

KANSAS TAX ABATEMENT OVERVIEW

Overview of Kansas Tax Abatement

There are two methods of obtaining real property tax abatement in Kansas. The first method is the issuance of revenue bonds pursuant to K.S.A. 12-1740-1749d, inclusive, as amended (the “IRB Act”). The second method is the constitutional method pursuant to Article 11, Section 13 of the Constitution of the State of Kansas and K.S.A. 79-213 and 79-251, as amended. This overview only discusses the industrial revenue bond method of obtaining property tax abatement.

Issuance of Revenue Bonds

K.S.A. 12-1740 permits cities and counties (each referred to herein as the “Issuer”) to issue revenue bonds for the purpose of paying the costs of purchasing, acquiring, constructing or equipping facilities for “agricultural, commercial, hospital, industrial, natural resources, recreational development and manufacturing purposes” and to enter into leases or lease-purchase agreements for such facilities with the party applying for the property tax abatement (referred to herein as the “Applicant”).

The IRB Act requires that the Issuer prepare a cost benefit report, conduct a public hearing, adopt an ordinance authorizing the issuance of the revenue bonds and follow certain other procedural requirements prior to issuing revenue bonds. Bond Counsel can provide a detailed description of the steps that must be followed to obtain property tax abatement.

Required Steps for Issuing Revenue Bonds

Deed of Property to Issuer. The IRB Act requires that the Issuer have a legal interest in the property that is subject to tax abatement. To satisfy this requirement, title to the property that will be subject to abatement is deeded to the Issuer. In some instances, in lieu of a deed, the property may be leased to the Issuer and then subleased back to the party applying for the property tax abatement (referred to herein as the “Applicant”).

Lease of Property to the Applicant. The Issuer will enter into a lease agreement with the Applicant. The term of the lease will generally be the same as the term of the property tax abatement, but may extend for a longer period in some circumstances. The Applicant will have the obligation to purchase the property at the end of the lease term. The Lease will require that the Applicant make lease payments during the term of the lease equal to the principal and interest payments due on the bonds.

Purchase of the Revenue Bonds

The Applicant is responsible for finding a purchaser for the revenue bonds. Revenue bonds may be purchased by a bank, by an underwriter or by the Applicant.

Applicant Purchased Bonds. This is commonly referred to as a buy your own bond tax abatement financing, and is the most common arrangement on tax abatement financings. For a buy your own bond financing, the bonds are sold to the Applicant. The Applicant then makes lease payments to itself. Under this structure, the bonds are commonly issued after the Applicant's lender has recorded its mortgage and advanced funds under its loan. When the property is transferred to the Issuer, it is transferred subject to the lender's mortgage. A diagram describing this method of tax abatement financing is attached as **Schedule 1**.

Bank and Underwriter Purchased Bonds. When revenue bonds are sold to a bank or to the public through an underwriter, the proceeds from the sale of the revenue bonds are made available to the Applicant and used to acquire and construct the property that will be subject to property tax abatement. The Applicant will agree to make lease payments under the lease which will then be passed on to the bank or the other owners of the revenue bonds.

Benefits of Issuing Industrial Revenue Bonds

Sales Tax Exemption Certificate. The Applicant may obtain a sales tax exemption certificate which may be used by the Applicant and its contractor to purchase construction materials, machinery and equipment if such items will be purchased with proceeds of the revenue bonds. K.S.A. 79-3606(d) exempts "all sales of tangible personal property or services purchased by a contractor for the purpose of constructing, equipping, reconstructing, maintaining, repairing, enlarging, furnishing or remodeling facilities for any political subdivision of the state . . . the total cost of which is paid from funds of such political subdivision . . . and which would be exempt from taxation under the provisions of this act if purchased directly by such political subdivision or district. This Section further provides that funds of a political subdivision include "the proceeds of any bonds."

K.S.A. 79-3606(d) sets forth the following mechanics for using the sales tax exemption certificate: "When any political subdivision of the state . . . shall contract for the purpose of constructing, equipping, reconstructing, maintaining, repairing, enlarging, furnishing or remodeling facilities, it shall obtain from the state and furnish to the contractor an exemption certificate for the project involved, and the contractor may purchase materials for incorporation in such project. The contractor shall furnish the number of such certificate to all suppliers from whom such purchases are made, and such suppliers shall execute invoices covering the same bearing the number of such certificate. Upon completion of the project the contractor shall furnish to the political subdivision . . . a sworn statement, on a form to be provided by the director of taxation, that all purchases so made were entitled to exemption under this subsection All invoices shall be held by the contractor for a period of five years and shall be subject to audit by the director of taxation. If any materials purchased under such a certificate are found not to have been incorporated in the building or other project or not to have been returned for credit or the sales or compensating tax otherwise imposed upon such materials which will not be so incorporated in the building or other project reported and paid by such contractor to the director of taxation not later than the 20th day of the month following the close of the month in which it shall be determined that such materials will not be used for the purpose for which such certificate was issued, the political subdivision . . . shall be liable for tax on all materials purchased for the project, and upon payment thereof it may recover the same from the contractor together with reasonable attorney fees. Any contractor or any agent, employee or subcontractor thereof, who shall use or otherwise dispose of any materials purchased under such a certificate for any purpose other than that for which such a certificate is issued without the payment of the sales or compensating tax otherwise imposed upon such materials, shall be guilty of a misdemeanor and, upon conviction therefor, shall be subject to the penalties provided for in subsection (g) of K.S.A. 79-3615, and amendments thereto."

Property Tax Abatement. Real property that is acquired with the proceeds of revenue bonds may be exempt from property taxation for a period of ten years. K.S.A. 79-201(a) *Second* states that any property “constructed or purchased in part with the proceeds of revenue bonds . . . shall be exempt from taxation to the extent of the value of that portion of the property financed by the revenue bonds and only for a period of 10 calendar years after the calendar year in which the bonds were issued.” Property used in any retail enterprise identified under SIC codes, major groups 52 through 59, inclusive, except facilities used exclusively to house the headquarters or back office operations of such retail enterprises, is not eligible for property tax abatement. A list of the prohibited retail enterprises is attached as **Exhibit A**. Although real property purchased with bond proceeds is 100% exempt from property taxes for a period of ten years, the Issuer will often require that the Applicant make certain payments in lieu of property taxes to the Issuer. It is common for an Issuer to require 50% payments in lieu of tax, which results in 10 years of 50% real property tax abatement. Kansas law treats all payments in lieu of tax the same as property tax payments.

Tax Status of Interest on Revenue Bonds

Federal Taxation. The interest paid on revenue bonds is generally subject to federal income taxation. If revenue bonds are used to finance certain projects, such as a project that will be used for manufacturing or processing, the interest paid on the revenue bonds may be exempt from federal income taxation. Bond Counsel should be consulted to determine whether interest paid on the revenue bonds may be exempt from federal income taxation.

State Taxation. The interest on all revenue bonds is exempt from state of Kansas income taxation. If the revenue bonds are purchased by the Applicant or a related party, the party purchasing the revenue bonds may not be able to receive the benefit of the tax-exempt interest. Tax counsel or an accountant should be consulted to determine the tax implications of purchasing revenue bonds.

Depreciation of Bond Financed Property

The Applicant should consult with its accountants and attorneys to determine how to depreciate bond financed property. It has been our experience that the Applicant will generally be treated as the owner of bond financed property for federal tax purposes. This accounting treatment is not uniform, and the Applicant and its accountants and attorneys should make their own determination.

More Information

For more information, please contact Gina M. Riekhof at (816) 221-1000, or visit the Gilmore & Bell website at www.gilmorebell.com.

Gilmore & Bell is one of the leading public finance law firms in the United States. The firm specializes in public finance transactions, serving as bond counsel or underwriters’ counsel in a wide variety of tax-exempt and taxable financings and providing tax and arbitrage rebate services in connection with tax-exempt financings. The firm also provides advice to cities, counties and states regarding economic development incentives, and handles commercial and corporate finance transactions and securities law matters. Gilmore & Bell has 51 attorneys and four offices, located in St. Louis and Kansas City, Missouri, Wichita, Kansas and Lincoln, Nebraska.

Schedule 1

Diagram for Applicant Purchased Bonds

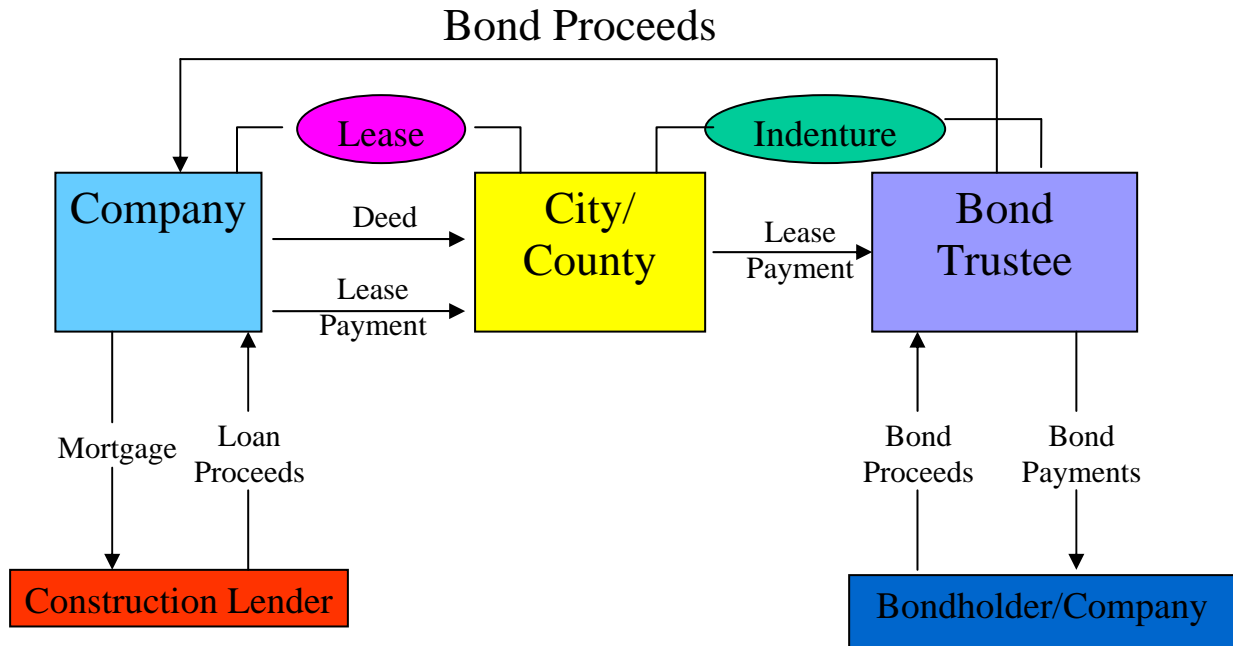


Exhibit A

Uses of Property not Eligible for Property Tax Abatement (SIC Codes Major Groups 52-59)

BUILDING MATERIALS, HARDWARE, GARDEN SUPPLY, & MOBILE HOME DEALERS

521 Lumber and Other Building Materials Dealers
523 Paint, Glass and Wallpaper Stores
525 Hardware Stores
526 Retail Nurseries, Lawn & Garden Supply Stores
527 Mobile Home Dealers

GENERAL MERCHANDISE STORES

531 Department Stores
533 Variety Stores
539 Miscellaneous General Merchandise Stores

FOOD STORES

541 Grocery Stores
542 Meat and Fish (Seafood) Markets, Including Freezer Provisioners
543 Fruit and Vegetable Markets
544 Candy, Nut and Confectionery Stores
545 Dairy Products Stores
546 Retail Bakeries
549 Miscellaneous Food Stores

AUTOMOTIVE DEALERS AND GASOLINE SERVICE STATIONS

551 Motor Vehicle Dealers (New and Used)
552 Motor Vehicle Dealers (Used Only)
553 Auto and Home Supply Stores
554 Gasoline Service Stations
555 Boat Dealers
556 Recreational Vehicle Dealers
557 Motorcycle Dealers
559 Automotive Dealers, Not Elsewhere Classified

APPAREL AND ACCESSORY STORES

561 Men's and Boy's Clothing and Accessory Stores
562 Women's Clothing Stores
563 Women's Accessory and Specialty Stores
564 Children's and Infants' Wear Stores
565 Family Clothing Stores
566 Shoe Stores
569 Miscellaneous Apparel and Accessory Stores

HOME FURNITURE, FURNISHINGS, AND EQUIPMENT STORES

571 Home Furniture and Furnishings Stores
572 Household Appliance Stores
573 Radio, Television, Consumer Electronics, and Music Stores

EATING AND DRINKING PLACES

581 Eating and Drinking Places

MISCELLANEOUS RETAIL

591 Drug Stores and Proprietary Stores
592 Liquor Stores
593 Used Merchandise Stores
594 Miscellaneous Shopping Goods Stores
596 Nonstore Retailers
598 Fuel Dealers
599 Retail Stores, Not Elsewhere Classified