayers would have had to submit refund claims within one year.

The fiscal note for the sales tax refund for telecommunications machinery and equipment was estimated to be a reduction of revenue of \$3.3 million in FY 2012 and a reduction of \$6.5 million revenue in FY 2013; \$9.8 million in FY 2014; \$13.0 million in FY 2015; and \$16.3 million in FY 2016.

The Senate approved the bill 24-10 on May 6, and the House approved it 76-48 on May 7. The Governor vetoed the legislation on May 16. The Governor observed in her veto message that she had been working with the telecommunications industry to enhance investment in Kansas; and that she hoped both she and the Legislature would have the opportunity to consider various proposals "on their own merit" in the future.

In August, the Legislative Coordinating Council, at the suggestion of Representative Wilk, assigned the sales tax refund issue to the Special Committee on Assessment and Taxation. The Committee is charged to study the proposed telecommunications sales tax refunds as an



equity issue relative to the current exemption for manufacturing machinery and equipment, review the relevant provisions of Senate Sub. for HB 2412, and make any recommendations deemed appropriate to the 2009 Legislature.

### COMMITTEE ACTIVITIES

At the September meeting, staff briefed the Committee on the history of the various proposals in 2007 and 2008 that would have provided for state sales tax refunds on telecommunications machinery and equipment purchases. Mark Beshears, representing Sprint/Nextel and others in the industry, said that the refunds would result in significant new investment and new jobs in the state. In response to a question, he said that the equipment purchases relating to broadband speed definitely need to qualify for the refunds.

The Chair asked the Department of Revenue to report back at the October meeting regarding the official position of the administration on the proposal heading in to the 2009 session. The Committee also asked the Department to provide any data they might have as to the extent to which sales of telecommunications machinery and equipment were stimulated on and after July 1, 2006, as a result of the property tax exemption for newly acquired or purchased business machinery and equipment.

At the October meeting, Secretary Wagon explained the position of the administration and noted that some sort of analysis would need to

be performed relative to the upcoming revenue estimates, the overall state budget picture, and the benefit that would be gained by providing the sales tax refunds before the Governor would commit to supporting the legislation in 2009.

### CONCLUSIONS AND RECOMMENDATIONS

The Committee finds that the telecommunications industry is a critical partner in the state's economic development efforts. The Committee strongly believes that authorizing state sales tax refunds for certain telecommunications machinery and equipment purchases will continue to encourage much-needed investment in Kansas.

The Committee therefore recommends introduction of a bill containing provisions similar to those of Senate Sub. For HB 2412 relative to such refunds that proposes to phase in the refunds from FY 2012 to FY 2016. The Committee requests that this legislation be introduced as a House bill.

# Special Committee on Assessment and Taxation

## PROPERTY TAX RELIEF FOR SENIORS

### CONCLUSIONS AND RECOMMENDATIONS

The Committee encourages the Department of Revenue to report to the Legislature on the effectiveness of the senior property tax relief programs. The Committee notes that any effort to evaluate the SAFE Senior program cannot occur until taxpayers have had several years of experience with the new credit. The Legislature also should continue to study the structure of similar programs in other states.

Should the fiscal cost need to be reduced, the Committee recommends a reduction of the \$350,000 valuation cap currently applicable for the Homestead and SAFE Senior credits.

Finally, the Committee applauds the development of software helping taxpayers distinguish which credit program will be most beneficial. The Committee asks that local officials also continue to advise senior taxpayers about these programs.

*Proposed Legislation:* None.

### BACKGROUND

During the 2008 Session, a new property tax relief program was approved as part of 2008 Senate Sub. HB 2434, the Selective Assistance for Effective Senior Relief ("SAFE Senior") income tax credit, which now joins the longstanding Homestead Property Tax Refund Act as another methodology for helping to reduce the burden on certain taxpayers. Another proposal, which would have established a property tax deferral program, was approved by the House but ultimately not enacted.

At the request of the tax conference committee, the Legislative Coordinating Council subsequently approved a charge for the Special Committee to study the current property tax relief programs for senior citizens, including the Homestead Program and SAFE Senior credit;

to further study the need for a separate property tax deferral program such as the one approved by the House in 2008. The Committee is asked to review the effectiveness and equity of the current programs and of any new proposals; and to determine if the Department of Revenue should provide annual reports to the Legislature on participation, costs, and effectiveness of the various programs. Finally, the Committee is asked to make any recommendations deemed appropriate to the 2009 Legislature.

### Homestead Program

Kansas in 1970 enacted the Homestead Property Tax Refund Act, KSA 79-4501 *et seq*, which is best characterized as the "circuit-breaker" style of property tax relief program. A "circuit breaker" is a form of property tax relief in which the benefit is dependent on income or

other criteria and the amount of property taxes paid. The moniker developed as analogy to the device that breaks an electrical circuit during an overload, just as the property tax relief benefit begins to accrue once a person's property taxes have become overloaded relative to his or her income.

The first property tax circuit breaker was enacted by Wisconsin in 1964. Kansas became the sixth state with such a program in 1970. According to the National Conference of State Legislatures (NCSL), 34 states currently have some form of circuit breaker program. Of these states, 27 (including Kansas) also allow renters to participate in the programs (based on the assumption that landlords are passing increased property taxes along in the form of higher rent).

The current Kansas program requires participants to meet both an income and a demographic test. The former test requires that household income be not more than \$29,700; the latter requires that at least one person in the household be (1) age 55 or above; (2) a dependent under age 18; (3) blind; or (4) otherwise disabled. Homeowners with a residence valued at \$350,000 or more may not participate in the program. Renters are eligible based on the statutory assumption that 15 percent of their rent is equivalent to property taxes paid.

The program most recently underwent expansions in both 2006 and 2007, the latter of which increased the fiscal impact by almost \$10 million largely as a result of legislation that allows 50 percent of Social Security benefits to be excluded from the definition of household income.

The following table shows a history of Homestead claims in recent years:

	Eligible Claims Filed	Amount (in millions)	Average Refund
FY 2006	72,927	\$16.643	\$229
FY 2007	79,661	\$21.220	\$265
FY 2008	96,020	\$31.127	\$324

### SAFE Senior Tax Credit Provisions

As noted earlier, the 2008 Legislature enacted the SAFE Senior Act, which will provide a refundable income tax credit beginning in tax year 2008 that will now be available to certain senior citizens to help reimburse a portion of property taxes paid on their homesteads.

Those taxpayers age 65 or older with household income of 120 percent or less of the federal poverty level for two persons (currently \$16,800) are eligible to claim the tax credit, which is equivalent to 45 percent of property taxes actually and timely paid on real or personal property used for residential purposes which was also their principal place of residence. Beginning in tax year 2011, the credit is increases to 75 percent of such amount.

The SAFE Senior credit is deemed supplemental to the Homestead Property Tax Refund Act, and taxpayers may not claim the credit for a given tax year if they have also claimed a Homestead refund.

Estimates are that \$2.040 million in SAFE Senior credits will be claimed in FY 2009; and \$3.400 million beginning in FY 2012 (when the credit increases to 75 percent).

### Property Tax Deferral Program

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 both 1990 and 2008 that would have established a Kansas deferral program for certain low income taxpayers who were age 65 and above.

Following a favorable recommendation by the 2007 Special Committee on Assessment and Taxation regarding the need for a deferral program, HB 2928 was introduced in 2008. That legislation ultimately was approved by the House on a vote of 93-32 on April 2.

HB 2928, as amended, would have enacted the Senior Citizen Property Tax Deferral Act (SCPTDA), a program which would have allowed certain taxpayers at least 65 years of age by December 31 to defer all or a portion of property taxes on their homestead property. The SCPTDA would have been effective for tax years 2009 to 2013, at which point the law would have sunset.

Eligible taxpayers would have been required to file claim forms along with their state income tax returns on or before April 15 of each year for which they are seeking the deferrals. Once deferrals became valid and allowed claimants to defer property taxes for a given tax year, they also would have created a lien against the homestead property for the taxes deferred. A lien established for deferred taxes and accrued interest (at the rate prescribed by KSA 79-2968) would have been filed in a qualifying taxpayer's county of residence. These liens would have been subordinate to any mortgage or deed of trust recorded prior to the date on the deferral certificate. The liens would have had priority over any other liens that attached after the date on the certificate.

The bill would have allowed the deferral to be claimed by the taxpayer, his or her guardian, the conservator, or the attorney-in-fact. Qualifications for the deferral would have included:

- The taxpayer must have total household income of \$60,000 or less;
- The property must be the homestead of the taxpayer claiming the deferral;
- The taxpayer must have resided in the homestead for at least 10 years;
- The taxpayer must own or jointly own the property;
- The property cannot be income-producing;
- The total unpaid balances of debts secured by mortgages and other liens on the property could not exceed 50 percent of its appraised value;
- All real property taxes for previous years must have been paid; and
- The property must be insured.

The Pooled Money Investment Board would have loaned to the Department of Revenue sufficient funds to cover the amount of deferred property taxes. Such amounts subsequently would have been paid to the appropriate county treasurers for distribution to taxing subdivisions in the same manner as general property taxes. Once the payment was made to the county treasurer, the right to receive payment for the deferred taxes and accrued interest and to enforce the lien created by the deferral would have been vested in the Department of Revenue.

In the event payment of deferred taxes and interest was paid to a county treasurer, the county treasurer would have been required to accept the payment and remit the money to the Department of Revenue. Upon receipt of this money, the Department would have been required to issue a release of the tax deferral lien.

Deferred taxes and accrued interest generally would have become payable when:

- The taxpayer claiming the deferral dies;
- The property for which the taxes have been deferred is sold or becomes subject to a contract for sale or title transfers to someone else;
- The property is no longer the homestead of the taxpayer, except in cases where the taxpayer for reasons of ill health is not able to live in the property; or
- The property no longer meets the eight aforementioned qualifying requirements for deferral.

An exception to these circumstances that would otherwise have triggered the deferred taxes and accrued interest to become payable would have been provided for spouses who are age 60 or older.

The Secretary of Revenue would have been required to submit an annual report to the Governor and the Legislature regarding the SCPTDA.

### COMMITTEE ACTIVITIES

At the October meeting, staff outlined the history of the Homestead and SAFE Senior credits and the property tax deferral program that had passed the House in 2008. Staff also presented a table comparing and contrasting features of all three programs.

The Department of Revenue demonstrated some new software that will help people determine which tax credit would be most advantageous to claim. The Committee also received testimony

from AARP indicating renewed support for the property tax deferral legislation.

### CONCLUSIONS AND RECOMMENDATIONS

The Committee encourages the Department of Revenue to report to the Legislature annually on the costs, participation, and effectiveness of the senior property tax relief programs. The Committee notes that any meaningful effort to evaluate the effectiveness of the SAFE Senior program cannot occur until taxpayers have had several years of experience with the new credit. The Legislature also should continue to study the structure of senior tax relief programs in other states.

Should the fiscal cost associated with the Kansas programs need to be reduced, the Committee recommends that the standing tax committees consider reducing the \$350,000 valuation cap currently applicable for the Homestead and SAFE Senior credits.

Finally, the Committee applauds the Department of Revenue's efforts to develop software helping taxpayers distinguish which credit program will be most beneficial. The Committee asks that county clerks and other officials also continue to advise senior taxpayers about these programs.

# Special Committee on Assessment and Taxation

## TAXATION OF WATERCRAFT

### CONCLUSIONS AND RECOMMENDATIONS

The Committee agrees with concerns expressed by several legislators and conferees indicating that Kansas may need to restructure boat taxes on a basis other than fair market value. The Committee therefore recommends introduction of a constitutional amendment similar to HCR 5015, to be placed on the August ballot in 2010.

The Committee further encourages Secretary Wagnon to work with the standing tax committees regarding the development of a potential new tax system with an eye towards being able to administer any such system on the new VIPS program.

**Proposed Legislation:** The Committee recommends introduction of one proposed constitutional amendment on this topic.

### BACKGROUND

During the 2008 Session, the House approved and sent to the Senate a proposed constitutional amendment, HCR 5015, that, if adopted by the voters, would have authorized the Legislature to classify watercraft on a different basis from other property. (Watercraft is currently assessed as “all other” personal property at 30 percent of its fair market value.) The authorization would have been effective as early as tax year 2009.

HCR 5015 was referred to the Senate Committee of the Whole in early April but was not subsequently acted on by the Senate.

Representative Bowers asked the Legislative Coordinating Council (LCC) for an interim study on the issue, and the LCC agreed, charging the Special Committee on Assessment and Taxation with reviewing the property tax burden on watercraft and the policy implications associated with HCR 5015. The Special Committee is further charged with making any recommendations deemed appropriate to the 2009 Legislature.

During a 1998 interim study, PVD conducted a survey of 85 counties and reported that there was about \$48.6 million in assessed valuation attributable to watercraft; and about \$5.5 million in property tax liability. The Secretary of Wildlife and Parks also reported at that time that there were over 100,000 watercraft registered in Kansas, a figure far in excess of the amount actually on the property tax rolls.

After a legislative authorization for a new tax system for “recreational vehicles” was adopted as part of a constitutional amendment in 1992, the Legislature in 1994 availed itself of this constitutional prerogative and enacted a new system for such vehicles under which liability since January 1, 1995 has been based on the weight and the age of the vehicles (rather than on fair market value.)

Proponents of a similar system for boats saw another constitutional amendment narrowly defeated at the polls in 2000 (SCR 1629) that would have authorized new tax treatment for both boats and aircraft. The Kansas Secretary of

State's office indicates that the amendment had been defeated by less than 12,000 votes (433,499 "no" to 421,621 "yes").

### COMMITTEE ACTIVITIES

At the September meeting, staff outlined the issue and explained that one key question that would need to be addressed before reintroducing the latest version of the amendment in 2009 would be whether to wait until 2010 to place it on the ballot or to seek a special election in 2009.

Among the conferees appearing in support of HCR 5015 was Representative Sharon Schwartz, who noted that Kansas may be losing revenue to the extent that boat owners have chosen to move their boats to surrounding states where taxes are lower. She also observed that under a new tax system, watercraft could be more easily registered and taxed by counties using the Vehicle Information Processing System (VIPS), as opposed to the current fair market value methodology.

Representative Dale Swenson also reminded the Committee that the amendment would have no immediate fiscal impact unless and until the Legislature passed a law that changed the tax treatment of watercraft.

Representative Lee Tafanelli said that passing the amendment and lowering boat taxes would help stimulate the Kansas economy.

A representative of Wildlife and Parks explained that federal matching funds are made available to states based on boats' being registered in the "state of principal use". The definition of "state of principal use" is generally the state in which that boat will be during most of in a calendar year and does not necessarily relate directly to residency of the owners. The Committee asked the conferee to return at the October meeting to provide an update relative to

his study of the extent to which Kansas residents have boats registered in surrounding states.

At the October meeting, Secretary Wagon noted that it would be helpful to know prior to May of 2009 what sort of tax system the Legislature might choose to design as an alternative and whether such system could be incorporated within the new VIPS program.

A representative of Wildlife and Parks reminded the Committee that boat owners pay a boat registration tax in addition to property tax. He also said that 64 percent of the registered boats in Kansas are 13 years old or more, indicating that this could be a result of the property tax situs issue.

### CONCLUSIONS AND RECOMMENDATIONS

The Committee agrees with concerns expressed by several legislators and conferees indicating that Kansas may need to restructure boat taxes on a basis other than fair market value. The Committee therefore recommends introduction of a constitutional amendment similar to HCR 5015, to be placed on the August ballot in 2010.

The Committee further encourages Secretary Wagon to work with the standing tax committees regarding the development of a potential new tax system with an eye towards being able to administer any such system on the new VIPS program.

# Special Committee on Assessment and Taxation

## COALBED METHANE

### CONCLUSIONS AND RECOMMENDATIONS

The Committee finds that the current property tax valuation system for oil and gas has very high administrative costs for all parties involved.

The Committee believes that the current complexities contributed to a lack of equity for royalty interest owners of coalbed methane gas. The Committee therefore recommends that the standing tax committees continue to analyze ways to provide a reduced tax burden for royalty interest owners relative to working interest owners, including exempting coalbed methane production from property taxation and imposing a special severance tax that would fall more heavily on working interests.

*Proposed Legislation:* None.

### BACKGROUND

As a result of rapid expansion in recent years of coalbed methane gas production in the Cherokee Basin, especially in Wilson, Montgomery and Neosho counties, a number of legislators requested a study of how such property is valued for taxation purposes. The Legislative Coordinating Council therefore asked the Special Committee to review the current property tax structure on coalbed methane production and the assessment of working and royalty interest relative to such production; review how the Department of Revenue and county appraisers determine the value of income derived from coalbed methane gas production; and make any recommendations deemed appropriate to the 2009 Kansas Legislature.

According to the Kansas Geological Survey, total gas production in 2007 was 371 billion cubic feet. While the Hugoton and Pomona fields in western Kansas continued to account for the majority of the state's production (212 billion

cubic feet), approximately 33.5 billion cubic feet came from the Cherokee Basin and was largely attributable to coalbed methane production.

Production from coalbed methane leases in southeast Kansas generally differs from production in the Hugoton and older fields in other areas of the state because of the extent to which production continues to increase during the early years as water is pumped off.

Under the current provisions of the Kansas Constitution, gas leaseholds producing 100 mcf per day or less are assessed at 25 percent of fair market value for property tax purposes; and leases producing more than 100 mcf per day are assessed at 30 percent of fair market value.

### COMMITTEE ACTIVITIES

At the September meeting, a representative of the Kansas Division of Property Valuation (PVD) explained the current valuation methodology for natural gas property, citing KSA 79-329, which



provides that natural gas is to be taxed as personal property; and KSA 79-331, which requires appraisers to consider a number of factors, including the age and probable life of the wells, the quality and quantity of gas produced, the proximity to market, and the cost of operation.

PVD personnel went on to explain how once estimated gross reserve value is determined for each lease, the typical lease is then subsequently disaggregated into a working interest (7/8ths or 87.5 percent) and a royalty interest (1/8th or 12.5 percent). A hypothetical lease in the Hugoton field, where production peaks at the outset and then steadily declines, might see the working interest bear 86 percent of the tax burden compared to 14 percent for the royalty interest. But a hypothetical lease producing coalbed methane, because of the different production life cycle, might see the working interest bearing only 45 percent of the tax burden compared to 55 percent for the royalty interest.

Gary Davidson, a landowner in Montgomery County, agreed with the analysis from PVD and said that he thought working interest owners should bear a considerably higher burden during the early years of coalbed methane production. He also noted that gas companies are taking gathering costs, transportation costs, and line shrinkage adjustments out of landowners' royalty incomes.

The Kansas Independent Oil and Gas Association and the Eastern Kansas Oil and Gas Association said that the current valuation process used by PVD was a "fair and open" approach and did not think any changes were needed.

The Chair asked PVD and staff to think about whether some sort of different valuation methodology for coalbed methane gas as opposed to more traditional gas produced elsewhere in the state would violate the uniform and equal requirement in the Kansas Constitution. He wanted to know if the perceived equity issue

could be addressed by changing rules and regulations, statutes, or the Constitution.

The Chair also asked if better equity between the working and royalty interests could be achieved pursuant to a special severance tax as an alternative to the current property tax.

At the November meeting, the Committee received additional information from staff at the Department of Revenue indicating that any efforts to effectively amend the oil and gas appraisal guide in a way that would cause royalty interests to be valued at something other than fair market value likely would be unconstitutional.

## CONCLUSIONS AND RECOMMENDATIONS

The Committee finds that the current property tax valuation system for oil and gas has very high administrative costs for taxpayers and the government alike.

The Committee believes that the complexities of the current system have contributed to a significant lack of equity for royalty interest owners of coalbed methane gas. The Committee therefore recommends that the standing tax committees in 2009 continue to analyze ways to provide a reduced tax burden for royalty interest owners relative to working interest owners, including exempting coalbed methane production from property taxation and imposing a special "add-on" severance tax that would fall more heavily on working interests.

# Special Committee on Assessment and Taxation

## LOCAL BONDED INDEBTEDNESS

### CONCLUSIONS AND RECOMMENDATIONS

The Committee recommends that the debt limitation relating to cities be studied by the appropriate standing committees to determine if there is a uniformity issue that could give rise to the exercise of Home Rule powers. These findings with respect to uniformity should be reported to the standing taxation committees for future deliberation.

The Committee does not at this time recommend altering the debt limits or statutory language found in KSA 10-306 and 10-308.

*Proposed Legislation:* None.

### BACKGROUND

The Legislative Coordinating Council charged the 2008 Special Committee on Assessment and Taxation with examining the issue of bonded indebtedness at the local level. This charge includes a study of how the State of Kansas monitors bonded indebtedness, the current amount of bonded indebtedness carried by local units of government, and the amount of property tax resources pledged to satisfying the bonded indebtedness.

#### Debt Limits for Cities and Counties

Kansas law establishes limits on the amount of debt a city or county may acquire as a result of issuing bonds.

For counties, KSA 10-306 limits bonded indebtedness to 3 percent of the assessed value of all tangible taxable property within the county. However, two counties are exempt from these limits. KSA 10-306 has been amended to allow Wyandotte and Franklin Counties to issue bonds up to 30 percent of the county's assessed value.

For cities, KSA 10-308 limits bonded indebtedness to 30 percent of the assessed valuation of the city. The only municipality exempted from this limit is the city of Junction City. The debt limit on its government is set at 40 percent through FY 2011.

#### Monitoring Bonded Indebtedness

The State of Kansas has two primary methods for monitoring bonded indebtedness.

The first method is detailed in KSA 10-108. The statute requires local governments to submit to the State Treasurer a transcript of the proceedings leading up to the issuance of bonds. The transcript is then given to the Office of the Attorney General for approval. This process is intended to ensure that the sale of bonds complies with state law. If approval is granted, the sale then is registered with the State Treasurer.

The second method for monitoring debt is conducted solely by the State Treasurer. Each year, county clerks, as required in KSA 10-110, must submit to the Treasurer a figure identifying their county's total amount of debt. The figures

provided by the county clerks are broken down into broad categories, such as “Cities” or “Fire Districts,” for example, but the figures do not include the debt carried by an individual city within that county. As a result, all cities located within a given county are aggregated into a single figure.

While these are two methods by which the State monitors a local government’s debt, it is necessary to note that KSA 10-108 and KSA 10-110 represent the extent to which state agencies are involved. In one report, the process outline in KSA 10-108 was labeled “perfunctory” since local governments are given broad authority to enter into debt under Kansas Statute.

### **Current Levels of Debt**

According to figures provided by the State Treasurer’s Office, the amount of debt carried by cities, counties, and other local entities in Kansas totals \$18,660,721,680. Approximately half of the total debt results from the issuance of industrial revenue bonds with another \$3.7 billion coming from bonds issued by local school districts.

For the categories labeled “County General” and “Cities,” the amount of debt is \$650 million and \$2.58 billion, respectively.

### **Policy Considerations**

In a 2006 report prepared for Kansas Department of Revenue, local economists offered several policy recommendations relating to this issue. In total, the report titled “Kansas Local Government 2005 Debt Affordability Report” concludes that the State has numerous policies in place that adequately regulate local debt.

The report does, however, encourage policy makers to promote debt coordination between units of local government that share the same tax base. Also included in the recommendations is a call for increased transparency on the part of

local governments in communicating with their citizens.

## **COMMITTEE ACTIVITIES**

At the October meeting, an official with the Office of the State Treasurer provided the Committee with information detailing levels of bonded indebtedness. The official described the data collection process and distributed materials listing debt levels by local units of government. In response to the testimony, the Committee requested information from 1990-2007 showing the trend lines for Kansas’ debt levels, both locally and statewide.

In response to a question from the Committee, a representative from the Kansas League of Municipalities described the different types of bonds that can be issued by local governments and the situation in which those bonds are most commonly used.

The Committee requested a response from the Office of the Attorney General clarifying their role in collecting information from local governments prior to approving their request to issue bonds.

## **CONCLUSIONS AND RECOMMENDATIONS**

The Committee recommends that the debt limitation relating to cities be studied by the appropriate standing committees to determine if there is a uniformity issue that could give rise to the exercise of Home Rule powers. These findings with respect to uniformity should be reported to the standing taxation committees for future deliberation.

The Committee does not at this time recommend altering the debt limits or statutory language found in KSA 10-306 and 10-308.

# Special Committee on Assessment and Taxation

## GAS SEVERANCE TAX

### CONCLUSIONS AND RECOMMENDATIONS

The Committee finds that because of changes in the gas industry, the current severance tax law (written in the 1980s) has become increasingly difficult to administer. The Committee believes that a helpful dialogue has been created as a result of this study and encourages the industry and the Department of Revenue to continue to work on a solution for some of these complexities.

The Committee recommends that all parties continue to work on proposals which ideally could be implemented by rules and regulations (in lieu of statutory changes). All parties should report back to the standing tax committees by mid-February.

The Committee further finds that because of dramatic increases in the price of oil in recent years, it may no longer be prudent for 50 percent of oil production to be exempt from the state's severance tax. The Committee therefore encourages the 2009 Legislature to review the low-production exemption for oil.

*Proposed Legislation* None.

### BACKGROUND

In response to concerns expressed by various legislators in recent years regarding equity issues associated with the severance tax on natural gas, the Department of Revenue requested a review of the current tax structure. The Legislative Coordinating Council agreed and charged the Special Committee with exploring the advisability of changing the basis of the tax such that the wellhead value of natural gas for severance tax purposes would be calculated based on an index price that would adjust annually, similar to the methodology utilized in Louisiana.

The gas severance tax law imposes a severance tax on the gross value of natural gas at the time it leaves the lease at an effective rate of 4.33% (8% rate minus a property tax credit of 3.67%). Exemptions in the law include a two-year "new

pool" exemption and a "minimum production" exemption for a well with average production of less than \$87 gross value of natural gas per day. Estimates are that only about 7.5 percent of all gas produced is exempt from severance taxation.

While the severance tax on oil imposes the same 4.33 percent rate, the various exemptions in the oil severance tax law combine to exempt about 52.3 percent of production.

The total volume of gas produced in FY 2008

FY08 Natural Gas Production Breakdown by Region		
Location	Volume	Reported (mcf)
North Central	16,776	0.00%
North East	550,875	0.14%
North West	3,586,550	0.94%
South Central	51,417,122	13.45%
South East	46,701,691	12.22%
South West	279,945,779	73.24%
Total	382,218,793	

## COMMITTEE ACTIVITIES

At the October meeting, staff briefed the Committee on the current severance tax structure and relevant statutes. The Department of Revenue subsequently explained that, unlike Kansas, Louisiana taxes the volume produced at a tax rate which is adjusted each year to reflect the change in the average Henry Hub index price.

### Department of Revenue Testimony

The Department then outlined a number of reasons why they believe this sort of methodology would be better than the current Kansas system, which was developed in 1983 during circumstances for the industry and markets that are much different than they are today. The Department's testimony included the following observations:

1. Industry practices have changed since the enactment of the current law

Kansas mineral severance tax laws were established in 1983 when gas was typically sold at the wellhead to a pipeline company for a regulated price under long term contracts. The tax is imposed on the gross value of natural

gas at the time it leaves the lease. Today, gas is typically sold off the lease at a centralized sales meter, however the value of the gas may be based on what is sold after the gas is processed into its various components: helium, residue gas and natural gas liquids (NGLs). This change in the point of sale and valuation method makes it difficult to determine the wellhead value for tax purposes. Some states use a "work back" method to determine taxable value; they take the sales price less expenses to get the gas to the point of sale. In theory, the costs incurred after the gas leaves the lease are adding value and should be deducted from the selling price to get back to wellhead value. This type of valuation results in inconsistent deductions and refund requests due to consultants finding additional "expenses" to deduct. The Department of Revenue issued a revenue ruling in 1998 stating that taxpayers should value their gas on the same basis used for calculating royalty payments. If the value of gas is understated on royalty statements due to high deductions for gathering, line loss, fuel usage, processing, etc., state severance taxes are also understated.

2. Deregulation of interstate pipelines

In the late 1980's, Congress deregulated the gas industry and now only the interstate pipelines are regulated and they can no longer purchase gas, just transport it. Each state's utility commission is now responsible for regulating intrastate pipelines and gathering systems. Generally states have decided not to regulate pricing even though in most cases gathering systems and gas plants operate as monopolies. A few companies have purchased most of the gathering systems in Kansas, and in some cases, gathering fees have quadrupled since deregulation. Gathering companies often take a percentage of the product as part of their transportation fee. Generally, tax is not paid on fuel used to move the product or to compensate gathering companies.

3. Lack of arms-length transactions and free market conditions

Over 40% of all natural gas sold in Kansas is between related entities, the first purchaser is a marketing affiliate of the company that operates the lease. Smaller independent operators often have no choice but to sell to the gathering system that is near their wells since it would be cost prohibitive to lay new pipelines to another system.

#### 4. Tax is not being paid on the gross value of natural gas extracted in Kansas

Many taxpayers are deducting several post production costs from the sales price of gas, such as gathering fees, fuel usage, line loss, electricity, depreciation, labor costs, processing costs, etc. Often gathering companies and processing plants take a certain percentage of the volume as part of their fee. Prices and fees are frequently renegotiated with unique contract terms. The end result is that the "gross value" of similar quality gas from the same part of the state will vary significantly depending on the provisions of the sales contract.

#### 5. Royalty settlements indicate the value of gas is being understated by large oil companies

The Department of Revenue's current policy is to value gas based on the value reported to land owners on their royalty statements. Several of the large oil companies have been sued by the Southwest Kansas Royalty Owners Association, resulting in millions of dollars in additional royalties. Most of the settlements are for periods prior to the three year statute of limitations for Kansas mineral severance tax.

#### 6. Large Price Fluctuations

During the last few years, the selling price of natural gas, NGL's and helium have increased significantly, with large monthly price fluctuations. This makes it difficult to determine the "true value" of natural gas as required under K.S.A. 79-4216(d).

#### 7. Large differences in pricing methodology

Returns filed for May 2008, have a price per million cubic feet (MCF) from less than a dollar to more than twenty dollars. County and township prices also vary significantly. If all taxable gas were reported for the month of May 2008 at the average price of \$9.75, an additional \$1.5 million in taxes would have been reported. A standard price applied to natural gas measured in mmbtu's (million British thermal units) would result in a more consistent and fair valuation method.

The Department concluded its presentation by recommending that Kansas adopt a method similar to Louisiana for valuing natural gas severed. The gross value of the gas would be determined by taking the amount of mmbtu's removed from the lease times a fixed price established each period from average market prices during the previous periods. This would result in a fairer and easier-to-calculate valuation method, according to the testimony.

The Department also recommended a review of severance tax exemptions, noting that oil wells producing up to \$500 per day of value are exempt, compared to only \$87 per day of value for gas wells. In addition to various new pool and low production exemptions, the Department also noted that the Legislature may wish to review the level of the current 3.67 percent property tax credit, which was also put in place at a time when energy prices were significantly different than they are today.

#### **Other Testimony and Committee Discussion**

Two conferees representing the Kansas Independent Oil and Gas Association (KIOGA) said that they opposed the Department's proposal regarding changing the tax imposition in Kansas to be more closely aligned with Louisiana's. The conferees said that because Kansas has multiple

producing zones, all with different characteristics relative to depth and gas quality, that a “one-size-fits-all” approach to price determination like that which is utilized in Louisiana would not be equitable.

A conferee representing British Petroleum said that she generally agreed with the Department of Revenue that because of changes in the gas industry over the last 25 years, the current law had become difficult to comply with and administer. She suggested in response to concerns from the two previous conferees that a generally uniform price or prices could be utilized but given some flexibility by being tied to heating value (to help distinguish quality); and perhaps allow certain transportation costs to be factored in to the determination.

During committee discussion, a number of members stated that the Department of Revenue had a point in raising concerns about the current system, which effectively allows private parties entering into lease agreements to affect state severance tax receipts relative to how such agreements treat deductions for gathering costs.

The Chair noted that because energy policy is about to be rewritten at both the national and state levels, Kansas had a unique opportunity to participate in helping simplify the tax structure on energy-related industries. He said that he challenged the industry to work with the Department of Revenue and other interested parties to draft legislation that could help refine and simplify the severance and property tax structure in Kansas.

At the November meeting, the Committee received additional proposals from KIOGA and British Petroleum that would have addressed some of the Department of Revenue’s concerns administratively.

## CONCLUSIONS AND RECOMMENDATIONS

The Committee finds that because of various changes in the gas industry, the current severance tax law (which was written in the 1980s) has become increasingly difficult to comply with and administer. The Committee believes that a helpful dialogue has been created as a result of this interim study and encourages the industry and the Department of Revenue to continue to work on a solution for some of these complexities.

The Committee recommends that all parties continue to work on a set of proposals which ideally could be implemented by administrative rules and regulations (in lieu of statutory changes). All parties should report back to the standing tax committees by mid-February relative to the progress made on such efforts.

The Committee further finds that because of dramatic increases in the price of oil in recent years, it may no longer be prudent for 50 percent of oil production to be exempt from the state’s severance tax (compared to only 6 percent of gas production). The Committee therefore encourages the 2009 Legislature to review the low-production exemption for oil.

# Special Committee on Assessment and Taxation

## MILL LEVY ISSUES

### CONCLUSIONS AND RECOMMENDATIONS

The Committee believes that legislative intent from 1999 was clear in that various mill levy procedural requirements have been suspended since that time. The Committee further notes that Attorney General Opinions have no force and effect of law, and encourages local taxing subdivisions to not act relative to those opinions on mill levies unless directed to do so by the courts.

However, the Committee does believe that various rights which taxpayers had prior to 1999 should be restored and therefore recommends the introduction of a bill to add protest petition provisions relative to certain tax increases by all taxing units, provided the petitions require at least 5 percent participation in order to trigger elections.

**Proposed Legislation:** The Committee recommends the introduction of one bill on this topic.

### BACKGROUND

Late in 2007, Attorney General Opinion 2007-34, issued in response to a request from the Cowley County Counselor on behalf of a fire district, concluded that while a statute enacted in 1999 (KSA 2007 Supp 79-5040) in fact suspended a specific five mill property tax fund levy limit for fire districts that had been established in a second statute (KSA 2007 Supp 19-3610), the 1999 suspension provision did not also negate election procedures outlined in the latter law.

Relying for precedent on a previous opinion from five years earlier (Attorney General Opinion 2002-36) that had gone largely unnoticed by taxing subdivisions and the Legislature, the 2007 opinion concluded that since there was “no statutory authority negating the election procedures ...any fire district that wants to exceed the five mill levy limit must follow the procedural steps set forth ...”

A number of legislators held discussions late in 2007 and throughout the 2008 session with staff, Department of Revenue personnel, and representatives of local units of government about the validity of these opinions and the potential implications on local taxing subdivisions.

### Property Tax Lid: 1989-1999

The Legislature in 1985 enacted an aggregate property tax limitation (tax lid) that was effective beginning with tax year 1989 so as to coincide with the implementation of property tax reappraisal and classification (see KSA 79-5021 et seq). Because of the significant expansion in statewide assessed valuation anticipated as a result of reappraisal, the Legislature wanted a limitation on overall property taxes imposed by taxing subdivisions (many of whom otherwise could have received a windfall if mill levy rates were not rolled back). Numerous individual statutory fund levy limits, therefore, were



suspended and replaced with the aggregate tax lid mechanism (see KSA 79-5022), which was applied to total property tax dollars levied in lieu of the mill levy rates.

At the same time the individual fund levy limits were suspended (5 mills for fire districts, for example), procedural requirements that had been in place prior to 1989 relative to elections or protest petitions (mandatory election for fire districts) also were suspended and replaced with a new mechanism.

The tax lid provided generally prohibited local units from levying property taxes in greater amounts than a “base” year (choice of either 1988 or 1989), subject to a number of exemptions and exceptions relative to property taxes levied for special purposes. Property taxes levied as a result of new improvements to real estate and added personal property were exempt from the computation, as were taxes levied as a result of added territory or a service that had been transferred from another governmental unit. Other exemptions from the formula included property taxes levied for public building commissions; judgments, settlements and expenses for protection against liability; employer contributions for workers compensation, unemployment insurance, health care costs, employee benefit plans, and employee retirement and pension programs; district court operations; payment of out-district tuition to community colleges and Washburn; certain juvenile delinquency and crime prevention programs; rebates granted to property owners in conjunction with neighborhood revitalization programs; expenses necessary to interface with the state criminal justice information system; certain mental health services; and revenues to replace reductions in motor vehicle taxes.

Local units seeking to levy more in taxes beyond amounts not authorized by the aforementioned exemptions and exceptions had home-rule-like authority pursuant to KSA 79-5036 to exempt themselves from all or a

portion of the remaining restrictions of the tax lid by approving charter ordinances or resolutions. Such ordinances or resolutions were then subject to various publication and protest petition requirements, under which a certain percentage of the electorate could force an election on the question of the proposed tax lid exemptions (and efforts to increase property taxes beyond a certain point).

The tax lid was extended a number of times throughout the 1990s, with the last extension coming in 1997 (see 1997 SB 7). Under that legislation, the tax lid was extended for an additional two years -- until July 1, 1999—at which time it was allowed to expire (see KSA 79-5038). Local units of government traditionally opposed reextension of the tax lid, generally arguing that local officials with authority to levy property taxes were elected just like members of the Legislature; that local units of government had a better idea of the demand for local services from the public and did not need to be micro-managed by statewide legislation; and that the tax lid appeared somewhat hypocritical in that its provisions did not apply to the state mill levies for building funds and school district general funds.

#### **Truth in Taxation Lid: 1999-Present**

Cognizant of the imminent expiration of the aggregate tax lid, the 1999 Legislature sought to replace it with a different mechanism known as “truth in taxation.”

The legislation was crafted amid ongoing concerns over confusion regarding the extent to which local units may or may not have been increasing property taxes. The fact that mill levy rates in and of themselves did not necessarily represent an accurate measure for annual changes in property taxes (the other big variable being changes in assessed valuation) caused the legislation to be drafted with an emphasis on requiring local units to acknowledge to the

press and the public when taxes were being increased.

The provisions of the truth in taxation lid, enacted in SB 45, provide that taxing subdivisions (defined more narrowly than the 1989 tax lid to exclude unified school districts and community colleges) are prohibited, absent adoption of a resolution or ordinance so acknowledging, from approving appropriations or budgets funded from property tax increases, except with regard to increases attributable to new improvements to real estate; certain added personal property valuation; property located within added jurisdictional territory; property which has changed in use; and for payment of principal and interest upon bonded indebtedness, temporary notes, and no-fund warrants (see KSA 79-2925b).

The acknowledgment resolutions and ordinances are not subject to protest petition but instead represent an official record for the benefit of the press and the public of certain property tax increases approved by local governing bodies, notwithstanding what may be happening with mill levies.

The 1999 legislation also provided for a permanent sunset of the pre-1989 provisions, effectively repealing the many hundreds of different statutory fund levy limits (and, it was assumed by legislators at the time, the various "procedural" requirements in those laws referenced in both Attorney General opinions which had not been applicable since the late 1980s, at which point in time they were replaced by the home-rule powers provided in KSA 79-5036).

The truth in taxation provisions have not been modified since they were enacted in 1999.

### **2002–New Election Requirements Rejected**

One very important example of the collective belief that there were no protest petition or

mandatory election requirements applicable to local units since 1999 relative to the setting of mill levies relates to the introduction of legislation in 2002 (HB 3025) by the House Taxation Committee, at the request of a taxpayer-advocacy group, that would have reimposed many petition and election requirements for most property taxes levied in excess of 103 percent of the previous year's amount. A similar bill (HB 2869) applicable more narrowly to cities and counties also was introduced by Representative Garner. Neither bill advanced out of the House Taxation Committee, a fact that totally overlooked just months later when the initial Attorney General's opinion was released in August. (Why would these bills have needed to be introduced in 2002 if the pre-1989 procedural requirements were still in place?)

### **2006 Interim Study**

Because of ongoing concerns over property taxes, the LCC in 2006 received interim study requests from Rep. Wilk, Senator Allen, and Senator Brownlee to review the truth in taxation provisions and determine whether they were functioning adequately as a replacement mechanism for the old tax lid law. The LCC subsequently approved the request and charged the Special Committee to study the current "truth in taxation" property tax law that local governments have operated under since the late 1990's. The Committee was asked further to determine if local governments are "complying with the "truth in taxation" provisions and if the provisions should be modified; or whether portions of the previous local government property tax lid law should be revived."

The 2006 Special Committee found that "the decision made in 1999 to abolish the tax lid in favor of the truth in taxation lid represented an appropriate choice of no longer seeking to micro-manage local units of government from the Statehouse." The Committee further noted that "no report surfaced of any local unit having violated the truth in taxation provisions over the

past seven years.” Moreover, during the public hearing on the issue, no conferees appeared to advocate for a return of the 1989-1999 tax lid provisions, which included protest petition procedures and potential subsequent election requirements for certain property tax increases.

### **2008 Legislative Response to AGOs**

During the 2008 Session, the Senate Approved SR 1836, which directed the Secretary of Revenue to seek a declaratory judgment in court as to whether the Tax Reform and Relief Act of 1999 and KSA 79-5040 suspended certain procedural requirements relating to the property tax levy limits of local taxing subdivisions. The resolution also noted that such a determination by the court (that certain election and other requirements were suspended along with the levy limits) would reinforce legislative intent from 1999 and create “a consistent and common sense interpretation of the law.” The resolution was critical of the conclusions reached in both the 2002 and 2007 Attorney General Opinions.

Secretary Wagon was unable to obtain such a declaratory judgment, and county clerks were advised that, absent any such finding to the contrary, the Attorney General’s Opinion should be interpreted as correct, and that they should not certify that any fire district levies of more than 5 mills without voter consent.

### **Implications of AGOs**

Data obtained from the Property Valuation Division show that in 2007, there were 100 out of 405 fire districts statewide that were levying more than 5 mills, presumably none of which had ever held an election. Those districts are located in 36 counties.

An analysis by the League of Municipalities also found that mandatory election requirements had been present in the pre-1989 laws relative to drainage districts (KSA 24-407) and cemetery

districts (KSA 15-1015). In addition a number of protest petition requirements had been present in the pre-1989 laws relative to watershed districts (KSA 24-1219), Washburn University (KSA 13-13a18), ambulance service districts (KSA 65-6113), recreation districts (KSA 12-1927), and general improvement districts (KSA 19-2753 et seq). It is likely than many of these local units are levying property taxes in excess of the pre-1989 fund levy limits without having held elections or met the publication requirements for a protest petition.

In the wake of the inability of the state to obtain a declaratory judgment and the decision of county clerks to adhere to the opinions, the LCC subsequently charged the 2008 Special Committee to study the subject matter in 2008 Senate Resolution 1836, especially relative to whether the Tax Reform and Relief Act of 1999 and KSA 79-5040 suspended certain procedural requirements relating to the property tax levy limits of local tax subdivisions. The Committee is further charged with recommending whether additional legislation is necessary to reinforce legislative intent from 1999 that certain election and other requirements were in fact suspended along with the fund levy limits.

### **COMMITTEE ACTIVITIES**

At the October meeting, staff briefed the Committee on the topic and on the implications for local units of the opinions. Secretary Wagon outlined why she was unable to obtain a declaratory judgment. A conferee representing the League of Kansas Municipalities also spoke about the history of the tax lid and constraints on local taxing subdivisions, noting his belief that the appropriate decision was made to let all components of fund levy limits and the tax lid law expire.

Secretary Wagon also indicated that Shawnee County had legally advised the county clerk that fire districts could levy in excess of

five mills absent an election. But Randall Allen of the Kansas Association of Counties said he thought that other clerks were wanting to err on the side of caution and in fact had convinced fire districts to place questions on the upcoming November 4 ballot.

At the November meeting, the Committee learned that a fire district in Rush County had in fact been asked to place a mill levy proposal on the ballot.

### **CONCLUSIONS AND RECOMMENDATIONS**

The Committee believes that legislative intent from 1999 was clear in that various mill levy procedural requirements have been suspended since that time. The Committee further notes

that Attorney General Opinions have no force and effect of law and encourages local taxing subdivisions to not act relative to those opinions on mill levies unless and until directed to do otherwise by the courts of this state.

However, the Committee does believe that various rights which property taxpayers had prior to 1999 should be restored and therefore recommends the introduction of a bill to add protest petition provisions relative to certain proposed tax increases by all taxing units, provided the petitions require at least 5 percent participation in order to trigger elections.

# Special Committee on Assessment and Taxation

## AEROSPACE ENGINEER CREDITS

### CONCLUSIONS AND RECOMMENDATIONS

The Committee recommends that this issue be approached from a higher education and economic development perspective with additional hearings occurring in those related committees. Any future legislative efforts in this area should focus on expanding engineering programs at Kansas' colleges and universities. The Committee also recommends that the engineering sector take advantage of tax credits given by the federal government

*Proposed Legislation:* None.

### BACKGROUND

The Legislative Coordinating Council (LCC) charged the Committee with studying potential tax policy options designed to attract and retain aerospace engineers in Kansas. In addition to this Committee, the topic also was referred to the Joint Committee on Economic Development, which held an extensive public hearing on this issue in September.

#### Oklahoma Tax Credits

Per the LCC charge, the Committee was to review tax credits passed in Oklahoma designed to increase their state's engineering workforce. A description of the credits can be found below.

The 2008 Oklahoma Legislature enacted House Bill No. 3239, which created three new tax credits for the aerospace industry in Oklahoma.

#### Oklahoma Tax Credit 1: Tuition Reimbursement

Employers whose principal business activity involves the aerospace sector are given a tax

credit for providing tuition reimbursement to any employee that has not previously worked in the aerospace sector. The credit is limited to 50 percent of the dollar amount reimbursed by the employer. The credit can be applied during each of the employee's first four years of employment.

The credit only applies to those employees who have been awarded a degree within one year of commencing employment with the eligible employer.

The credit is non-refundable.

#### Oklahoma Tax Credit 2: Compensation Credit

A qualified employer is eligible for a 10 percent tax credit on all compensation paid to employees who have graduated from an institution within Oklahoma during each of their first five years of employment. If the employee graduated from an institution outside of Oklahoma, the tax credit is lowered to 5 percent.

The credit cannot exceed \$12,500 for each qualified employee annually and is non-refundable.

### **Oklahoma Tax Credit 3: Employee's Tax Credit**

Any employee who has not previously worked in the aerospace sector is eligible for a \$5,000 a year tax credit during each of their first five years of employment.

The credit is non-refundable and may be carried over to each of the five subsequent taxable years.

## **COMMITTEE ACTIVITIES**

At the October meeting, the Department of Revenue provided the Committee with a fiscal note outlining the cost of enacting tax credits similar to those passed in Oklahoma. In total, the cost of the three credits would amount to \$11.5 million in FY 2010; rising to \$72.2 million in FY 2014. When taking the credits individually, the 10 percent of compensation credit carried the largest fiscal note at \$32.85 million in FY 2014. The tuition reimbursement credit and \$5,000 employee credit had FY 2014 figures listed at \$20.2 million and \$19.15 million, respectively.

After hearing from staff and the Department of Revenue, the Committee's discussion focused on multiple policy options. During this discussion, the Committee was informed that the Board of Regents appointed a task force to examine and report back to the Board on how to best expand the engineering programs at Kansas universities. There was interest from several members on approaching the issue from a spending, not tax, perspective.

At the November meeting, staff reviewed prior Committee discussions and provided additional information on the topic of bonded indebtedness. The Committee also discussed an

exemption found in KSA 10-308 as it relates to Junction City. Several members of the Committee expressed concern that an exemption for Junction City could potentially cause other municipalities to ignore the debt limits outlined in statute. The Committee noted that Home Rules authority granted to local units of government might run counter to the debt limits.

At the November meeting, staff reviewed prior Committee discussions and provided additional information on the topic. The Committee's discussion primarily focused on existing tax credits at the federal level and the role played by Kansas colleges and universities in developing the state's engineering workforce.

## **CONCLUSIONS AND RECOMMENDATIONS**

The Committee recommends that this issue be approached from a higher education and economic development perspective with additional hearings occurring in those related committees. Any future legislative efforts in this area should focus on expanding engineering programs at Kansas' colleges and universities. The Committee also recommends that the engineering sector take advantage of tax credits given by the federal government.

# Special Committee on Assessment and Taxation

## NET OPERATING LOSS CARRYBACKS

### CONCLUSIONS AND RECOMMENDATIONS

The Committee sympathizes with the tax circumstances of the bill's proponent and recommends that legislation be introduced narrowly tailored to those circumstances.

*Proposed Legislation:* The Committee recommends the introduction of one bill on this topic.

### BACKGROUND

Late in the 2008 session, HB 2992 was introduced and referred to the House Taxation Committee but did not get a hearing. That bill would expand retroactively to tax year 2007 the net operating loss carryback deduction for income tax purposes to allow certain losses to be carried back up to three years if (1) incurred from the sale of a real asset improved by funds borrowed on both the asset and the farmland; and (2) the farmland had previously been sold as a gain to pay off a mortgage.

A fiscal note provided by the Department of Revenue and Division of Budget indicated that no accurate fiscal note could be provided relative to the potential loss in SGF receipts if the bill were to be enacted. The fiscal note did indicate, however, that the bill would necessitate an additional \$58,720 in administrative costs if it were to be enacted.

The Legislative Coordinating Council in August, at the suggestion of Senator Derek Schmidt and others, charged the Special Committee on Assessment and Taxation with reviewing the subject matter of HB 2992 relative to the proposed expansion of farm net operating loss carrybacks and make any recommendations deemed appropriate to the 2009 Legislature.

### COMMITTEE ACTIVITIES

At the September meeting, staff outlined the provisions of HB 2992 and the extent to which net operating loss carrybacks would be expanded if the bill were to be enacted. Staff also explained that one policy question that would need to be considered before reintroducing some version of the bill in 2009 would be whether the legislation should continue to be retroactive; or whether it should be prospective beginning in tax year 2009. This decision would have obvious implications relative to the fiscal impact.

Mr. Paul Finney of Humboldt spoke in support of reintroducing the legislation. He noted that for his particular circumstance, he in fact would need to the legislation to be made retroactive to tax year 2006 to get the tax benefit.

The Department of Revenue said that while did they did not necessarily have an accurate fiscal note, the cost to the state could be as much as \$6.25 million per year, depending on the number of taxpayers who could avail themselves of the expanded net operating loss carryback provisions. The Department also reviewed the extent to which other states allow both carrybacks and carryforwards of net operating losses for income tax purposes.

## CONCLUSIONS AND RECOMMENDATIONS

The Committee expresses its sympathy for the tax circumstances experienced by Mr. Finney, but is concerned about the potential fiscal note.

The Committee therefore recommends the introduction of legislation more narrowly tailored to apply to Mr. Finney's circumstances and applicable only to tax year 2006.