

## MINUTES

### SPECIAL COMMITTEE ON ASSESSMENT AND TAXATION

September 15-16, 2005  
Room 519-S—Statehouse

#### Members Present

Representative Kenny Wilk, Vice Chairperson  
Senator Pat Apple  
Senator Les Donovan  
Senator Janis Lee  
Senator Roger Pine  
Representative Virginia Beamer  
Representative Pat George  
Representative Tom Holland  
Representative Kasha Kelley  
Representative Bruce Larkin  
Representative Arlen Siegfried  
Representative Tom Thull

#### Member Absent

Senator Barbara Allen, Chairperson

#### Staff Present

Chris Courtwright, Kansas Legislative Research Department  
Martha Dorsey, Kansas Legislative Research Department  
Gordon Self, Office of the Revisor of Statutes  
Rose Marie Glatt, Committee Secretary

#### Conferees

Christy Davis, Acting Director, Cultural Resources Division, Kansas State Historical Society  
Ken McClintock, Vice President & Attorney, Historic Preservation Corp; Council Grove, Kansas  
Mark Beck, Director, Property Valuation Division, Kansas Department of Revenue  
Joan Wagon, Secretary of Revenue, Kansas Department of Revenue  
Richard Cram, Director, Policy and Research, Kansas Department of Revenue  
Tony Folsom, Deputy Director, Property Valuation Division, Kansas Department of Revenue  
Roger Hamm, Property Valuation Division, Kansas Department of Revenue  
Steve Brunkan, Kansas Department of Revenue

**Thursday, September 15**

## Morning Session

The meeting was called to order at 10:00 a.m. by Vice Chairperson Kenny Wilk, who welcomed everyone back to Topeka for a busy interim schedule. Senator Lee and Representative Thull also made introductory remarks before all other Committee members were asked to introduce themselves.

Chris Courtwright provided an overview of the topics assigned by the Legislative Coordinating Council:

1. ***Property Tax - Valuation of Historic Property***  
Study a proposed constitutional amendment that would authorize a different valuation methodology for certain property and improvement association with renovation, rehabilitation, or preservation of certain historically significant real estate.
2. ***Tax Treatment of Not-for-Profit Entities***  
Review the sales and property tax treatment of not-for-profit entities and make any policy recommendations deemed appropriate.
3. ***Motor Vehicle Taxes***  
Review the recommendation of the 2004 Special Committee on Assessment and Taxation about the equity of the valuations used for motor vehicle tax purposes. Consider various options regarding replacing the valuation-based system with a fee structure. Also made recommendations as to whether school finance local effort could be enhanced by reinstating the distribution of motor vehicle tax receipts to school district general funds.
4. ***Excise Tax or Licensure Tax - Sexually Oriented Businesses***  
Study a proposed excise tax or licensure tax on certain sexually oriented businesses similar to legislation under consideration by Oklahoma earlier this year.
5. ***Analysis of State and Local Tax Policy***  
Review the current state and local tax structure, focusing on the shifts in reliance on sales, property, and income taxes since 1990. Study the impact on the tax structure of the ongoing shift in the Kansas economy to a more service sector-driven economy. Review the impact of: (1) property tax relief in the 1990s; and (2) the 2002 tax increases on the Kansas economy and tax structure. Study the future of Kansas tax policy for the next 10 to 20 years, and recommend which tax structure components would be most equitable to the taxpayers of Kansas; and would improve Kansas' competitiveness with other states.
6. ***Tax Lien Certificates***  
Study how other states are utilizing tax lien certificates and the potential for application of such a program in Kansas.

Chris Courtwright subsequently reviewed final State General Fund (SGF) receipts for FY 2005 ([Attachment 1](#)) and the first two months of FY 2006. At the request of the Vice Chairperson, he also briefly reviewed the consensus revenue estimating process and noted that the consensus estimating group would be reconvening in late October and early November to revise the FY 2006 estimates

and make the initial estimate for FY 2007. The Committee subsequently requested the latest SGF profile and projected ending balance through FY 2008 (Attachment 2). Staff explained that an updated profile and the revised consensus estimates also should be available for the Committee's review at the November meeting.

## **Topic 1 - Property Tax Valuation of Historic Property**

Chris Courtwright presented a background memorandum and observed that this topic relates to a constitutional amendment adopted by voters in Nebraska in 2004 that authorized the Nebraska Legislature to provide statutorily that the increased valuation attributable to the renovation, rehabilitation, or preservation of certain historically significant real estate may be exempted, in whole or part, from property taxation. The Nebraska Legislature in 2005 unanimously approved LB 66, legislation based on similar provisions in place in South Dakota and Illinois, that authorized a different valuation methodology for certain real property (Attachment 3).

Kansas, since tax year 2002, has provided an income tax credit equivalent to 25 percent of certain expenditures incurred in the restoration and preservation of qualified residential and commercial historic structures, provided such expenditures equal \$5,000 or more.

Christy Davis, Acting Director, Cultural Resources Division, Kansas State Historical Society (KSHS), testified that KSHS fully supports the creation of tools that encourage the rehabilitation of the state's most significant buildings (Attachment 4). She noted that with proper planning, a statewide property tax abatement could work in tandem with the existing income tax credit to ensure the economic feasibility of such projects.

Ken McClintock, Historic Preservation Corporation, distributed copies of an application prepared by his wife, Shirley A. McClintock, for an exemption from ad valorem tax in Morris County (Attachment 5). The exemption was denied by the State Board of Tax Appeals. He described the improvements to six buildings on the historic Santa Fe Trail made possible by various contributions and grants from the community. The restorative focus has been the Terwilliger Home, from which the Trail Days Bakery Café operates, providing much needed funds for its upkeep. Discussion followed regarding whether the neighborhood revitalization program would represent a more attractive alternative relative to a constitutional amendment.

Ms. Davis agreed to provide information from an impact study on the income tax credit program for the October meeting, and staff was asked to provide additional background information on the neighborhood revitalization program.

Mark Beck spoke about policy issues associated with limiting property taxation for certain classes. He discussed various property tax relief options available to the Legislature and reminded the Committee about the potential for property tax shifts.

## Afternoon Session

### Topic 5 - Analysis of State and Local Tax Policy

Chris Courtwright briefed the Committee on four major areas of taxation starting with a review of *Kansas Tax Facts*. The presentation included a discussion of the composition (tax mix) of the Kansas state and local tax structure; revenue elasticity of the major tax sources; the progressivity of the major tax sources; and the extent to which economic development competition with surrounding states influences tax policy.

As part of the discussion on elasticity, Mr. Courtwright noted that while Kansas does apply the sales tax to more services than many states, one of the reasons the elasticity of the tax has been declining relates to the fact that as incomes go up, people tend to spend more of their disposable income on services which are exempt (such as tax preparation, tanning salons, and pet grooming services). He distributed information (Attachment 6) on the extent to which all states tax services.

Several legislators expressed concern during discussion about mill levy increases in rural areas and the impact the elimination of property tax relief (demand transfer) funds from the state has had on property taxes. Senator Lee stated that many of the rural areas experiencing large property tax increases have very limited ability to provide any local property tax relief through the imposition of local sales taxes.

Vice Chairperson Wilk invited Secretary Wagon to address the Committee. She stated that the Department took seriously that part of the charge to study and project the future of tax policy for the next 10 to 20 years and to recommend which tax structure components would be most equitable and improve Kansas' competitiveness.

She reviewed five major topics that she believed were imperative for future tax considerations:

- What does the future hold if the present trends continue? Continued erosion of the tax base will have the following results:
  - Higher tax rates and less equity among the groups of taxpayers;
  - Higher rates will lead to less competitiveness and more taxpayers' discontent; and
  - More special groups that request exceptions for their cause.
  
- The need to return to the Basic Principle of Taxation
  - Taxation is the rule and exemptions should be the exceptions; and
  - The broader the base means a lower rate for all, by being fair, equitable, and good for competition.
  
- How Tax Base Erosion Occurs

- Exemptions and Tax Credits;
  - Economic Shift (consumption and business practices; E-commerce trends and personal services); and
  - Policy Shifts (tax credits, STAR bonds, tax increment finance, and IRBs).
- Lack of Ability to Backtrack - once a special practice is established it is difficult to stop that process
    - Need for specific guidelines from which to make sound financial decisions. Hodge Commission and formulation of special commission to review tax policies and programs and make the decisions on which should be eliminated or restructured.
    - The Department of Revenue is currently working on various issues being discussed in conjunction with the Kansas Advisory Committee, Hugo Wall Center at Wichita State University, and the Department of Commerce. There will be forthcoming in-depth studies that will provide additional information to determine the policy framework for the future of taxation.
- What is on the Horizon that will Impact Future Kansas Tax Structure?
    - Implications of federal tax reforms;
    - Over-reliance on debt financing; and
    - Federal preemption of state taxing authority.
- What Can We Do To Stop the Erosion of the Tax Base?
    - Initiate a study commission to make further recommendations;
    - Modernize corporate income tax;
    - Revisit property taxation of business machinery and equipment;
    - Protect the withholding tax;
    - Look at the estate tax policy after the federal law is finalized; and
    - Fix local sales tax uniformity of local sales tax. Interested Committee members were invited to a meeting on October 18, upon adjournment, with a small group that plans to formulate a proposal.

Secretary Wagnon then distributed information on studies which are scheduled for completion in June, 2006: *A Study of Property Tax Base Erosion in Kansas* and *A Study of Sales Tax Base*

*Erosion in Kansas (Attachment 7)*. She also distributed historical information on the sales and use tax and an update on the efforts of the states to tax Internet sales (Attachment 8).

She subsequently distributed an analysis of the corporation income tax and asked that the Committee pay particular attention to the number of filers claiming various income tax credits (Attachment 9). She also invited Committee members to the upcoming prosperity summit meetings and encouraged them to invite community business leaders to attend, as well.

The meeting was adjourned at 4:45 p.m.

## **Friday, September 16 Morning Session**

### **Topic 6 - Tax Lien Certificates**

Martha Dorsey provided a briefing on a study on how other states are utilizing tax lien certificates and the potential for application of such a program in Kansas (Attachment 10).

Gordon Self explained the differences in tax lien certificates throughout a number of states that utilize such a program. The use of certificates in other states ranges from a simple authorization to very detailed and explicit statutory procedures.

Ms. Dorsey and Mr. Self subsequently delineated those areas the Committee would need to address if a Kansas tax lien certificate proposal were to be introduced, including:

- The specific authority necessary to allow the sale of these certificates;
- Potential limitations as to who may purchase such certificates;
- Potential limitations on the amount of sale;
- When sales would be conducted;
- What would be the redemption period;
- What would be the interest rate;
- Would transaction fees be authorized;
- Rights of purchasers; and
- Resale rights.

Staff agreed to continue to review the policies of other states to secure more details and provide the information at the October meeting. NCSL will be contacted for additional information, as well. The Vice Chairperson suggested that the various surrounding states be contacted to ascertain what their experiences had been with the certificates.

Other questions raised by the Committee included: (a) the responsibility of the mortgagee to the person who paid the delinquent taxes; (b) the rationale behind not employing more aggressive ways to collect delinquent taxes in lieu of authorizing certificates (such as raising the delinquent property tax interest rate); (c) how do delinquent taxes affect home ownership in the states authorizing certificates. The Vice Chairperson asked staff to compare and contrast current law with the basic assumptions about tax lien certificate authorization legislation, as well as SB 45, which passed the Senate last session.

## **Topic 2 - Tax Treatment of Not-For-Profit Entities**

Chris Courtwright handed out a background memorandum ([Attachment 11](#)). He reviewed the sales, property, and income tax treatment of not-for-profit entities in Kansas and distributed a copy of the federal law relating to not-for-profit organizations ([Attachment 12](#)).

Secretary Wagon explained the financial and physical make-up of a typical not-for-profit organization in Kansas and why property tax exemptions are important to such an entity. She said that as a matter of policy, sales tax exemptions are more typically withheld from non-profit groups, since those taxes provided the only source of revenue that goes back to the local community. The Committee asked PVD for information on the total valuation statewide and the amount of exempt valuation, as well as a disaggregation by county of exempt values.

A copy of a report ([Attachment 13](#)) on property tax exemptions, prepared by Tony Folsom of PVD, was distributed. The Secretary turned the Committee's attention to a memorandum on general principles for taxation ([Attachment 14](#)). She said that the state currently does not award many sales tax exemptions for not-for-profit groups and added that such policy was a derivative of the 1970 Hodge Commission study. She recommended that the Committee apply the six questions listed when evaluating potential new sales tax exemptions in an effort to establish a framework that would be fair and consistent.

A memorandum on sales tax treatment for not-for-profit entities, prepared by Steve Brunkan, was distributed ([Attachment 15](#)). If Kansas were to exempt all 501(c)(3) entities, the loss of sales tax receipts would be about \$25 million.

The Secretary invited the Committee to dinner at her home, on Monday, October 17, 2005 at 6:30 p.m. and observed that such a gathering would be not be exempt from the Open Meetings Act.

Senator Lee asked for a briefing at the October meeting on the sales tax exemption number/certificate issue and expressed her frustration that tax-exempt numbers keep changing.

## **Topic 3 - Motor Vehicle Taxes**

Chris Courtwright provided a staff briefing and went over the valuation procedure for motor vehicle tax purposes and the 2004 interim study ([Attachment 16](#)).

Roger Hamm of PVD distributed copies of an overview of the valuation process for tagged motor vehicles ([Attachment 17](#)). Included in his handout were charts that reflected depreciation schedules of vehicles as they age.

The Department of Revenue was requested to work with Senator Donovan and others to provide options for consideration in October that would replace the valuation-based system with a fee structure.

#### **Topic 4 - Excise Tax on Sexually Oriented Businesses**

Gordon Self reiterated that the charge was to study a proposed excise tax or licensure tax on certain sexually oriented businesses, similar to legislation under consideration by the Oklahoma Legislature earlier this year. A staff memorandum (Attachment 18) provided a description of the tax, a comparison of Oklahoma and Utah legislation, guidance with the analysis of the comparison of the two laws, and a brief description of some of the legal challenges to the Utah law as well as a general legal analysis.

He described the on-going legal activities in Utah and how they are affected by the First Amendment. He recommended that if Kansas is to proceed and consider legislation on this topic, the tax should be imposed so as to serve a compelling state interest and be narrowly drawn to achieve that purpose.

The Department of Revenue was asked to provide information on the number of businesses in Kansas that could be affected by such a tax, as well as how much they are remitting in state sales taxes under current law.

The Vice Chairperson encouraged Committee members to advise their constituents of the public hearings in October and to contact staff to be placed on the agenda.

The meeting was adjourned at 1:20 p.m. The next meeting is October 17-18, 2005.

Prepared by Rose Marie Glatt  
Edited by Chris Courtwright

Approved by the Committee on:

October 18, 2005

Date