



STATE OF KANSAS

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ATTORNEY GENERAL OPINION NO. 89- 85

Terry D. Hamblin
Director of Property Valuation
Kansas Department of Revenue
Docking State Office Building
Topeka, Kansas 66612

Re: Constitution of the State of Kansas--Finance and
Taxation--System of Taxation; Classification;
Exemption

Synopsis: The definitions of "merchant," "manufacturer" and
"inventory" in K.S.A. 1988 Supp. 79-201m are
drafted broadly enough to encompass coal and gas
held by a public utility for resale or to use in
generating electricity. Therefore, such property
is eligible for a tax exemption as merchants' or
manufacturers' inventory pursuant to article 11,
section 1 of the Kansas Constitution. Cited
herein: K.S.A. 1988 Supp. 79-201m; 79-213; K.S.A.
79-5a01 et seq.; K.S.A. 1988 Supp. 79-3602;
K.S.A. 84-9-109; K.S.A. 79-1001 et seq.
(repealed, L. 1988, ch. 375, §9); Kan. Const.,
Art. 11, §1.

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Dear Director Hamblin:

You request our opinion regarding the classification
amendment, Kan. Const., Art. 11, §1, and certain
exemptions found therein. Specifically your questions are as
follows:

"1. Is it possible for a public utility as defined by K.S.A. 1988 Supp. 79-5a01 to be a merchant and/or manufacturer as defined by K.S.A. 1988 Supp. 79-201m?

"2. If yes, is 'gas stored in an underground storage facility' and/or 'coal' held by an electricity generating facility 'inventory' as defined by K.S.A. 1988 Supp. 79-201m?

"3. If the answers to questions 1 and 2 are yes, then under Article 11, Section 1 of the Constitution of the State of Kansas (the 'Classification Amendment') are 'merchant's and manufacturer's inventories' owned by a public utility as defined by K.S.A. 1988 Supp. 79-5a01 exempt from property taxation?"

You advise that as Director of Property Valuation you are responsible for determining eligibility for exemption of a public utility's merchants' and manufacturers' inventory. K.S.A. 1988 Supp. 79-213(n); 79-5a01 et seq. Pursuant to this statutory authority, you have determined that a public utility may be a merchant or manufacturer and that gas stored in an underground storage facility and coal held by an electricity generating facility are inventory and that, therefore, such gas and coal are exempt from property taxes pursuant to article 11, section 1(b)(2) of the Kansas Constitution. You have been questioned regarding the appropriateness of this determination and thus ask us to review your interpretation of the applicable statutes and constitutional provision, keeping in mind the deference afforded an agency's interpretation of provisions it administers. See, e.g., In re Tax Appeal of R. & R Janitor Service, 9 Kan. App. 2d 500, 503 (1984); United Parcel Service, Inc. v. Arnold, 218 Kan. 102, 107 (1975).

Your first two questions require interpretation of the definitions found in K.S.A. 1988 Supp. 79-201m:

"To the extent herein specified, merchants' and manufacturers' inventory shall be and is hereby exempt from all property or ad valorem taxes levied under the laws of the state of Kansas.

"As used in this section:

"(a) 'Merchant' means and includes every person, company or corporation who shall own or hold, subject to their control, any

tangible personal property within this state which shall have been purchased primarily for resale in the ordinary course of business without modification or change in form or substance, and without any intervening use, except that, an incidental use, including but not limited to the rental or lease of any such property, shall not be deemed to be an intervening use;

"(b) 'manufacturer' means and includes every person, company or corporation who is engaged in the business of transforming, refining or combining materials and labor to convert tangible personal property from one form to another including packaging; and

"(c) 'inventory' means and includes those items of tangible personal property that: (1) Are primarily held for sale in the ordinary course of business (finished goods); (2) are in process of production for such sale (work in process); or (3) are to be consumed either directly or indirectly in the production of finished goods (raw materials and supplies). . . ."

It is our understanding that the gas in question is being held for resale, and the coal is being used to generate electricity. A utility engaged in the business of purchasing gas for resale without modification or change in form appears to meet the definition of a merchant if gas is determined to be tangible property. Similarly, a utility engaged in the business of transforming coal into electricity may be considered a "manufacturer" if both the coal and the electricity created therefrom are considered tangible personal property. Clearly coal is tangible personal property. Further, legislative definitions of the term "tangible" would indicate that gas and electricity are tangible personal property as well. See K.S.A. 1988 Supp. 79-3602(m)(B); Attorney General Opinion No. 88-158. Courts in other jurisdictions have adopted the notion that gas and electricity are tangible. Annot. 17 A.L.R.3d 7, 102 (1968); Annot., 48 A.L.R.3d 1060 (1973). It is therefore our opinion that your interpretation of the term manufacturer, as used in K.S.A. 1988 Supp. 79-201m, to include public utilities engaged

in the business of generating electricity, and of the term merchant to include public utilities which purchase gas for resale is neither arbitrary nor capricious and would be upheld by a court of law. Additionally, we believe interpreting the term "inventory" to include gas held of resale and coal used to generate electricity is valid as well. We must therefore look to the provisions of article 11, section 1 of the Kansas Constitution to determine whether this property is entitled to an exemption as "merchant's and manufacturer's inventories" under that provision.

Article 11, section 1 provides in part:

"Property shall be classified into the following classes for the purpose of assessment and assessed at the percentage of value prescribed therefor:

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"Class 2 shall consist of tangible personal property. Such tangible personal property shall be further classified into six subclasses, shall be defined by law for the purpose of subclassification and assessed uniformly as to subclass at the following percentages of value:

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"(c) Public utility tangible personal property. 30%

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(2) [M]erchant's and manufacturer's inventories . . . shall be exempt from property taxation."

Article 11, section 1 does not define the term "merchant's and manufacturer's inventories." In construing a constitutional provision, consideration should be given to what appears to have been the intendment and understanding of the people at the time of its adoption. State ex rel. Frizzell v. Highwood Service, Inc., 205 Kan. 821, 825, 826 (1970). Its language should be interpreted to mean what the words imply to men of common understanding. Id. at 825. K.S.A. 1988 Supp. 79-201m was enacted two years after article 11,

section 1 was adopted. At the time of adoption of article 11, section 1, gas held by a public utility for resale and coal used by a public utility to generate electricity were not considered merchant's and manufacturer's inventory under K.S.A. 79-1001 et seq. (repealed, L. 1988, ch. 375, §9) because all utility property was treated separately under K.S.A. 79-5a01 et seq. For these two reasons it is arguable that the legislature and the voting public did not intend for this property to be considered merchants' and manufacturers' inventory. However, commonly used definitions of the terms merchant, manufacturer and inventory at the time of adoption were similar to the definitions used in K.S.A. 1988 Supp. 79-201m. The American Heritage Dictionary 821, 796, 688 (New College Edition 1976); Black's Law Dictionary 890, 870, 740 (5th ed. 1979). See also K.S.A. 84-9-109(4); Oldfather "Floor Plan Financing Under Article 9 of the Uniform Commercial Code," 14 U. Kan. L. Rev. 571, 575, 576 (1966). Further, subsequent enactment of K.S.A. 1988 Supp. 79-201m is indicative of legislative intent to include the type of property in question as merchants' or manufacturers' inventory. We have found nothing in recorded legislative history to evidence a contrary intent. Thus, your interpretation appears to coincide with commonly held notions of what constitutes merchants' or manufacturers' inventory for purposes of exemption pursuant to the Kansas Constitution. We find nothing in article 11, section 1 which would preclude personal property of a public utility from being considered merchants' or manufacturers' inventory entitled to exemption from taxation.

Very truly yours,



ROBERT T. STEPHAN
Attorney General of Kansas



Julene L. Miller
Deputy Attorney General

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