

State of Kansas

Kansas Department of Revenue
Division of Property Valuation

The following appraisal directive is adopted by the director of property valuation pursuant to K.S.A. 79-505:

DIRECTIVE #98-032: Classification and valuation of commercial and industrial machinery and equipment under construction.

A question has arisen as to how commercial and industrial machinery and equipment, which is under construction on January 1st, should be valued and classified for property tax purposes. Such property shall be listed at its retail cost when new and depreciation shall begin the first year the property is listed for taxation without regard to the stage of completion.

Prior to this directive, there were two schools of thought as to how such property should be classified. These two views have differing tax ramifications, particularly after the Kansas Supreme Court decision in *Board of Leavenworth County Comm'rs. v. McGraw Fertilizer Serv., Inc.*, 261 Kan. 901, 933 P.2d 698, *modified* 261 Kan. 1082, 941 P.2d 1388 (1997). If the property is considered to be "commercial and industrial machinery and equipment," it is valued in accordance with the constitutional formula set forth in art. 11, § 1 of the Kansas Constitution for such property and it is assessed at 25%. If the property is not yet considered to be commercial and industrial machinery and equipment, then it is classified as "other" personal property and it is value based upon its fair market value and it is assessed at 30%.

In Attorney General Opinion #97-97, the attorney general opined that: "commercial and industrial equipment that otherwise meets the criteria for classification as such does not become 'other' property to be valued at market and assessed at a different rate merely because it is not yet in operation." The attorney general based the opinion upon a common person's understanding of the term "commercial and industrial machinery and equipment" set forth in art. 11, § 1 of the Kansas Constitution.

County appraisers shall value commercial and industrial machinery and equipment that is under construction on January 1st in accordance with Attorney General Opinion #97-97 and the formula set forth in art. 11, § 1 of the Kansas Constitution. County appraisers shall construe the term "retail cost when new" for valuation purposes consistently with the aforementioned *McGraw Fertilizer* case. County appraisers shall assess such property at 25%.

Art. 11, § 1 of the Kansas Constitution requires that commercial and industrial machinery and equipment be valued based upon its retail cost when new less straight-line depreciation over its economic life or a seven-year period, whichever is less.

When applying this constitution formula to commercial and industrial machinery and equipment that is under construction on January 1st, county appraisers shall depreciate the property in the same manner as other property in that subclass. For example, a new desk that is acquired in the midst of a year is listed the immediately following January 1st and it is allowed one year of depreciation the first year it is listed. Similarly, here, when commercial and industrial machinery and equipment is constructed on site commencing in the midst of a year, it shall be listed the immediately following January 1st and it shall be allowed one year of depreciation the first year it is listed. The second January 1st the property is listed, it shall be allowed two years of depreciation. Depreciation for the following years will follow suit in accordance with the language in the Constitution.

County appraisers shall use the total retail cost when new each January 1st as the starting point for each year's valuation. The retail cost when new of commercial and industrial machinery and equipment that is under construction will typically increase each January 1st until such time as the construction is complete, then the cost will generally become consistent absent some unusual circumstance.

In summary, commercial and industrial machinery and equipment that is under construction on January 1st shall be considered to be commercial and industrial machinery and equipment for valuation and classification purposes. Depreciation shall be allowed commencing with the first year the property is listed. The retail cost when new of the property shall be determined each January 1st until the construction is complete and the full retail cost when new of the machinery and equipment is known and established.

APPROVED: June 12, 1998

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