

Approved: March 31, 1994
Date

MINUTES OF THE SENATE COMMITTEE ON ASSESSMENT AND TAXATION.

The meeting was called to order by Chairperson Audrey Langworthy at 1:00 p.m. on March 28, 1994 in Room 313-S of the Capitol.

Members present: Senator Langworthy, Senator Tiahrt, Senator Martin, Senator Bond, Senator Corbin, Senator Feleciano Jr., Senator Hardenburger, Senator Lee, Senator Reynolds, Senator Sallee, Senator Wisdom

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

Conferees appearing before the committee: Pete McGill, Kansas Military Retirees for Tax Fairness
John Frieden, Counsel, Kansas Military Retirees for Tax Fairness

Others attending: See attached list

JOINT MEETING WITH SENATE FEDERAL AND STATE AFFAIRS

HB 3068--INCOME TAX REFUNDS FOR RETIRED MILITARY PERSONNEL

Chris Courtwright reviewed **HB 3068** for the joint committee. He said this bill, as amended, would direct the Secretary of Revenue to approve and recommend judicial approval of a settlement agreement, to resolve income tax refund claims of military retirees pending in the class action, *Keyton E. Barker, et al. v. State of Kansas, et al.* The bill provides that the settlement, if approved by the Shawnee County District Court, would be made pursuant to revenue transfers from the State General Fund that would equal \$66,485,498.50 over a three year period. The FY 1995 transfer would be \$21,446, 935 and the FY 1996 and 1997 transfers (which include 5 percent interest) would be \$22,519,281.75.

The settlement agreement, which would have to be submitted to the District Court by May 15, 1994, would be required to contain provisions for joint administration under the supervision of the Secretary of Revenue and counsel for the class.

If the settlement agreement receives judicial approval, the bill states that the payment of refunds would represent a "final and complete" settlement of all refund claims of all military retired personnel for tax years 1984 through 1991, including any appeal or administrative process perfected pursuant to law. Payment of the refunds would be subject to the jurisdiction and supervisory control of the District Court.

HB 3068 creates the Military Retirees Income Tax Refund Fund, which would be administered by the Secretary of Revenue in accordance with the provisions of the bill. No expenditures could be made from such fund unless: (1) the settlement agreement is approved by the District Court; and (2) eligible persons have been afforded: reasonable notice and an opportunity to be heard."

Mr. Courtwright also gave a brief background of the history of the bill and why it is being proposed.

Pete McGill, Kansas Military Retirees for Tax Fairness, talked about the bill at length, and went over some of the questions which have been asked by committee members. (Attachment 1) He spoke of two statements, on page 2, line 18 which says "the agreement shall represent a final and complete settlement of all claims" which he said it is doubtful a court would approve. In line 27, there is additional protection for the state. He provided a summary of action taken in 17 other states that have settled with their veterans. He mentioned specifically, Missouri, Iowa, Oklahoma, Colorado, Arkansas and New Mexico, all states which are geographically close to Kansas. He also discussed in the bill as originally introduced the money is to be payable over a three-year period. He also said there is no contingency fee for the attorneys. The Court will

CONTINUATION SHEET

MINUTES OF THE SENATE COMMITTEE ON ASSESSMENT AND TAXATION, Room 519-S
Statehouse, at 1:00 p.m. on March 28, 1994.

determine what should be reasonable attorney fees. Mr. McGill said this is an issue of fairness, the military retirees are not asking for a handout but only what the Court has determined is money which should not have been taken from them. The military retirees are also having to go through the administrative appeals process and the out-of-pocket cost to each retiree without paying attorney fees or travel expenses will exceed \$250.00. He made several references to fairness to the military retirees. If the committee chooses to recommend **HB 3068** favorably, he suggested two minor amendments that need to be made. On line 21 of page three, the date should be changed from 1995 to 1994. In line 30 "statute book" should be changed to the Kansas Register.

Mr. McGill was asked a question from the committee concerning a letter which had gone out to all the military retirees from the attorney's office requesting \$150 to take care of expenses. He said Mr. Frieden was in a better position to answer that.

Mr. Frieden answered some of the questions of the committee. He said they received a number of responses to their letter--none unfavorable. He has also had a lot of phone calls. He was also asked about the money being paid over a three year period. He said they had no problem with the two year period, but there is concern with the three years. He was asked if any of these military retirees will opt-out of the case. He said it is a non-opt-out class action case. He was also asked to provide a list of the committee members of the military retirees who were giving direction in the case. Another member of the committee asked him to provide how the amount of \$64 million was arrived at and if he could have that at the next meeting tomorrow.

The meeting adjourned at 2:00 p.m.

The next meeting is scheduled for Tuesday, March 29, 1994.

DATE: March 28, 1994

[illegible]

TESTIMONY
OF
PETE MCGILL
OF
PETE MCGILL & ASSOCIATES
ON BEHALF OF
KANSAS MILITARY RETIREES
FOR TAX FAIRNESS
PRESENTED BEFORE THE
SENATE
ASSESSMENT AND TAXATION
COMMITTEE

MARCH 28, 1994

RE: HB 3068

*Senate Assessment + Tax
March 28, 1994
attach 1-1*

Madam Chairman and members of the Committee, I am Pete McGill of Pete McGill and Associates. I appear here today on behalf of the Kansas Military Retirees for Tax Fairness seeking legislative assistance in providing a remedy for what they believe has been the unfair and illegal tax policies of the State of Kansas.

This group has been fighting a costly, frustrating and time consuming battle for several years attempting to secure a refund of what the United States Supreme Court has said were taxes illegally collected by the State on their military pensions.

Encouraged by a large number of Legislators and supported by a recent decision of the United States Supreme Court, this group has elected to come to the Legislature seeking your assistance in providing a fair and equitable remedy. Because they have limited knowledge and experience in working with the Legislature, they have asked for the assistance of our firm in helping coordinate their activities as they attempt to work through the legislative process.

Some of you have asked, as have some members of the House, does the legislature have authority to provide a settlement, and if so, will that settlement be binding upon all eligible retirees. The answer is "Yes". There is a non-opt out class action lawsuit pending in District Court which provides that all eligible retirees will be bound by any settlement

approved by the Court. However, I am informed by Counsel that he may have an alternative that may be more acceptable to you.

In addition, page two of HB 3068 states on line 18, "The payment of refunds as provided in the settlement agreement shall represent a final and complete settlement of all claims." It is doubtful a court would approve any settlement that contains such an expression of the legislature unless the Court was convinced there was compliance.

Line 27, on the same page of the bill, also provides additional protection for the State. "In the event that the settlement agreement does not receive Judicial approval, no expenditure or refund payments shall be made pursuant to this section."

There is an additional very important aspect that should be considered as you go about your deliberations on this very important issue. Any proposed legislative settlement must be approved by Counsel for the military retirees and the Court. Counsel has sole authority, subject to court approval to make the determination what settlement is fair and reasonable for the class.

For that reason I have asked John Frieden, Chief Counsel for the Retirees, to appear here with me to respond to any questions you may have.

A few days ago I mailed to each of you a blue folder that I prepared early in the session for members of the House. This folder contains

several legal questions which had been asked of me by legislators regarding this issue--I prepared the questions, but the answers were all provided by Counsel who has been working on this project for the past five years. I know from personal experience that at this time of a legislative session, many of you would not have had time to review them. If anyone would like an additional copy, I have left them with the committee secretary.

I have also provided you a summary of action taken in 17 other states that have settled with their veterans. You may have noticed that Missouri, Iowa, Oklahoma, Colorado, Arkansas and New Mexico, all states geographically close to Kansas have provided or are in the process of providing full refund settlements, plus interest.

House Bill 3068 was introduced by the Federal and State Affairs Committee and referred to the committee on Taxation. That Committee had briefings earlier in the session and held a hearing on this subject. At that hearing I had asked the Retirees to have their Counsel appear before the committee and relate to them what would be an acceptable compromise solution. I had informed the Retirees that it was my observation and belief if there was to be a legislative solution, it would have to be for some amount less than the full amount to which they believed they were entitled.

I also suggested to them if they were indeed interested in some compromise legislative settlement, that they have their counsel, Mr. Frieden, appear before the Committee and present to them the parameters

of any such settlement that would be acceptable to the Retirees. I explained to them there was no historical state precedent for this type of settlement and it would be impossible to negotiate with 165 legislators divided between two houses.

For that reason I was very insistent that such testimony provide the committee with the absolute bottom line--a definitive dollar figure that would be acceptable should the legislature express an interest in such a solution. At two prior hearings, the Department of Revenue had stated the maximum potential state liability was between \$81 and \$85 million. Based on those figures and after receiving the approval of the 18 members of the Retired Military Committee, which have been providing direction on this matter, Mr. Frieden offered to reduce the interest rate from 12 percent to five percent and the total figure he gave the committee was \$64,340,805, payable over a two-year period.

HB 3068 as originally introduced, reflected that amount payable over a three-year period. I have reason to believe that three-year period would not be objectionable if that was necessary to accommodate the budget concerns of the legislature.

The \$64 million figure was not an arbitrary figure arrived at by Counsel and the Retiree Committee, and not a decision made in a vacuum. That figure was determined by a series of consultations with the Retirees after the Department of Revenue stated the potential liability for the State was \$81 to \$85 million.

Several days later, the Retirees became aware of a letter written by Gloria Timmer, the State Budget Director, to Representative Keith Roe, Chairman of the House Taxation Committee, in which she stated the potential liability for the State was \$91,586.000, some six and one-half million dollars more than the maximum the State had previously stated.

I sat in on a discussion of the Retirees in my conference room a few days later when the decision was made to let their original offer of settlement of \$64,000,000 stand, but it was a unanimous decision of the Retirees that was indeed the bottom line.

Before I go any further, I want to address the issue of attorneys fees. That subject has come up in every hearing in the House, the Governor has made comments about it, every news article comments about it and many legislators have asked me questions about it.

In 1989, the retirees retained the attorneys to file a class action lawsuit and for five long years they have been pursuing their legal remedies through the system. They have been all the way to the United States Supreme Court and won. They have been instrumental in bringing a halt to the discriminatory tax throughout the United States and are directly responsible for ending the tax which had been imposed in Kansas. They are now attempting to take each Retiree through a cumbersome, confused administrative process. And will continue to do so, absent a legislative resolution to the problem.

If the legislature does not provide an acceptable solution for settlement, the only alternative available to the veterans is to continue their fight through the courts which could be as much as another two year or more. Every mailing the attorneys send to these 19,000 retirees is as much as \$7 to \$12 thousand dollars. The attorneys have had to put on additional staff just to respond to the concerns and questions of the veterans. To date, the attorneys have been footing the entire expense with no absolute assurance they will ever be compensated.

If the case is settled by legislation, which would have to be approved by the Retirees counsel and the Court, the attorney fees will be determined by the Court on the basis of what is reasonable.

There is no contingency fee involved, there is no one-third or 25 percent as has been suggested in some instances. Following any settlement, the attorneys will present their expenses and number of hours involved through the years to the Court. The Court and the Court alone, will determine what should be reasonable attorney fees.

Let me restate that, the Court, and the Court alone, will determine reasonable attorney fees whether it is a legislative resolution, a court settlement or if the Retirees continue the action and obtain a court judgment, as most of you believe they will. Obviously, the longer the case goes on the more time will be spent by attorneys and the higher the fees will be.

You may recall what the State approved for the attorneys for KPERS was totally a contingency fee with no expense risk involved. You may recall the KPERS attorneys are not only being reimbursed for their out-of-pocket expenses, which I understand to date has been approximately \$2 million dollars, but will receive a contingency of 25 percent of the first \$50 million and 22 percent of amounts between \$50 and \$100 million.

If the State can pay its lawyers shouldn't the Retirees have the same right--especially when any class action fee has to be approved by the Court as reasonable and every retiree has the right to appear in court and voice his opposition before the fee is approved.

The one thing that is certain, if the legislature does not provide an acceptable compromise solution and the Retirees ultimately win in court, as nearly everyone believes they will, the State's liability which is increasing at the rate in excess of \$17,000 per day could be in excess of \$100 million dollars, payable in one lump sum.

This issue is not just risk management, but one of fairness and is not nearly as complicated as some try to make it. The State illegally taxed military retirement benefits and now the Retirees want the state to refund their money. They are not asking for a hand out, they are not asking for a gift, they are only asking for what the Court has determined is money which should not have been taken from them.

Approximately 10 percent of the retirees never paid this illegal tax in the first place. The Department of Revenue has stated they do not plan

to attempt to force that group to pay. The State has fought every step of the way to resist returning the money to those that did pay the tax. No reasonable person could conclude this is fair. In fact, when the Chair of the House Federal and State Affairs Committee asked Chief Counsel for the Department of Revenue if he thought this was fair, Counsel responded that fairness was not an issue of concern to state taxing officials. I do not believe that expresses the sentiment of any member of the legislature.

I respectfully submit Madam Chairman, the issue here has far more to do with fairness than it does with the application of legal principles. The retirees who refused to pay the tax received the benefit of the Supreme Court decision, but for those that paid the illegal tax, refund relief has been denied.

If we are talking about cost, you should know that the State is making each individual go through the administrative appeals process. That means between 19,000 to 21,000 individual appeals. The cost to each individual includes travelling to Topeka, on one or more occasions, testifying, paying a court reporter, compiling a record for appeal, amending eight years of tax returns and paying filing fees. The out-of-pocket cost to each retiree without paying attorney fees or travel expenses will exceed \$250.00. Depending on how many Retirees exhaust their administrative remedies, the total cost would most certainly well exceed a million dollars. Is that fair? Is it fair for the State to send the Retirees through the difficult process of administrative appeals only to end up back in court years later, trying to get their money back?

Is it fair for the Department of Revenue to have misled these people by telling them they did not need to exhaust administrative remedies and then get the Court to order them to exhaust?

Is it fair not to pay back taxes which were illegally taken from the Retirees?

If the tables were turned, would the State forgive a taxpayer from back taxes, penalties and interest if the taxpayer misinterpreted the law?

A just government cannot in good conscience illegally take money from its citizens and refuse to return it.

I noticed in the paper over the weekend, Senator Burke's suggestion. Senator Burke is a strong supporter of the Military Retirees and in favor of settling this issue this session as he stated to the press. He suggested amending this bill by adding the language "subject to appropriation". Originally, I could see no objection to that and I might have even suggested that at one time. But as you think that through, I doubt if the Retirees would sign off on any proposal that contains such language and it does not seem logical that the Court would consider that to be fair to the Retirees.

We have all heard the reports that the budget will continue to be tight for the next few years at least. It is conceivable that you could appropriate the money for the first year of a three-year settlement and a future legislature might determine different priorities for the second and

third year and ultimate settlement could be delayed for several more years.

As each of you know, this group of retirees is an aging class. Several of those eligible in this class action lawsuit when it was started five years ago are no longer with us today. Sad as it may be, if you accepted a three year payout and started this year, some number of those eligible would not be with us to collect their final payment. I think it would be cruel to build up potentially false hope by suggesting the legislature does want to settle this, but is not going to provide any real assurance.

As a practical matter, we all know one legislature cannot bind future legislatures, but I respectfully suggest it would be far more preferable to the Retirees if the legislature would offer an acceptable settlement without conditions. You will note, the House struck that specific condition from the bill they approved.

If it is the intent of the legislature to provide a settlement acceptable to the Retirees and the Court, both would need to have no reservations about that before the class action lawsuit was dismissed.

However, that is not a decision for me to make and one of the reasons I have asked Mr. Frieden to be here today. You can ask him that question in a few minutes and only he is authorized to tell you what would or would not be acceptable to the Retirees.

Chairman of the House Taxation Committee offered an amendment in committee to take the settlement back to \$40,000,000, payable over four years, subject to legislative appropriation. That language was stricken from the bill on the House floor and language inserted in the bill as it appears before you. The House approved the bill in its present form by a vote of 112 to 13.

In the debate in committee and again on the House floor it was evident that a large number of House members believed that Retirees were entitled to 100 percent refund, plus interest, as has been the policy of all the surrounding states that have settled, which I mentioned earlier in my comments.

As I conclude my comments, I would like to leave with you this thought. Is there any among you, if you had overpaid your taxes to the State and had a sizeable refund coming, that would not be irate if the State were to refuse to return your money? If you owe the State money, they not only assess you sizeable penalty, but 18% interest for every day you refuse to pay. The Retirees are not even asking for a return of all their money, only a portion of that to which they are rightfully entitled.

This issue is one of fairness.

If this committee chooses to recommend HB 3068 favorable, there are two minor amendments that need to be made. On line 21 of page three, the date should be changed from 1995 to 1994. In line 30, "statute book " should be changed to official state paper.

Mr. Frieden may suggest another amendment relative to the opt-out class.

Now Madam Chairman and members of the Committee, I will be here to repond to questions, but I would like to yield to Mr. Frieden, Counsel for the Retirees. He may have a brief statement, but he can more appropriately respond to any questions you may have.