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STATEMENT OF BRAD SMOOT  
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MONTGOMERY COUNTY  
HOUSE TAXATION COMMITTEE  
Regarding 2012 HB 2501  
March 13, 2012

Mr. Chairman and Members:

Thank you for this opportunity to visit with the Committee on HB 2501. Montgomery County officials and other local governments around the state have huge interest in what commercial assets are determined to be “machinery and equipment” and thereby exempt from ad valorem property taxes and what assets are determined to be “fixtures” which must be taxed as real property. This is the controversy raised by HB 2501, as well as the recent Court of Tax Appeals decision involving the Coffeyville Resources Nitrogen Fertilizer plant. As you may hear from others, this issue is complicated by constitutional law, case law, statutes and distinct factual situations.

The fact that this subject matter is very complex is nothing new to many members of this committee. Some of you were members of the Legislature that oversaw an exhaustive review of Kansas tax policy by the Division of Legislative Post Audit, including a specific report on property tax exemptions. That Performance Audit, delivered in March of 2010, reached at least three conclusions that are worthy of mention and provide an important “context” for today’s discussion:

- 1) The “machinery and equipment” exemptions currently in state law have already “significantly eroded the local tax base.” See Audit page 23.
- 2) “Due to the increase in property tax exemptions which reduces the tax base, tax revenues based on residential real estate have grown faster than any of the other major property categories.” See Audit page 6. By 2008, residential taxes increased as a percentage of total property taxes from 38% in 1994 to 47% in 2008. See Audit page 7.
- 3) As if your job of establishing statewide tax policy wasn’t difficult enough, “Kansas lacks good information about the impact of property tax exemptions on the state.” See Audit page 17. Unlike sales tax exemptions, information on exempt property exist ONLY for real estate taken off the tax rolls. “For most exempt personal property, such as machinery and equipment, no cost information is available” and as a result, the fiscal notes you are provided to evaluate proposed statutory exemptions “often are nonexistent.” Audit page 19.

Take a moment to glance at the Fiscal Note prepared by the Department of Revenue for HB 2501, which states: “. . . the Department does not have data on how much of the current assessed valuation of commercial and industrial real property includes assessments on trade fixtures; therefore, a precise estimate of the amount of decreased property tax revenue and its effect on local and state revenues cannot be estimated.” In short, no one can tell you exactly what HB 2501 will cost your constituents.

In response to a request from the House Taxation Committee Chairman, the Division of Property Valuation, after comparing three other refining plants across the state with the Coffeyville Resources facility, concluded that the House Bill 2501, “could require a reevaluation by each county on the classification of fixtures and assets of these manufacturing operations.” In other words, the legislation before you, not the COTA decision, is likely to set off county-by-county reclassification of manufacturing property.

A more recent Department of Revenue Memorandum dated March 5, 2012, notes that HB 2501 would create an estimated loss of tax dollars for just the 3 refineries and one fertilizer plant of \$42.7 million per year. There would also be a loss of \$15.7 million per year for railroad properties and a significant undetermined loss related to 12 ethanol plants. The Memorandum notes that the 2011 taxable value for real commercial improvements in Kansas was over \$5 Billion or 17% of the overall ad valorem valuation base. In addition, a survey of the counties by the PVD indicates that there is considerable concern that HB 2501 will impact appraisals of various manufacturing facilities, industrial and warehouse facilities, grain handling and storage, gas processing, hog and dairy facilities and even banks, office and retail properties. In short, HB 2501 throws into doubt the classification of \$5 billion in property valuation.

From your own state agencies, the evidence is clear. HB 2501 presents a complex and controversial issue, something far beyond the impression this committee may have been given initially. The Kansas Association of Counties has recommended a moratorium on reclassification of machinery and equipment in response to concerns of the business community that personal property will be reclassified as real estate. The proposed 2 year moratorium should give the Legislature time to figure out how to deal with various classes of personal and real property in a reasonable fashion with little disruption to the current tax base. In addition, we think the Division of Legislative Post Audit or other state agencies could provide expert assistance to lawmakers in resolving these complex issues during the period of the moratorium.

We are hopeful that the Legislature will not rush to judgment on this bill. Without having better information, the passage of HB 2501 might be a big mistake for Kansas businesses, farmers, homeowners and local governments. Thank you again for your willingness to hear from us today and for taking a deliberate approach to proposed changes in state tax policy. I would be pleased to respond to questions at the appropriate time.