MINUTES

SPECIAL COMMITTEE ON ASSESSMENT AND TAXATION

October 23-24, 2008
Room 545-N—Statehouse

Members Present

Representative Kenny Wilk, Chairperson
Senator Pat Apple
Senator Karin Brownlee
Senator Derek Schmidt
Representative Sydney Carlin
Representative Stan Frownfelter
Representative John Grange (23rd only)
Representative Jeff King
Representative Bill Light
Representative Steve Lukert
Representative Ron Worley

Members Absent

Senator Les Donovan, Vice-Chairperson
Senator Janis Lee

Staff

Chris Courtwright, Kansas Legislative Research Department
Corey Carnahan, Kansas Legislative Research Department
Gordon Self, Office of the Revisor of Statutes
Scott Wells, Office of the Revisor of Statutes
Kathy Beavers, Committee Assistant
Gary Deeter, Committee Secretary

Conferees

Joan Wagnon, Secretary, Kansas Department of Revenue
Randall Allen, Executive Director, Kansas Association of Counties
Bill Waters, Legal Counsel, Kansas Department of Revenue
Don Moler, Executive Director, Kansas League of Municipalities
Dan Hesket, Assistant Division Director of Law Enforcement and Boating Law Administrator, Kansas Department of Wildlife and Parks
Scott Gates, Director, Learning Quest Program, Office of the State Treasurer

Larry Baer, Assistant General Counsel, Kansas League of Municipalities
Carol Ireland, Audit Manager, Kansas Department of Revenue
Richard Cram, Office of Policy and Research, Kansas Department of Revenue
Steve Dillard, Pickrell Drilling Company, Kansas Independent Oil and Gas Association
David Dayvault, Abercrombie Energy, Kansas Independent Oil and Gas Association
Jeanne Davidson, British Petroleum
Kathy Damron, Public Relations and Governmental Affairs

Others Attending

See attached sheet.

October 23, 2008
Morning Session

The Chairperson called the meeting to order at 10:12 a.m.

Legislative Research Department Staff Chris Courtwright briefed the Committee on the State General Fund (SGF) receipts for the past quarter (July-September), stating that SGF receipts were $18.9 million below estimates (Attachment 1). He commented that the Consensus Revenue Estimating Group will meet in November to consider the FY 2010 state budget and that, given the current economic climate, he surmised a continued erosion of SGF receipts. Mr. Courtwright answered members' questions:

- The state budget committee will meet next week to consider whether the economic downturn will affect the Kansas Department of Social and Rehabilitation Services caseloads such as Medicaid;
- There are very few components of the federal bailout that will affect Kansas.

The Chairperson commented that even though Kansas has a strong network of community banks, the credit freeze will affect them. He suggested one response to the economic crisis would be to take the consensus estimating figures and consult with recognized economic advisors to project a future economy six, 12, and 18 months hence.

Joan Wagnon, Secretary, Kansas Department of Revenue (KDOR), commented that nothing definitive will be known about the Kansas economy until April's Consensus Revenue Estimating Group report.

Topic 8: Mill Levy Issues

Mr. Courtwright gave a brief history of legislative action on mill levies (Attachments 2 and 3). He said that before 1989 the Legislature regulated levy limits through a myriad of individual statutes, but a 1989 tax lid law attempted to equalize tax revenues, a mechanism that included a procedure for exceeding levy limits through a petition and vote of patrons in a given district.

The procedure also suspended the current statutory mill levy limits, which were replaced with tax lid provisions. Legislation in 1999 ("Truth in Taxation") permanently suspended both tax lid levies and protest/referendum provisions and allowed local units of government to set mill levies as they see fit, with the stipulation that increases in valuation which enhance tax revenues without a mill levy increase require a local unit of government to publish a resolution acknowledging an increase in revenues.

Mr. Courtwright explained that two Kansas Attorney General (AG) opinions stating that the protest petition provisions in the 1989 tax lid are still valid have caused confusion for some county clerks, but that the AG opinions have been widely ignored. Seeking a definitive response through the courts, Senate Resolution 1836 (2008 Legislative Session) requested that KDOR seek a declaratory judgment from the courts, but KDOR discovered that without some basis for harm, it had no standing to file a lawsuit (Attachment 4).

Members discussed at length various responses to clarify the intent of the statute. Recommendations ranged from requesting the AG to issue a different opinion to seeking an entity to clarify the law through a court case. Staff offered to provide a technical bill to clarify the statute, but members were reluctant to revisit the statute during session. Randall Allen, Executive Director, Kansas Association of Counties, said he had sought to enlist a local unit of government to file a lawsuit, but to date none had occurred. Mark Beck, Director, Property Valuation Division, KDOR, said certain entities who raise the mill levy must call an election, but most local units of government are free to raise the mill levy without a constituency vote; however, in a convolution of logic, the protest petition statute is still valid even though a vote would be to exceed a limit that does not exist. Staff noted that although the 1999 law makes no reference to a protest petition, the law essentially re-established the 1989 statute regarding protest petitions.

October 23, 2008
Afternoon Session

Don Moler, Executive Director, League of Kansas Municipalities (LKM), commenting on the morning's discussion regarding mill levies, stated that he believed the statute eliminating mill levy limitations also eliminated the need for elections.

Topic 4: Taxation of Watercraft

Dan Hesket, Assistant Division Director of Law Enforcement and Boating Law Administrator, Kansas Department of Wildlife and Parks (KDWP), reviewed current law regarding Kansas' registration and taxation of watercraft (Attachment 5). He said the U.S. Coast Guard sets the standards that qualify the state to receive federal reimbursements for watercraft. Noting that boats are registered, not titled, in Kansas, he said registration is based on the boat's "principal use" location and that a boat must be located in Kansas for 60 consecutive days before being required to be registered. Noting that over half of Kansas' registered boats are more than 13 years old and noting that Oklahoma has 4,507 registered boats with Kansas addresses, Mr. Hesket said owners with newer boats often register them in neighboring states to escape paying Kansas property taxes. He requested the Committee consider adjustments in the law to make boating registration more easily enforceable. Responding to questions, Mr. Hesket said a constitutional amendment would be required to adjust watercraft statutes. He estimated that Kansas loses $300,000 each year to neighboring states whose taxes on watercraft are nonexistent or much lower. He replied that currently KDWP received $1 million in federal matching money, but $1.3 million is available if the Department had the matching funds.

The Personal Watercraft Industry Association (Chris Neal, State Affairs Manager) provided written testimony urging the Committee to reclassify watercraft for tax purposes in order to give Kansas a competitive advantage in relation to neighboring states (Attachment 6).

Randall Allen, Executive Director, Kansas Association of Counties, provided written testimony suggesting that a constitutional amendment should be placed on the 2010 ballot and that the Committee recommend that KDOR include watercraft in their new Vehicle Information Processing System (VIPS) in order to more accurately track watercraft (Attachment 7). Secretary Wagnon stated that if the Committee wanted to include watercraft in VIPS, the project being designed could accommodate the addition of watercraft; however, the agency needs to know by December in order to include watercraft in the software design. The Chairperson asked Representative Grange to give some thought to the issue and report back to the Committee.

Topic 5: Coalbed Methane Valuation

No conferees appeared to testify on the topic.

Topic 6: Local Bonded Indebtedness

Legislative Research Department Staff Corey Carnahan briefed the Committee on the debt limits for cities and counties and the two ways that Kansas monitors bonded indebtedness: through KSA 10-108, by which the State Treasurer receives validation of the bonds from the Kansas Attorney General; and through sole oversight by the State Treasurer's Office (KSA 10-110). Answering a question, Mr. Carnahan said school districts are considered a separate entity with separate statutes (Attachment 8).

Scott Gates, Director, Learning Quest Program, and General Counsel, Office of the State Treasurer, explained that the Treasurer's Office tracks bonds and indebtedness, but does not track debt limits (Attachments 9, 10, and 11). The Chairperson requested more detailed information, specifically, information showing the percentage of debt to assessed value for each county and for state agencies. He requested information from 1990 to 2007 to show trends. Mr. Beck replied that KDOR could provide the data in order for Mr. Gates to do a comparison. A member noted that one-half of indebtedness listed came from industrial revenue bonds (IRBs). The Chairperson requested that Mr. Gates' figures show percentages with and without the IRBs.

Members discussed at length various aspects of the bonding process. Larry Baer, Assistant General Counsel, LKM, responded to most of the questions:

- Many cities do not request a rating for bonds;
- Special projects are treated differently and assessed to a specific benefit district;
- A city backs special benefit district projects and can levy taxes to pay for them, but the state is not liable for these projects;
- Temporary notes are advance payments anticipating a bond issue;

- No-fund warrants are financial emergencies; there are no funds in the budget for the emergency, but funds are allocated from other sources and must be paid back within three to five years;

- General Obligation bonds address a city or county's infrastructure;

- IRBs go to qualifying business ventures;

- Revenue bonds (STAR, or Sales Tax and Revenue) are funded through sales taxes; and

- The bonding process is self policing.

The Chairperson requested that staff provide information regarding the AG's involvement in reviewing the bonding process.

Topic 3: Property Tax Relief for Seniors

Legislative Research Department Staff Chris Courtwright reviewed 2008 Senate Substitute for HB 2434, the Selective Assistance for Effective Senior Relief (SAFE Senior) income tax credit and how it compares with the Homestead Property Tax Refund Act (Attachment 12). Commenting on the Homestead Act, he stated that the Legislature has expanded the Act by excluding 50 percent of Social Security income from household income, which created a $10 million impact on the SGF. He noted that SAFE Senior is considered a supplement to the Homestead Act; a senior may claim one or the other but not both. It is estimated that about $2 million will be claimed in FY 2009.

Regarding the property tax deferral program, Mr. Courtwright said 24 states have such programs. The Kansas House passed HB 2928 in 2008 establishing such a program, but it failed to pass in the Senate. He provided details about the proposed program and outlined in a chart the comparisons among the three property-tax-relief initiatives for seniors.

Richard Cram, Office of Policy and Research, KDOR, distributed a question-and-answer document answering questions regarding the SAFE Senior initiative (Attachment 13), and Carl York, Office of Policy and Research, KDOR, presented information giving specific details of the SAFE Senior property tax relief (Attachment 14). Answering a question, Mr. Cram said the program relates to earned income, not capital gains or losses. Mr. York replied that the website for the program is still being built. Mr. Courtwright stated that the total cost for the homestead refund, including SAFE Senior, is expected to be about $31.5 million.

The following submitted written testimony regarding the property tax-relief programs:

- George Lippencott, AARP Volunteer Coordinator for Economic Security, provided support for the current programs and offered positive recommendations regarding the tax-deferral proposal (Attachment 15); and

- Mark Desetti, Kansas National Education Association, noted concerns regarding the consequences of the programs, commenting that reducing taxes paid by seniors will increase the tax burden on others and that not all seniors are struggling to meet their tax payments (Attachment 16).

October 24, 2008
Morning Session

Topic 2: Sales Tax on Telecommunications

Mr. Courtwright reviewed previous legislative proposals regarding refunding sales tax paid by telecommunications companies on the purchase of machinery and equipment. He stated that a bill passed the Kansas House and Senate in 2008 but was vetoed by the governor. Secretary Wagnon explained that the governor was not opposed to the bill, but vetoed it because it was bundled with other less desirable legislation. Ms. Wagnon urged the Committee to weigh fiscal priorities carefully in deciding whether to recommend such legislation again, noting that some view telecommunications not as a manufacturer, but as a service industry providing a dial tone to customers and thus ineligible for the sales tax refund. The Chairperson requested Mark Beck to provide clarifying information as to whether or not the telecommunications industry falls under the machinery-and-equipment sales tax exemption of other companies.

In considering the November 13 Committee meeting and the state's budget process, the Chairperson expressed a desire to hear from financial experts. Secretary Wagnon recommended Rob Weigand, Professor of Finance, at Washburn University in Topeka.

Topic 7: Gas Severance Tax

Staff Scott Wells reviewed KSA 79-4216 and 79-4217, which address aspects of the mineral severance tax (Attachment 17).

Carol Ireland, Audit Manager, KDOR, testified regarding ambiguities associated with the agency's assessing the gas severance tax (Attachment 18). Noting that in FY 2008, $91.5 million was collected from the gas severance tax, she said the statute requires the agency to assess the value of gas at the wellhead, which can be measured either at 1,000 cubic feet (MCF) or in thermal units. She said the difficulty in assessing the tax equitably is that gas is not sold at the wellhead, but at a distribution point, where it is often mixed with differently valued gas. Further, prices vary widely for the same quality gas. Present agency policy links gas value to the royalty payments made to the landowner; however, some gas companies discount costs before making payments to the owner, creating further inequities in determining the value of the gas. Based on complaints from legislative constituents, she requested that the Committee recommend a more equitable measure of value.

Steve Dillard, Vice-President and Land Manager, Pickrell Drilling Company and Natural Gas Chairperson, Kansas Independent Oil and Gas Association (KIOGA), pointed out the many variables in determining a value for natural gas (Attachment 19). He gave a brief history of deregulation, which allowed Kansas to take a "light-handed" approach to regulation, a path which he said has increased the state's tax revenues. He urged the Committee to take no action on the issue. Answering a question, Mr. Dillard said in September there was a 300 percent difference in value among companies selling gas in Kansas. A member noted that gas is taxed three times: at the wellhead, as property tax, and as income tax. He suggested combining the taxes as a way to bring equity to the issue.

David Dayvault, Abercrombie Energy and Chairperson of KIOGA, commented that currently gas is taxed at its relative *value*; KDOR's proposal would tax gas at its relative *volume*, creating far more inequities than the current system (Attachment 20). He stated that taxing gas volume ignores the wide variance in gas quality, whereas the current system recognizes value as reflected by payments to the royalty owner. He urged the Committee to reject KDOR's proposal, noting that the agency has the authority to address abuses in the present system. Responding to a question, Mr. Dayvault said royalty payments and costs associated with gathering the gas vary widely and are determined by each contract. Members discussed merging the severance tax with another tax. Secretary Wagnon replied that such a move would require major statutory changes. Responding to other questions, Mr. Dayvault said oil is priced by volume, gas by value. Low-production wells are exempt from severance tax.

Jeanne Davidson, British Petroleum, acknowledged that gas varies widely in quality and urged that, in considering the KDOR proposal, the Committee create a process that can be customized, can be tied to the heating value of gas, and can be applied county-wide. The Chairperson requested that Ms. Davidson provide written testimony for the Committee.

Topic 9: Aerospace Engineer Credits

Staff Corey Carnahan outlined the proposal for three tax credits patterned after 2008 Oklahoma legislation, which provides a tax credit for aerospace engineers for tuition reimbursement, employer compensation, and an employee working in aerospace for the first five years (Attachments 21, 22, 23, and 24). He said the proposal is an effort to address the shortage of engineers in Kansas, especially in the aerospace industry.

Richard Cram reviewed the fiscal impact on the SGF, stating that the proposal would reduce tax revenues about $72.2 million over a five-year period. Members discussed the ramifications of the proposed tax credits and, while acknowledging the need to attract more engineers to Kansas, especially in the aerospace industry, agreed that the Committee should recommend other ways to recruit and retain engineers, one of which would be to align legislative action through workforce development at the Kansas Board of Regents. Kathy Damron, Public Relations and Governmental Affairs, commented that the Regents already have created a task force to address the issue of engineer recruitment and retention. The Chairperson requested a report from the Regents. Secretary Wagnon noted that incentives to increase the engineer workforce are best focused on elementary and secondary education.

The minutes for the September 18-19 meeting were approved. (Motion by Representative Worley, seconded by Representative Light.)

The meeting was adjourned at 12:04 p.m. The next meeting is scheduled for November 13, beginning at 9:00 a.m.

Prepared by Gary Deeter
Edited by Corey Carnahan

Approved by Committee on:

November 13, 2008
(date)