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PUBLIC POLICY STATEMENT

HOUSE COMMITTEE ON TAXATION

RE: Support for HB 2285

February 21, 2013 Topeka, Kansas

Testimony provided by:
Brad Harrelson
Assistant Director
KFB Governmental Relations

Chairman Carlson and members of the House Committee on Taxation, thank you for the opportunity to appear in support of HB 2285. I am Brad Harrelson, Assistant Director—Governmental Relations for Kansas Farm Bureau. KFB is the state's largest general farm organization representing more than 40,000 farm and ranch families through our 105 county Farm Bureau Associations.

As you are aware, production agriculture is very capital intensive and requires substantial investment in land, machinery and equipment. Kansas agricultural producers are the largest land owners in the state. Because of these unique requirements, often accompanied by high risk and marginal returns, property taxes place a substantial burden on farmers and ranchers, and often becomes a deterrent to such investment. Stability in classification of property is essential to the long term business decisions made by ag producers, and continued success of the state's largest industry.

For as long as heavy equipment and machinery has been used in Kansas, the machines and equipment that businesses use to operate have been classified as personal property, not real property. The Kansas Supreme Court has held repeatedly that machinery and equipment serves the business and not the land to which it is attached. Therefore, such machinery is personal property.

Due to the differences in how the actual amount of tax is determined in Kansas between real and personal property, in general the ultimate taxes paid by Kansas agriculture could increase significantly under the Court of Tax Appeals decision and the inevitable reclassification of machinery and equipment. While manufacturing and industrial businesses may be most affected by the decision, production agriculture is not unaffected. There are many examples of ag equipment that could be negatively impacted by this departure from long standing precedent. Some examples include, but are not limited to: certain livestock handling equipment, feedbunks, boilers, grain and feed handling equipment, stock waterers, milling equipment, environmental protection equipment, and much more.

Passage of HB 2285 would reaffirm legislative intent and clarify that equipment and machinery is personal property for classification purposes. Kansas Farm Bureau respectfully urges your recommendation to pass favorably HB 2285. Thank you, once again, for the opportunity to appear before you and share the policy of our members. KFB stands ready to assist you as you consider this important measure.



Real vs. Personal Property

January 2013

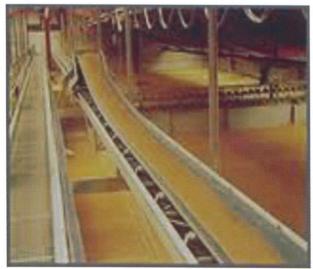
For decades, the clear intent of Kansas property tax law was that commercial and industrial machinery and equipment (CIME) attached to a building for the purpose of serving the building was real estate, while

CIME attached to the building for the purpose of the business was personal property. The classic example is a boiler used to create steam. If the steam was created to heat the building the boiler was real estate. If the steam was used to heat materials to make an industrial or agricultural product, the boiler was personal property. This treatment of fixtures was consistently applied throughout the state for many years.



A 2012 Court of Tax Appeals decision on a 2-1 split vote rejected this widely accepted rule. Some counties in Kansas are attempting to re-classify machinery and equipment as "real" property in order to capture tax revenue on what historically has either been exempt from property tax or at much lower rates. Counties in question are hiring out-of-state appraisers either unfamiliar with past guidance from the State or willing to ignore it.

WHY IS THIS ISSUE IMPORTANT? – The difference in tax obligation between CIME being treated as real estate instead of personal property is significant. CIME that is personal property purchased prior to 2006 is



appraised based on a straight-line depreciation schedule with a 20% residual value. CIME purchased after 2006 that is personal property is 100% exempted from property tax. But CIME classified as real estate is appraised at its fair market value and assessed at 25% to determine its tax value, resulting in much higher property taxes. (By comparison, residential property is assessed at an 11.5% level to determine its tax value.)



What are the anticipated impacts of this tax policy change?

- Treatment of CIME as real estate will dramatically impact the Kansas business climate, including
 profitability and expansion. All of Kansas' neighboring states exempt business personal property
 from property taxes. And, they all regard most commercial and industrial machinery and equipment
 as personal property not real estate.
- Long standing guidance on this tax policy by the Department of Revenue is reversed, creating uncertainty about future tax liability for many businesses including certain ag operations.
- Some businesses have already seen their property taxes increase nearly ten-fold.

Why is this a concern for agriculture?

- While this applied to a large industrial facility, the change in precedent by the Court of Tax Appeals'
 decision could extend to agricultural equipment historically classified as personal property. Possible
 examples might include augers, conveyors, feed bunks, elevator legs, dryers, feed processing
 equipment, bulk tank storage, etc.
- By it's very nature the decision creates the possibility for arbitrary and unequal treatment of similarly identified machinery and equipment across the entire state. It is likely this inequitable approach to appraisal will stimulate significant tax protests, appeals and expensive litigation. The solution is for the legislature to simply codify long standing guidance into state law.

Relevant Kansas Farm Bureau Policy (excerpted)

AT-2

 ... We support the continuation of on-farm grain and hay facilities designated as farm equipment ...

AT-3

• We support a tax mix that would decrease the dependency on property tax and focus more on sales and income taxes for the support of state/local governmental units. Reductions in Kansas personal income tax, or sales tax, should not increase further reliance on property tax as a revenue source for state or local governments. It is important to the citizens of Kansas that the state tax mix not place Kansas at a competitive disadvantage with neighboring states. ... The sales tax should not be imposed on services. The sales tax should be applied at the retail level. We oppose taxing inputs or raw agricultural products, whether by removal of sales tax exemptions or by the imposition of an excise tax, a value-added tax or a transaction tax. ...

AT-4

Kansas has appropriately created justifiable tax exemptions for agriculture, business, industry
and many not-for-profit groups. This has been done to assist economic development and provide
for competitiveness with our neighboring states. Existing exemptions should remain in place. ...