

Approved: _____

Date

3/14/94

MINUTES OF THE HOUSE COMMITTEE ON TAXATION.

The meeting was called to order by Chairperson Keith Roe at 9:00 a.m. on March 9, 1994 in Room 519-S of the Capitol.

All members were present except:

Committee staff present: Chris Courtwright, Legislative Research Department
Tom Severn, Legislative Research Department
Don Hayward, Revisor of Statutes Office
Bill Edds, Revisor of Statutes Office
Lenore Olson, Committee Secretary

Conferees appearing before the committee:

David Cunningham, Director, Division of Property Valuation
Mikel Filter, Senior Research Analyst, Kansas Inc.
Dave Porter, WI/SE Partnership & Kansas Industrial Developers Association
Lavern Squier, Ellis County Coalition for Economic Development
Dr. Charles Warren, President, Kansas Inc.

Others attending: See attached list

Chairperson Roe opened the hearing on SB 572.

SB 572 - director of PVD deemed agency head for KAPA purposes.

David Cunningham, Director Division of Property Valuation (PVD) testified in support of SB 572. He said this bill is to streamline appeals from decisions of the Director of PVD and will benefit both the taxpayers and the Department of Revenue by eliminating an unnecessary step and potential confusion in the appeals process (Attachment 1).

The Chair concluded the hearing on SB 572.

Chairperson Roe opened the hearings on SB 461 and SB 463.

SB 461 - tax incentives for certain service sector firms.

SB 463 - research and development tax credit sunset extension.

Mikel Filter, Senior Research Analyst, Kansas Inc., testified in support of SB 461. Ms. Filter explained the recommended amendments to the Kansas Enterprise Zone Act. She said this bill would make export-oriented service sector firms eligible for incentives under the state's High Performance Firms Incentives Program (SB 73) and make export-oriented service sector firms a qualified investment under the Kansas Certified Venture Capital Companies statute (Attachment 2).

Dave Porter, WI/SE Partnership and Kansas Industrial Developers Association, testified in support of SB 461. He said the concepts outlined in this bill will assist in eliminating the retail interpretation problems that several service sector firms have recently experienced from the Department of Revenue (Attachment 3).

Lavern Squier, Ellis County Coalition for Economic Development, testified in support of SB 461. He said that many older buildings can be put to a higher and better use through interim leases, and more new construction could be justifiable through the language in this bill (Attachment 4).

CONTINUATION SHEET

MINUTES OF THE HOUSE COMMITTEE ON TAXATION, Room 519-S Statehouse, at 9:00 a.m. on March 9, 1994.

Dr. Charles Warren, President, Kansas, Inc., testified in support of SB 463 and said a two year extension of the R&D tax credit would enable them to retain this incentive and allow for an evaluation of its use and effectiveness. Dr. Warren also said he proposed that the Kansas Science and Technology County study this issue and include recommendations on incentives for R&D in their strategic plan (Attachment 5).

Chairperson Roe concluded the hearings on SB 461 and SB 463.

The Chair directed the Committee to return to deliberation on HB 2933.

HB 2933 - individual medical accounts.

On March 8, 1993, a motion was made by Representative Wagle, seconded by Representative Crowell, to amend HB 2933 with several conceptual amendments to be prepared by the Revisor of Statutes.

Representative Wagle reviewed a balloon prepared by the Revisor amending HB 2933 and the Committee discussed the proposed changes* Representative Wagle agreed with a request by Representative Adkins to amend lines 16-18 on page 2 of HB 2933, to read "to purchase medical insurance for the account holder or the account holders dependents which would have a deductible of \$5000 but not to exceed \$10,000, which would cover all medical expenses of those deductibles." * (Attachment 6)

A substitute motion was made by Representative Wiard, seconded by Representative Welshimer, to table HB 2933. The motion failed with a vote of 9 ayes and 12 nays.

The Chair directed the Committee to return to the motion by Representative Wagle to amend HB 2933. The motion carried.

A motion was made by Representative Mays, seconded by Representative Crowell, to amend HB 2933 in Section F on page 2 that upon the death of one spouse the account of the other spouse is named the beneficiary and the account will then be transferred to the surviving spouse only. The motion carried.

A motion was made by Representative Wagnon, seconded by Representative Shriver, to amend the balloon on HB 2933 on page 2, lines 16-18 to read "purchase major medical coverage for each account holder or account holder and dependents of the account holder to cover all medical expenses." The motion carried.

A motion was made by Representative Wilk, seconded by Representative Crowell, to pass HB 2933 favorably as amended.

A substitute motion was made by Representative Larkin, seconded by Representative Shriver, to amend HB 2933 that once one or both spouses are deceased, any money left in the account is to be put into an estate and would be subject to state income tax. The motion carried with a vote of 12 ayes and 8 nays.

A motion was made by Representative Wilk, seconded by Representative Crowell, to report HB 2933 favorably as amended. The motion carried

The minutes of March 8, 1994, were approved as read.

The meeting adjourned at 11:45 a.m.

The next meeting is scheduled for March 10, 1994.

DATE 3/9/94

REPRESENTING

[illegible]

STATE OF KANSAS

David C. Cunningham, Director
Robert B. Docking State Office Building
915 S.W. Harrison St.
Topeka, Kansas 66612-1585



(913) 296-2365
FAX (913) 296-2320

Department of Revenue
Division of Property Valuation

MEMORANDUM

To: Representative Keith Roe, Chairman,
House Taxation Committee

From: David C. Cunningham, Director, *DCC*
Division of Property Valuation

Date: March 9, 1994

Subject: Senate Bill No. 572

I appear today in support of S. B. No. 572. The purpose of this bill is to streamline appeals from decisions of the Director of Property Valuation. This will benefit both the taxpayers and the Department of Revenue. A similar provision exists for the Director of Taxation.

The gist of this proposed change is to avoid an unnecessary step and potential confusion in the appeals process. Under the Kansas Administrative Procedures Act a taxpayer must appeal the Director's decision to the Secretary of Revenue in order to exhaust administrative remedies because the Secretary is the "agency head." Another statute, K. S. A. 74-2438, specifies that an appeal from the Director's decision is to the Board of Tax Appeals. While an argument can certainly be made that K. S. A. 74-2438 controls the appeal, the potential confusion is there. Furthermore, an appeal to the Secretary is an unnecessary step that only delays the appeal. While this potential confusion has not been a problem to date, the question has come up and the proposed amendment clarifies the procedure.

I will be happy to answer any questions.

3/9/94
House Taxation Committee
Attachment 1

HOUSE COMMITTEE ON TAXATION

THE KANSAS LEGISLATURE

S.B. 461

PROPOSED AMENDMENTS TO:

High Performance Firms Incentives Program
1993 Supp. K.S.A. 74-50,131

Kansas Venture Capital Companies
K.S.A. 74-8307

Kansas Enterprise Zone Act
K.S.A. 74-50,114 and 74-50,115

TESTIMONY OF:

Mikel Filter
Senior Research Analyst
Kansas Inc.

March 9, 1994

3/9/94
House Taxation Cmte
Attachment 2

Thank you for the opportunity to testify before you today concerning S.B. 461. This bill would make export-oriented service sector firms eligible for incentives under the state's High Performance Firms Incentives Program (1993 S.B. 73), and make export-oriented service sector firms a qualified investment under the Kansas Certified Venture Capital Companies statute. The bill would also clarify existing Enterprise Zone legislation and add a provision to allow lessors access to tax exemption in certain situations.

Background

As you will recall, Kansas Inc. released the State's new economic development strategy, "A Kansas Vision" in February of 1993. To implement the strategy, Kansas Inc. assembled six "Action Planning Committees." These committees are made up of legislators, cabinet officials, community leaders, men and women with expertise in business, education, technology, and finance, and the state's best economic development professionals.

During the 1993 Interim Session, Kansas Inc. worked with the Business Tax and Incentives Committee and legislative leadership to develop a collection of recommendations to improve the accountability and targeting of economic development tax incentives.

In December, the Kansas Inc. Board of Directors voted to support the Action Planning Committee's recommendations as part of the 1994 Kansas Inc. legislative agenda to implement "A Kansas Vision."

Charles Warren and I presented a paper and testimony to the Senate Assessment and Taxation Committee proposing that the state extend tax incentives to export-oriented service sector firms, as recommended by Kansas Inc.'s Action Planning Committee on Business Tax & Incentives. Subsequently, amendments to both the High Performance Firms Incentives Program (S.B. 73) and the Kansas Certified Venture Capital Companies statutes to allow export-oriented service sector firms access to those programs were drafted.

On January 11, 1993⁴, Kansas Inc. requested introduction of bill making those changes and an additional bill amending the Kansas Enterprise Zone Act. The Senate Assessment and Taxation committee introduced all three bills as S.B. 461. S.B. 461 was reported favorably and was then passed by the full Senate Committee of the Whole on February 8 with technical amendments.

My testimony will explain the amendments contained in the bill. I will first speak to the recommended amendment to S.B. 73. Second, I will cover the proposed amendment to the Kansas Certified Venture Capital Companies statute. And third, I will explain the recommended amendments to the Kansas Enterprise Zone Act, which covers two issues: (1) clarifies the existing statutory definitions found in the Act, and

(2) allows lessors access to sales tax exemption under the E-Zone Act.

I will be happy to answer questions after each major section.

Kansas Inc. and the Action Planning Committee on Business Tax and Incentives support the following provisions of S.B. 461:

Section 1 expands eligibility under the High Performance Firms Incentives Program to include export-oriented service sector firms and other non-manufacturing export-oriented firms.

When determining the allocation of economic development resources, it is important to use a decision making process based on established theory. The **basic industry theory** or the **new dollars theory** has been used in the past by Kansas lawmakers to justify targeting economic development incentives toward manufacturers. The premise behind the basic industry theory is that *firms that bring new dollars into the state by exporting Kansas products are the real wealth producers and therefore have a higher industry value than the industries that simply circulate Kansas dollars in and around Kansas. In a word, those firms bringing new dollars into the state merit economic development incentives.*

This same argument can also be used to justify affording tax incentives to export-oriented service sector firms. Services exported outside the state of Kansas bring significant new wealth to the state. In terms of employment alone, approximately 37,000 jobs in Kansas are dependent on the income generated by service sector exports (Jarvin Emerson, 1989).

Our problem in Kansas has not been in recognizing the value of our export-oriented service sector firms, but rather in writing workable tax law that would (1) identify specific service sector firms meeting the basic industry or new dollar criteria; and that would (2) be administratively feasible for the Department of Revenue to process.

We don't have these problems in the case of the High Performance Firms Incentives Program because (1) the program is administered by the Department of Commerce & Housing, and therefore doesn't need to be written into tax law, and (2) the number of program participants is very low when compared with other incentives programs.

Section 1 of S.B. 461 provides the Department of Commerce & Housing with a method to determine whether applicants for the High Performance Firms Incentive Program are indeed export-oriented service sector firms. By analyzing each applicant's customer base, Commerce can measure the degree to which the firm contributes to the state's economy.

The extent to which the applicant either

(1) exports its services, or

(2) provides substitutes for imports

determines whether the firm will qualify for the S.B. 73 incentives.

This test begins with the three broad categories of businesses that the Bureau of Economic Analysis recognizes as service-related enterprises (Attachment A). Each of these sectors actually encompasses a sometimes diverse group of sub-industries that are looked at individually with this qualifying method. The three broad categories are: (1) Transportation, Communication, and Utilities, (2) Finance, Insurance, and Real Estate, and (3) Services.

To qualify for S.B. 73 incentives a firm would have to:

- 1) a) Be among the eligible firm categories, and
b) demonstrate that 51% of its sales are made to either (1) commercial customers or governmental entities out-of-state, or (2) to Kansas manufacturers, or (3) a combination of both.

or

- 2) a) Be among the eligible categories, and
b) Be a corporate headquarters or back-office operation providing direction, management, or administrative support for transactions made by a national or international corporation.

If a firm meets these qualifications, the applicant would still be required to meet the same high performance standards currently applied to manufacturing firms before actually receiving any benefits.

Adding qualifying export-oriented service sector firms is in keeping with the overall mission of the state's economic development strategy. Kansas Inc. urges the Committee to report this portion of the bill favorably.

Kansas Inc. and the Action Planning Committee on Business Tax and Incentives support the following provisions of S.B. 461:

Section 2 expands the eligibility for venture capital tax credits to allow investments in export-oriented service sector firms.

Current legislation restricts Kansas Certified Venture Capital companies from investing in any service sector firm. The Kansas Department of Commerce & Housing confirms that over the past several years, there have been a number of instances when this restriction has prohibited Kansas Certified Venture Capital Companies from investing in otherwise viable and potentially highly successful export-oriented service sector firms.

The expansion of statutory language to allow export-oriented service sector firms to

qualify as investments under this Act would allow us to address the needs of these firms that currently fall through the cracks of the assistance network.

This amendment would require Kansas Certified Venture Capital Companies to qualify service sector investments with the same method as is proposed in the S.B. 73 amendment.

Kansas Inc. also supports the following provisions of S.B. 461:

Section 3 clarifies existing firm classifications used to determine eligibility under current Enterprise Zone legislation.

This amendment is recommended in response to a serious problem that was brought to our attention regarding the newly reconstructed Enterprise Zone statutes adopted by the 1992 Legislature. In short, due to the present wording of the bill, many firms are being denied the enterprise zone credits the original authors meant them to be entitled to.

When a firm applies for E-Zone incentives, the Department of Revenue classifies the firm as either a "manufacturing business," a "non-manufacturing business," or a "retail business." This classification determines what incentives a business is entitled to under the E-Zone Act. As illustrated in Attachment B, if the business is classified as a "retail businesses" it qualifies for only very limited benefits, and only if the business is located in a community of 2,500.

The way the law is currently written and being interpreted by the Department of Revenue, all businesses except manufacturers, wholesale businesses and warehousing operations are being classified as "retail businesses". According to Revenue officials, an engineering firm such as Black and Veatch, a medical laboratory providing services for insurance companies, or even a Federal Express terminal would be classified as "retail business." Clearly, it was not the intent of the original authors to exclude these type of export-oriented service sector firms.

Section III of SB 461 is an amendment which was tailored with the cooperation of Kansas Inc., the Kansas Department of Commerce & Housing, the Kansas Department of Revenue, and Legislators who participated in the original drafting of the current enterprise zone laws.

The amendment would simply clarify the firm classification definitions to ensure that the original intent of the enterprise zone laws are carried out. **It would not change which firms were meant to be entitled to enterprise zone benefits in any way. The amendment would simply enforce the law as it was originally meant to be interpreted.**

To accomplish this, we begin by better defining the term "retail". The new definition

starts with businesses that are subject to retail sales tax. With the help of Representative Jack Wempe, we also added other types of firms the original authors meant to be classified as retailers, including certain professional services (Attachment C.)

We have also clarified the "non-manufacturing" definition by including national headquarters and back office operations of national or international companies.

As I mentioned, Kansas Inc., the Departments of Commerce and Revenue, as well as legislators who originated the 1992 legislation met over the course of a month, and we feel these amendments will ensure that the original intent of the authors is carried out.

Section 4. extends sales tax exemptions to lessors under the Kansas E-Zone Act.

Discussions between Kansas Inc., the Department of Revenue, and Bill Thompson of the Industrial Development Division of the Department of Commerce resulted in our requesting that the Kansas Enterprise Zone Act be further amended to make lessors eligible for sales tax exemption on purchases made in conjunction with new building construction which will be leased to a qualifying job creating entity for a period of at least 5 years.

Section 4 would effect K.S.A. 74-50,115 by adding the following paragraph:

"(d) Any person constructing, reconstructing, remodeling, or enlarging property which will be leased for a period of 5 years or more to a business that would be eligible for a sales tax exemption hereunder if such business had constructed, reconstructed, enlarged, or remodeled such property itself shall be entitled to the sales tax exemptions property under the provisions of subsection (ee) of K.S.A. 1993 Supp. 79-3606a, and amendments thereto.

Conclusion

I respectfully urge the Committee to report favorably on S.B. 461. Thank you for your attention. I'll now stand for further questions.

ATTACHMENT A: Criteria for qualifying as an export oriented service sector firm.

Transportation/Communications/Utilities (SIC 40-49)
Finance/Insurance/Real Estate (SIC 60-67)
Services (SIC 70-89)

EMPLOYS LESS THAN 500 FTE

And is either a **HEADQUARTERS** or _____ or _____ at least 51% of total gross revenues are a result of
BACK OFFICE OPERATIONS of a sales to **COMMERCIAL** or **GOVERNMENTAL CUSTOMERS**
national or multi-national corporation **OUTSIDE THE STATE**

or

at least 51% of total gross revenues are a result of
sales to **KANSAS MANUFACTURERS**

or

at least 51% of total gross revenues are a result of
sales to a combination of both above.

and either

PAYS HIGHER THAN
AVERAGE WAGES

or

IS SOLE TWO DIGIT
SIC IN COUNTY

and either

SPENDS AT LEAST 2% OF TOTAL
PAYROLL ON WORKER TRAINING

or

PARTICIPATES IN KDOC&H'S
KIT/KIR OR SKILL PROGRAMS

ATTACHMENT B: Summary of E-Zone incentives.

Summary of Incentives

Eligibility for the various incentives and the value of the incentive depend on 1) the type of business, 2) the location of the business within the state, and 3) the number of net new jobs created. The *Kansas Enterprise Zone Act* defines the six counties of Douglas, Johnson, Leavenworth, Sedgwick, Shawnee, and Wyandotte as metropolitan counties. As such, they are ineligible to apply for the enhanced job credits available to designated non-metropolitan counties.

<i>Number of Jobs Criteria All Counties</i>	<i>Basic Incentives All Counties</i>	<i>Enhanced Incentives Design. Non-metropolitan Regions</i>
<u>MANUFACTURING</u> Must create a minimum of two (2) net new jobs	<u>MANUFACTURING</u> Sales Tax Exemption Job Creation Tax Credit - \$1,500 per net new job created Investment Tax Credit - \$1,000/\$100,000 (or major fraction) of qualified business facility investment	<u>MANUFACTURING</u> Sales Tax Exemption Job Creation Tax Credit - \$2,500 per net new job created Investment Tax Credit - \$1,000/\$100,000 (or major fraction) of qualified business facility investment
<u>NON-MANUFACTURING</u> Must create a minimum of five (5) net new jobs	<u>NON-MANUFACTURING</u> Sales Tax Exemption Job Creation Tax Credit - \$1,500 per net new job created Investment Tax Credit - \$1,000/\$100,000 (or major fraction) of qualified business facility investment	<u>NON-MANUFACTURING</u> Sales Tax Exemption Job Creation Tax Credit - \$2,500 per net new job created Investment Tax Credit - \$1,000/\$100,000 (or major fraction) of qualified business investment
<u>RETAIL</u> Must create a minimum of two (2) net new jobs	<u>RETAIL</u> Sales Tax Exemption (<i>This is available only for businesses in communities of less than 2,500 population</i>)	<u>RETAIL</u> Sales Tax Exemption (<i>This is available only for businesses in communities of less than 2,500 population</i>)

ATTACHMENT C: Professional services deemed retail businesses.

17-2707. Professional corporation law; definitions. As used in this act, unless the context clearly indicates that a different meaning is intended, the following words mean:

(a) "Professional corporation," a corporation organized under this act.

(b) "Professional service," the type of personal service rendered by a person duly licensed by this state as a member of any of the following professions, each paragraph constituting one type:

- (1) A certified public accountant;
- (2) An architect;
- (3) An attorney-at-law;
- (4) A chiropractor;
- (5) A dentist;
- (6) An engineer;
- (7) An optometrist;
- (8) An osteopathic physician or surgeon;
- (9) A physician, surgeon or doctor of medicine;
- (10) A veterinarian;
- (11) A podiatrist;
- (12) A pharmacist;
- (13) A land surveyor;
- (14) A certified psychologist;
- (15) A specialist in clinical social work;
- (16) A registered physical therapist;
- (17) A landscape architect;
- (18) A registered professional nurse.

(c) "Regulating board," the board or state agency which is charged with the licensing and regulation of the practice of the profession which the professional corporation is organized to render.

(d) "Qualified person":

(1) Any natural person licensed to practice the same type of profession which any professional corporation is authorized to practice; or

(2) the trustee of a trust which is a qualified trust under subsection (a) of section 401 of the internal revenue code of 1954, as amended, or of a contribution plan which is a qualified employee stock ownership plan under subsection (a) of section 409A of the internal revenue code of 1954, as amended.

History: L. 1965, ch. 157, § 2; L. 1972, ch. 63, § 1; L. 1976, ch. 109, § 1; L. 1980, ch. 242, § 27; L. 1981, ch. 104, § 1; July 1.

Senate Committee on Assessment and Taxation

March 9, 1994

Testimony Concerning SB 461

Presented by: Dave Porter

Director, Business Development

WI/SE Partnership

Wichita, Kansas

and

Board Member, Kansas Industrial Developers Association

I'm Dave Porter, Director, Business Development, for the WI/SE Partnership in Wichita. WI/SE is the economic development corporation for Wichita, Sedgwick County, and I am responsible for recruiting new industry to the area, as well as helping local companies with their growth.

I thank you for the opportunity to testify this morning. I am here today wearing two hats. I would first like to address a concern we have in Wichita, then make a statement on behalf of the Kansas Industrial Developer's Association.

1993 was a difficult year in Wichita. Boeing announced major cutbacks which could have impacted 6,000 jobs. This announcement was followed by Sears announcing the closings of their six tele-catalog centers around the country, including the one in Wichita. The Wichita Catalog Center employed 1,700 people, and over 2,000 during their peak season.

In 1988, Sears chose Wichita over other cities in other states because of the highly productive labor force Kansas has to offer, as well as the various incentive programs offered by the state, including the Enterprise Zone benefits.

It has been nearly one year since the Sears closing, and thus far, we have been unable to find a new tenant for this special use facility. However, we do have a "hot" lead on an out-of-state company that is seriously considering Wichita for a new tele-catalog center which could employ 1,800 people. This company is aware of recent interpretations by the Kansas Department of Revenue affecting eligibility of corporate income tax credits to service sector companies. This prospect is very concerned about their own eligibility for these tax credits should they decide to locate in Wichita, Kansas. They are waiting the outcome of the legislative session before proceeding with a final decision.

I strongly urge your support for SB 461 which could greatly enhance our chances of success with this new prospective business.

Now, I am putting on my KIDA hat.

On Monday afternoon, the Board of Directors for the Kansas Industrial Developers Association met to discuss the various economic development bills and requested my presence here today.

KIDA supports the concepts outlined in SB 461 which will assist in eliminating the retail interpretation problems that several service sector firms have recently experienced from the Department of Revenue. This clarification is very important for all communities throughout the state, and will help local economic development officials to assist the rapid growth in the service sector industry.

I will gladly answer any questions you may have.

3/9/94
House Taxation Committee
Attachment 3



To: Members of House Tax Committee

My name is Lavern Squier, Executive Director of the Ellis County Coalition for Economic Development. I am also a member of the board of directors for the Kansas Industrial Developers Association (KIDA). In that capacity, I am here to support SB 461 and the concepts contained within.

Others from this group (KIDA) have additional information for you to consider.

I would like to comment on one aspect of the bill, that being the corrective language to allow lessees to qualify for all enterprise zones benefits. Previously, the rules were less than clear regarding this issue.

Many times, lessees of buildings and/or equipment are truly the creators of substantial jobs, no less so than owners of real property. As we all know, the intent of enterprise zone legislation is to create jobs through investment and expansion.

In my current position in Ellis County, I have dealt with this dilemma firsthand. Many small communities assist development through lease relationships. This serves to ease concerns on the part of the prospective employer about utilization of finances, growth potential, long-term property values, etc. Many older buildings can be put to a higher and better use through interim leases, and more new construction could be justifiable through the revised language.

KIDA supports this bill in its present form.

*3/9/94
House Taxation Cmte
Attachment 4*

Testimony On

S.B. 463

Before the House Committee on Taxation

March 9, 1994

to

Extend the duration of Research and Development Tax Credits

Senate Bill 463 would extend the availability of tax credits for investments in research and development until January 1, 1996. This is the only change to the existing statute proposed in the bill.

The State R&D tax credit was established in 1986 and expired on December 31, 1993. This tax credit has not been used extensively by Kansas businesses. Only \$586,000 of credits have been claimed in the period between 1987 and 1991. However, we believe that it can be an important incentive to business and that it could play an important role in our broader objective of increasing the research and development investments of Kansas Industry.

One of our major objectives in "A Kansas Vision" is to enhance the R&D capacity of both our universities and our industries. Kansas Inc. has established the Kansas Science and Technology Council which is chaired by Dave King. This 30 member public-private council is preparing a strategic plan for science and technology. It also oversees the EPSCoR program to increase R&D capacity in our regents' universities.

A two year extension of the R&D tax credit would enable us to retain this incentive and allow for an evaluation of its use and effectiveness. Dr. Warren has proposed that the Kansas Science and Technology Council study this issue and include recommendations on incentives for R&D investment in their strategic plan. Specifically, Dr. Warren has asked the Council to address the following questions:

1. Should the R&D tax credit be retained?
2. What explanations are there for the relatively low utilization of the existing R&D tax credit?
3. If it is to be continued, what changes in the existing statute are recommended with respect to:
 - a. the definition of research and development in statute for which credits can be claimed?
 - b. the method by which the base R&D expenditures are calculated?

3/9/94
House Taxation Cmte
attachment 5

- c. the percentage amount of expenditures that can be claimed and the maximum amount for which a deduction is allowed?

We would like to obtain answers to these questions and provide recommendations to this committee by next session so that we can make an informed decision on the retention or modification of the R&D tax credit.

In addition, H.B. 2556, which is being heard in Senate Tax and Assessment today, will allow Kansas Inc. access to company specific tax credit information which will facilitate further study of the value of the R&D tax credit.

I urge your support of Senate Bill 463 to retain the existing incentive for research and development. I would be please to answer any questions.

HOUSE BILL No. 2933

By Representatives Wagle, Boston, Bradley, Bryant, Chronister, Cornfield, Cox, Crowell, Donovan, Empson, Farmer, Flower, Freeborn, Gatlin, Haulmark, Hayzlett, Jennison, Kejr, King, Phill Kline, Lawrence, Lowther, Mason, Mayans, Mead, Mollenkamp, Morrison, Myers, Neufeld, O'Neal Packer, Pottorff, Samuelson, Scott, Shallenburger, M. Smith, Snowbarger, Toplikar, Vickrey, E. Wells and Wilk

2-4

14 AN ACT relating to individual medical accounts; amending K.S.A.
15 1993 Supp. 79-32,117 and repealing the existing section.
16

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

18 New Section 1. This act may be cited as the individual medical
19 account act.

20 New Sec. 2. For the purposes of this act:

21 (a) "Account holder" means the individual on whose behalf the
22 individual medical account is established.

23 (b) "Dependent ~~child~~" means ~~any person~~ under the age of 21
24 years ~~for any person who is~~ legally entitled or subject to a court
25 order for the provision of proper and necessary subsistence, edu-
26 cation, medical care or any other care necessary for their health,
27 guidance or well-being, and who is not otherwise emancipated, mar-
28 ried or a member of the armed forces of the United States ~~or who~~
29 ~~is~~ mentally or physically incapacitated.

30 (c) "Individual medical account" means a ~~trust created or organ-~~
31 ~~ized to~~ pay the eligible medical, dental and long-term care expenses
32 of the account holder.

33 (d) ~~"Trustee"~~ means a chartered state bank or trust company
34 authorized to act as a fiduciary, a national banking association or
35 savings and loan association authorized to act as a fiduciary, or an
36 insurance company.

37 New Sec. 3. (a) ~~For taxable years beginning on or after the~~
38 ~~effective date of this act, a resident~~ shall be allowed to deposit
39 contributions to an individual medical account. The amount of deposit
40 for the first taxable year subsequent to the effective date of this act
1 shall not exceed:

- 42 (1) \$2,000 ~~for the~~ account holder; or
43 (2) ~~\$2,000 for the account holder and \$1,000 for each dependent.~~

the spouse of the account holder and any
child of the account holder who is: (1)

; (2)

: (3)

custodial account established

or the account holder and the account
holder's dependents

custodian

or health maintenance
An individual organization

if the individual medical account is for
the sole benefit of the

3/9/94
House Taxation Cmte
Attachment 6

6-2

1 child of the account holder.

2 (b) The maximum allowable amount of deposit for subsequent
3 years shall be increased annually by a percentage equal to the pre-
4 vious year's increase in the national consumer price index.

5 (c) Interest earned on an individual medical account shall be
6 exempt from state income taxation ~~as adjusted gross income in this~~
7 ~~state.~~

8 ~~(d) Upon agreement between an employer and employee, an~~
9 ~~employer may contribute to the employee's individual medical ac-~~
10 ~~count or continue to make contributions under the employee's ex-~~
11 ~~isting health insurance policy or program, subject to the restrictions~~
12 ~~in subsection (f)(1).~~

(d) 13 ~~(e)~~ The individual medical account shall be established as a ~~trust~~
14 ~~under the laws of this state and placed with a trustee. The trustee~~
15 ~~shall:~~

16 (1) Purchase major medical coverage for each account holder to
17 cover all medical, dental and long-term care expenses in excess of
18 \$10,000 and

19 (2) utilize the ~~trust~~ assets solely for the purpose of paying the
20 medical, dental and long-term care expenses of the account holder.

(e) 21 ~~(f)~~ Individual medical account funds may be withdrawn by the
22 account holder at any time for any purpose, subject to ~~the following~~
23 ~~restrictions and penalties:~~

24 ~~(1) There shall be a distribution penalty for withdrawal of indi-~~
25 ~~vidual medical account funds by the account holder. Such penalty~~
26 ~~shall be 10 percent of the amount of interest earned as of the date~~
27 ~~of withdrawal on the account, and, upon such withdrawal, the in-~~
28 ~~terest earned during the tax year in which withdrawal occurs shall~~
29 ~~be subject to state income taxation.~~

30 ~~(2) after an account holder reaches 60 years of age, withdrawals~~
31 ~~shall be permitted for medical, dental or long-term care expenses~~
32 ~~only, and may be withdrawn without penalty.~~

33 ~~(3)~~ Upon the death of the account holder, the account principal,
34 as well as any interest accumulated thereon, shall be distributed to
35 the decedent's estate and ~~taxes~~ as part of the estate.

(f) 36 Sec. 4. K.S.A. 1993 Supp. 79-32,117 is hereby amended to read
37 as follows: 79-32,117. (a) The Kansas adjusted gross income of an
38 individual means such individual's federal adjusted gross income for
39 the taxable year, with the modifications specified in this section.

40 (b) There shall be added to federal adjusted gross income:

41 (i) Interest income less any related expenses directly incurred in
42 the purchase of state or political subdivision obligations, to the extent
43 that the same is not included in federal adjusted gross income, on

\$5,000 if the individual medical account
is for the benefit of the account holder
and the account holder's dependents

custodial account and placed with a custodian

custodian

or account holder and dependents of the ac-
count holder

an amount equal to or greater than \$5,000
but not to exceed \$10,000

remainder of the

in the custodial account

or dependents of the account holder

for use for other than medical, dental and
long-term care expenses

equal to 10% of the amount withdrawn

the amount withdrawn and

taxed