MINUTES

MONTANA HOUSE OF REPRESENTATIVES
52nd LEGISLATURE - 2nd SPECIAL SESSION

COMMITTEE ON TAXATION

Call to Order: By Rep. Dan Harrington, Chairman, on July 8, 1992, at 8:30 a.m.

ROLL CALL

Members Present:
Dan Harrington, Chairman (D)
Bob Ream, Vice-Chairman (D)
Ben Cohen, Vice-Chair (D)
Ed Dolezal (D)
Jim Elliott (D)
Orval Ellison (R)
Russell Fagg (R)
Mike Foster (R)
Bob Gilbert (R)
Marian Hanson (R)
David Hoffman (R)
Jim Madison (D)
Ed McCaffree (D)
Bea McCarthy (D)
Tom Nelson (R)
Mark O'Keefe (D)
Bob Raney (D)
Ted Schye (D)
Fred Thomas (R)
Dave Wanzenried (D)

Members Excused: Rep. Stang

Members Absent: None

Staff Present: Lee Heiman, Legislative Council
Jill Rohyans, Committee Secretary

Please Note: These are summary minutes. Testimony and discussion are paraphrased and condensed.

Announcements/Discussion: None

HEARING ON HOUSE BILL 10

Presentation and Opening Statement by Sponsor:

REP. BARDANOUVE, House District 16, Harlem, said that although some computer software has been assessed, the assessment has not been equally enforced across the state. Computers are assessed, but software is much more expensive and valuable. He said local governments could benefit considerably from software assessments as many large corporations and banks own software worth thousands of dollars.

Proponents' Testimony:

There were no proponents.

Opponents' Testimony:

STEVE WHITE, Advance Business Computing Corporation, presented his testimony to the Committee (Exhibit #1).

Questions From Committee Members:

REP. ELLIOTT asked how software is currently assessed.

Mr. Adams said software is currently included in personal property schedules by administrative rule at acquired cost with depreciation over a four year period.

REP. NELSON asked if the complimentary computer discs he has received from various entities in the course of his business are taxable.

Mr. Adams replied if the discs were not purchased, they are not taxed. If, for example, a person owns Word Perfect 5.1 discs, they are not taxed unless they are treated as an asset and depreciated for tax purposes. If a person is buying the service from Word Perfect, it is treated like an intangible. However, if the program is treated as property to be purchased and/or sold, it would be taxed.

REP. NELSON asked if the rights to a program are taxable if a person develops his own program and sells it, but retains the rights.

Mr. Adams said he did not know.

REP. REAM asked Mr. Adams if this is a valid bill.

Mr. Adams replied it is valid. The computer tax section has not been looked at for a number of years and the evolution of the computer industry has been tremendous. He said the software area needs to be addressed and this bill clarifies procedures.

REP. GILBERT said DOR doesn't seem to be able to process returns in a timely fashion and he wondered how these procedures could be implemented any time soon.

Mr. Adams replied a different division would be handling the computer software provisions. The rules are updated every year in personal property tax procedures.

Closing by Sponsor:

REP. BARDANOUVE said the idea for the bill was brought to him by a businessman. Some software is being taxed, some is not, and this bill tells DOR it needs to be done uniformly. Software is an increasingly important and valuable arm of business and should be assessed. If all software is assessed equally, the costs are passed on to the consumer and no one would have an unfair competitive advantage. He encouraged DOR to "beef up" their assessment and enforcement procedures.

HEARING ON HOUSE BILL 11

Presentation and Opening Statement by Sponsor:

REP. BARDANOUVE, House District 16, Harlem, said this bill was introduced in the 1989 session and supported by Auditor Bennett in a recent legislative session. The bill would eliminate the Montana Life and Heath Insurance Guaranty Association tax offset. **REP. BARDANOUVE** said the state is, in essence, paying for insurance of the insurance industry which is not fair. Banks pay for their own and the insurance industry should not have their insurance paid for by statutory appropriation. **REP. BARDANOUVE** said the fiscal note indicates the cost is approximately $700,000 per year. He said the state should not be providing free insurance for any segment of Montana business.

Proponents' Testimony:

There were no proponents.

Opponents' Testimony:

Michael J. Mulroney, General Counsel, Montana Life and Health Insurance Guaranty Association, presented testimony in opposition to the bill (Exhibit #2).

Patrick M. Driscoll, American Counsel of Life Insurance, presented testimony in opposition to the bill (Exhibit #3).

Tom Hopgood, Health Insurance Association of America, said his organization represents half of the private health insurers in the state. He said the insurance industry, unlike other industries in the state, is highly regulated. The regulations take up 600 pages in the codes and the industry is under the control of the State Auditor. When an insurance company gets into financial difficulty, the rest of the insurance companies contribute to the guaranty fund to pay off that company's policy holders. The Guaranty Association members were assessed between $30 and $35 million to cover Life of Montana's debts. The assessments are being paid off on a contractual basis by the Guaranty Association. The contract is basically an interest free loan to the state by the companies in the Association. One of the terms of the contract was that the Association's member companies would be allowed to credit their assessments against premium taxes. If HB 11 passes and the premium tax offset is repealed the terms of the contract will have been violated, and the state will undoubtedly be sued. He referred to the technical note on the fiscal note, "The retroactive applicability of the bill may face a constitutional challenge".

Steve Browning, State Farm Insurance, presented his testimony in opposition to the bill (Exhibit #4).

Larry Akey, Montana Association of Life Underwriters, said his organization opposes the bill because it is a tax against insurance consumers as increased costs are not paid by the companies but passed on to the customer. The health care crisis would be exacerbated by this bill as increased taxes would be passed on to higher health care costs.

Questions From Committee Members:

REP. NELSON asked if Blue Cross Blue Shield belongs to the Guaranty Association.

Mr. Hopgood replied the "Blues" do not belong. They do not pay premium taxes, but neither do they get the tax offset.

REP. RANEY asked if the Department of Revenue (DOR) had reviewed

the bill for the constitutionality aspect of impairing the obligation of contracts as it applies to the state's contracts with the insurance companies through the Guaranty Association.

Mr. Adams replied DOR is not the agency that deals with the contract procedures and suggested the Auditor would be the appropriate office to contact.

REP. RANEY asked to have the Auditor submit an opinion on the constitutionality issue.

REP. GILBERT said the fiscal note indicates a fiscal impact of $3.5 million each year. He asked Mr. Hopgood if that is correct.

Mr. Hopgood replied that is essentially correct. The total assessments as a result of the Life of Montana failure were approximately $30 - $35 million. There have been $20 million in credits taken to date and there will be another $20 - $25 million in credits taken over the next four years.

REP. GILBERT asked if the "Blues", if effect, have a $3.5 million competitive economic advantage over the other insurance companies that are members of the Guaranty Association.

Mr. Hopgood answered they do.

REP. REAM expressed concern about additional insolvencies, including two major companies, which will be impacting the state in the near future.

<u>Closing by Sponsor</u>:

REP. BARDANOUVE closed by saying the insurance companies do not pay one penny in costs. They pay a 2% premium assessment on policies which has nothing to do with the insurance fund. Insurance companies do not pay the corporation license tax, however, they pay the 2% assessment in lieu of the corporation tax. If they are making a loan to the state they are using the people's money to make the loan. If the companies increase the assessment to cover the costs it would constitute a loan. However, they have not, and therefore, **REP. BARDANOUVE** felt they are the recipients of free insurance from the state. He said the consumer will have to pay as they always do. He urged the Committee to give the bill serious consideration.

CHAIRMAN HARRINGTON asked **REP. RANEY** to contact the Auditor for the constitutionality information and also to address the fiscal impact of any anticipated insolvencies.

HEARING ON HOUSE BILL 12

Presentation and Opening Statement by Sponsor:

REP. BARDANOUVE, House District 16, Harlem, said the state has historically had large cash reserves against which the state could borrow. Cash reserves are extremely low at present and there is not enough money in the highway fund to pay contractors if the federal money does not arrive by July 15. One way to increase the cash balance is to move the property assessment payments to the 25th of May so that they can arrive in Helena before June 31. If the payments are not received by July 1, the TRANS notes cannot be paid. He submitted proposed amendments submitted by DOR (Exhibit # 5).

Proponents' Testimony:

Denis Adams, Director, DOR, said he supports either backing up the payment date or asking the County Treasurers to accelerate payments. He said the Department was going to submit similar legislation and urged the Committee to support the bill.

Opponents' Testimony:

Gordon Morris, Executive Director, Montana Association of Counties (MACO), said the June 20th date would work a hardship on counties as June 30 is the end of the FY for counties. This bill would require counties to close out tax collections for state distribution purposes by June 20th. He asked what is the intent of changing the November date in subsection 3 and suggested subsection 3 be stricken.

Cort Harrington, Montana County Treasurers Association, said the Treasurers felt the Governor's proposal was unworkable and prefer Rep. Bardanouve's plan. However, the Association opposes the bill because the estimated $17 million in proceeds is unrealistic. He felt the figure would be closer to $3 - $4 million. The Fiscal Analyst's review of the Governor's proposal indicated $7 million would be an optimistically high figure. Most County Treasurers hold their books open at the end of May in order to include the receipts they get early in June that are postmarked May 31. He agreed with Mr. Morris that this will be a burden on County Treasurers. The bill does not solve the problem it was intended to address.

Dave Ashley, Department of Administration, said that while taxpayer dates are intact, the County Treasurers have five days less time to remit the money to the state. He felt the bill could be married to Rep. Cobb's bill, HB 13, so that both the

taxpayers and Treasurers must comply with an accelerated date of ten days. He said the November date change is simply a cash management measure and is not important.

Questions From Committee Members:

REP. McCAFFREE asked if there will be a fiscal impact on counties due to a loss of interest for the accelerated days.

Mr. Adams replied he didn't know, but would get the information for the Committee.

REP. ELLISON asked what percentage of taxes are paid in the last few days of the period.

Mr. Harrington replied most taxes are paid on the last day. As long as they are postmarked May 31, they are considered to be paid on time.

Closing by Sponsor:

REP. BARDANOUVE closed saying there is always some concern when procedures are changed. The bill has some inconveniences, but also some possibilities. He said the accelerated payment procedure would work better in the long run. He added he would have no objection to working out the November date to the satisfaction of DOR.

HEARING ON HOUSE BILL 15

Presentation and Opening Statement by Sponsor:

REPRESENTATIVE COHEN, District 3, Whitefish, said the bill has been introduced to correct an error made during the 1989 special session. HB 20, passed in that session, provided that all personal property valued above 9% would be reduced to the 9% level. It then provided a block grant to the counties to reimburse them the difference between 9% and the county's taxable value of the property at the 1989 level. HB 15 would base reimbursement on the current value of the property that was reduced to 9% from a higher valuation in 1989. Reimbursements are still being made to counties based on the 1989 value of the property even when the property has left the county or depreciated significantly since 1989. He submitted amendments from DOR which would have the effect of depreciating the property at 10% a year instead of a one time drop to current level (Exhibit #6). **REP. COHEN** presented review of reimbursements for

the 1991 tax year (Exhibit #7). The reimbursement (block grant) total for 1991 was $19.1 million. The state cannot continue to pay that amount of money for property that has depreciated. The amendments, if adopted, would save the state $1.9 million the first year, $3.8 million the second year, growing by 10% per year until the property is fully depreciated.

Proponents' Testimony:

There were no proponents.

Opponents' Testimony:

Gordon Morris, MACO, said the Governor and the legislature promised local governments that they would be held harmless when the personal property values were dropped to the 9% level. The reimbursement was based on a dollar for dollar schedule. He expressed concern the stricken language on page 4, section 7, confuses the intent of the legislation. He wondered what would happen to other local government entities such as counties, fire districts and airport districts.

Alec Hanson, Montana League of Cities and Towns, presented a letter in opposition to the bill from **Chuck Stearns, Finance Officer/City Clerk, Missoula,** in opposition to the bill (Exhibit # 8). **Mr. Hanson** said the bill completely violates the agreement made in 1989. It relieves the legislature from any responsibility to reimburse local governments over a 10 year period. Schools and local governments will lose $1.9 million per year for the next 10 years. Cities and towns cannot take another hit. He said the legislation is not fair and local governments should be continued to be held harmless.

Phil Campbell, Montana Education Association (MEA), said 60 - 65% of the local school dollars are affected by the bill. The language is confusing and, although he had not seen the amendments, if the intent is to take money away from schools, he would oppose the bill.

Questions From Committee Members:

REP.McCAFFREE asked why the reference to local governments was stricken on p. 4, subsection 7.

REP. COHEN the Legislative Council bill drafter made the correction in the code to conform to an Attorney General's ruling.

REP.REAM asked why the reimbursement seems to be creeping up from the 1989 fixed level.

Mr. Adams said there have been mill levy increases which in turn cause the reimbursement amounts to increase. He noted the personal property that was lowered to the 9% level was "lumped in" with all the other property in that class.

REP. REAM asked if the reimbursement remains the same even if there is a substantial shift in the personal property in a given county - if a large amount of equipment is moved out.

Mr. Adams said yes, it remain the same since there is no way to separate which was originally a higher level property.

REP. GILBERT asked if the state is still reimbursing for property that was in a county in 1989 even if it is not there now.

Mr. Adams said that is correct.

REP. GILBERT asked if this was fair to the taxpayers.

Mr. Morris said he helped craft the reimbursement mechanism in 1989. The intent at that time was, and to his knowledge was until this hearing, that if the property was no longer in the county, the local government would not be reimbursed for it. He said it is not fair to reimburse for it if it is not there. If it still is in the county, then the reimbursement should continue.

Closing by Sponsor:

REP. COHEN said the premise behind the reduction of personal property taxes in HB 20 was that the tax reduction would stimulate an increase in business equipment and property in the counties which would expand the tax base for local governments. He said he doesn't blame local governments for not wanting to lose this income. Sixty-five percent of the money goes to school equalization and the university system. So, in effect, we give money to schools one way or another. Local governments must learn to live on their own tax base and this bill is a graduated method of correcting a large problem.

ADJOURNMENT

Adjournment: 10:30 a.m.

Rep. Dan Harrington, Chair

Jill D. Rohyans, Secretary

DH/jdr

HOUSE OF REPRESENTATIVES

TAXATION COMMITTEE

ROLL CALL DATE 7/8/92

NAME	PRESENT	ABSENT	EXCUSED
REP. BEN COHEN, VICE-CHAIRMAN	✓		
REP. ED DOLEZAL	✓		
REP. JIM ELLIOTT	✓		
REP. ORVAL ELLISON	✓		
REP. RUSSELL FAGG	✓		
REP. MIKE FOSTER	✓		
REP. BOB GILBERT	✓		
REP. MARIAN HANSON	✓		
REP. DAVID HOFFMAN	✓		
REP. JIM MADISON	✓		
REP. ED MCCAFFREE	✓		
REP. BEA MCCARTHY	✓		
REP. TOM NELSON	✓		
REP. MARK O'KEEFE	✓		
REP. BOB RANEY	✓		
REP. BOB REAM, VICE-CHAIRMAN	✓		
REP. TED SCHYE	✓		
REP. BARRY "SPOOK" STANG			X
REP. FRED THOMAS	✓		
REP. DAVE WANZENRIED	✓		
REP. DAN HARRINGTON, CHAIRMAN	✓		

HOUSE TAXATION

EXHIBIT #1 7/8/92

TESTIMONY OF R. STEPHEN WHITE

HB 10 - 07/08/92

As the principle owner of Advance Business Computing Corporation located in Helena, I speak in opposition to HB 10 for the proposed inclusion of computer software as property for taxation purposes.

For the last 14 years my company has provided consulting and software to companies in over 25 states and four countries. Presently over 75% of our business is in Montana, with Montana businesses. The software business is different than any other type of business today. Software is typically not sold to a business or individual, but only licensed for use. All software is protected by US Copyright to prevent unlawful distribution. The license agreement from my company, or any other software business specifically states that the purchasing company is only obtaining a legal right (license) to use the software.

In the case of my company, the situation becomes even more complicated for taxing purposes. It is common for my clients to request modifications to the purchased package. These changes may range in cost from $50 to thousands of dollars. My client does not own the modifications, but only has obtained a right to use them.

To place a taxable value on a company's business software is very difficult. In my company's case, we pay income taxes on all revenue derived from these programming changes, and find it very unfair to have the result of our efforts taxed again as personal property.

If all our clients' property taxes increased with the result of our contracted work, the end result would be disastrous to my company.

Software cannot be treated in the same way as hardware. Software is not a fixed and easily defined entity in any business. In many cases it is not as simple as looking at the prices of software in a computer store, and taxing it's value by those prices. It is even possible that businesses may opt for software piracy than risk including a software purchase in a tax schedule.

In summary, the taxation of computer software as property is not as simple as it may appear. To tax custom software in any business would cause an unfair burden to both the user and developer of new software systems.

I urge you to oppose this bill.

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HOUSE TAXATION

EXHIBIT #2 7/8/92

MONTANA LIFE AND HEALTH INSURANCE GUARANTY ASSOCIATION

AL D. PONTRELLI, CLU, EXECUTIVE DIRECTOR

July 8, 1992

Representative Francis Bardanouve
Representative Dan Harrington
State Legislature
State Capitol
Helena, MT 59620

RE: HB-11

Gentlemen:

The purpose of this letter is to outline our opposition to HB-11 which would eliminate the Montana Life and Health Insurance Guaranty Association (the "Association") premium tax offset; amending Section 33-10-230, MCA; and providing an immediate effective date and a retroactive applicability date.

THE ASSOCIATION

The Association was created by statute to protect policy owners, insured, beneficiaries, annuitants, and assigns of life insurance policies, health insurance policies, annuity contracts, and supplemental contracts, subject to certain limitations, against failure in the performance of contractual obligations due to the impairment of the insurer issuing such policies or contracts. Section 33-10-201, MCA et seq.

The Association's membership consists of all life and health insurance companies licensed to conduct business in Montana. Presently there are some 950 member companies that form the Association.

In general terms the Association's statutory responsibilities are triggered by a court order finding a member company impaired or insolvent. In connection with the insolvency of a member company domiciled in Montana the Association's obligation is to assess all of its member companies an amount or amounts sufficient to meet the Association's statutory responsibilities outlined above. Such assessments are limited on an annual basis and may be made only when required. Section 33-10-227(4) and (5), MCA. That is if enough funds cannot be assessed in one year to cover an insolvency additional assessments must be made thereafter until the Association's responsibilities have been met but each annual

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assessment is limited by statute and only one assessment may be made in any one calendar year. In practical terms this means that all member companies become the ultimate creditor of the insolvent company (through the Association) as they are obligated to pay the liabilities of the insolvent company by such assessments less the amount recovered from its assets. Since the creation of the Association, member companies have been statutorily permitted to write off such assessments over a five-year period as an offset against premium taxes paid by such companies to the State of Montana. Many other states have similar write-off provisions while some states allow no write-off or permit such write-off over a longer time period.

LIFE OF MONTANA

For many years Life of Montana, located in Bozeman, has been the only operating life and health insurance company domiciled in this state. Life of Montana was found to be impaired in 1987 and declared insolvent by court order on January 7, 1988. The Association formally and actively participated in all phases of the Life of Montana problem in support of the Commissioner of Insurance since it was first informed of the company's potential impairment. Upon the finding of insolvency the Association employed experts to initiate a thorough study of the best ways to meet its statutory obligations and in December of 1987 began to assess its member companies for sufficient funds to meet the Association's legal obligations to policyholders. Since the amount each member company may be assessed is limited in any one year by statute, a program of future required assessments was finalized in 1988 as the size of the insolvency was ascertained. In furtherance of this program additional assessments were made in 1988 and 1989 and will be made each year concluding in 1992. HB-11 if enacted would deny offset of these assessment amounts against the premium tax liability of the member companies paying such assessments for each year after 1991. Thus, while the Association clearly complied with its legal obligations arising out of the insolvency of Life of Montana, HB-11 would now deny the benefit of the offset to members of the Association "after the fact" i.e., after the Association had met its duty but before it could realize the corresponding benefit provided by statute at the time the duty was met. Had the Association been able to assess its members for the total cost of the insolvency in 1987 (which by statute it could not) then the total offset of all assessments would have been assured even under HB-11. While no one could argue against the manifest unfairness and anti-business aspects of

HB-11, the Association believes the bill violates at least two provisions of the Montana Constitution and at least one provision of the U. S. Constitution thereby costing the Association's members some twenty million dollars in unlawful additional premium tax liability.

CONTRACTUAL RELATIONSHIP

The Association believes it contracted in good faith with the Commissioner of Insurance (as liquidator of Life of Montana) to carry out the Association's statutory obligations with respect to the insolvency of Life of Montana and the Association believes the terms of that contract cannot now be lawfully impaired by legislation in the form of HB-11. The Association further believes that the evidence establishes such contract and the Commissioner of Insurance will be estopped to deny such contract.

Under Section 33-10-220(2), MCA, the Commissioner of Insurance may take over the duties and powers of the Association if it fails to act within a reasonable period of time during the liquidation of an insolvent insurer. Under Section 33-10-205(1)(e), MCA, the Association has the power to negotiate and contract with any liquidator, rehabilitator, supervisor or ancillary receiver to carry out the powers and duties of the Association.

Under Section 28-2-802, MCA, an existing legal obligation is good consideration for a promise to an extent corresponding with the extent of the obligation. Thus, the Association was empowered to enter into a contract with the Commissioner of Insurance to carry out the Association's duties and powers with respect to the insolvency of Life of Montana and the obligations of both parties became fixed as of the date of the insolvency of Life of Montana or within a reasonable time thereafter when the Commissioner elected not to take over the duties and powers of the Association with regard to the insolvency. In short, a contract was entered into whereby the Association and not the Commissioner of Insurance would undertake its responsibilities with regard to the insolvency. The Association has promised to fulfill its obligations and has met its contractual responsibilities, in part, by assessing its members annually to the extent permitted by law. The Commissioner has promised to fulfill her obligations and has met her contractual responsibilities, in part, by forwarding to the Association some one million dollars in cash which she received from the sale of certain assets of Life of Montana.

At the time of entering into the contract the law provided the offset HB-11 denies.

CONSTITUTIONAL VIOLATIONS

Under Article II, Section 31 of the Montana Constitution the legislature may not pass a law impairing the obligation of contracts. Under Article XIII, Section 1(3) of the Montana Constitution the legislature may not pass a law retrospective in its operations which imposes on the people a new liability in respect to transactions or considerations already passed. Under Article I, Section 10 of the U. S. Constitution no state may pass a law impairing the obligation of contracts. The Association believes HB-11 violates these provisions and that a court or courts of competent jurisdiction would so hold.

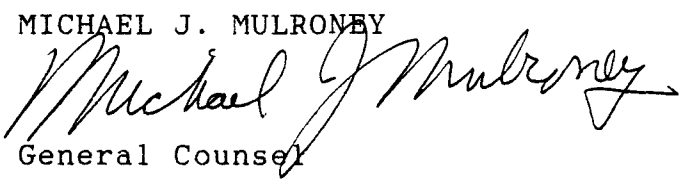
CONCLUSION

Since HB-11 violates both the Montana and U. S. Constitution it should not be enacted into law and accordingly, the Association herewith registers its opposition to the bill.

The Association believes that the foregoing should be of interest to the bill's sponsor and to the chairman of the Committee on taxation which will consider this bill. Should either of you or any member of the Committee request, the Association will provide a person to answer any questions concerning HB-11 at any hearing or at your convenience.

Sincerely,

MICHAEL J. MULRONEY



General Counsel

MJM/vjz

cc: Board of Directors

HOUSE TAXATION

EXHIBIT #3 7/8/92

HB 11

MEMORANDUM

TO: Representative Dan Harrington
Chairman of the Montana House Taxation Committee

FROM: Patrick M. Driscoll, Esq.

SUMMARY OF TESTIMONY OF AMERICAN COUNCIL OF LIFE INSURANCE BEFORE THE HOUSE TAXATION COMMITTEE IN OPPOSITION TO
HOUSE BILL 11: To Eliminate the Insurance Premium Tax Offset

DATE: July 8, 1992

The American Council of Life Insurance includes the great majority of companies which sell life insurance in the State of Montana. The Council opposes passage of House Bill 11, which would eliminate the offset by life and health insurers under section 33-10-230, MCA, of assessments by the Guaranty Association. ACLI supports Montana's present arrangement for handling liquidations among insurers.

The present arrangement used by most states is a contract between insurance companies and the State. Healthy life and health company's doing business in Montana manage insolvencies through a guaranty association.

In opposition to passage of House Bill 11 we submit the following summary of testimony.

THE CONTRACT CLAUSE OF THE CONSTITUTION PROHIBITS THE STATE FROM CHANGING THE RULES IN THE MIDDLE OF THE GAME WHEN IT HAS ENTERED INTO AGREEMENTS.

HB11 would change the rules and the financial burdens associated with insurance insolvencies. The American Council of Life Insurance opposes the change attempted in HB11 because it is unfair. It is so clearly unfair we believe it is unconstitutional to change the terms of your contract. This is especially true after performance of that contract is all but completed by one side.

1. THE CONSTITUTION PROHIBITS THE PASSAGE OF LAWS WHICH IMPAIR OBLIGATIONS UNDER EXISTING CONTRACTS.

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2. THAT PROHIBITION APPLIES TO CONTRACTS OF PUBLIC ENTITIES.

3. CONTRACTS OF PUBLIC ENTITIES INCLUDE STATUTES WHICH FORM THE BASIS FOR SUCH CONTRACTS.

4. A CONTRACT EXISTS BETWEEN THE STATE AND THE INSURERS DOING BUSINESS IN MONTANA TO HELP MANAGE INSOLVENCIES AND PROTECT AFFECTED POLICY HOLDERS.

5. TO CONTINUE ALLOWING OFFSET OF ASSESSMENTS AGAINST FUTURE PREMIUM TAX LIABILITY IS AN UNDERLYING ELEMENT OF THE CONTRACT BETWEEN INSURERS AND THE STATE.

6. THE EXISTING ASSESSMENT OFFSET IS A SIGNIFICANT FINANCIAL INDUCEMENT FOR THE INSURERS TO PARTICIPATE IN THE LIQUIDATION OF INSOLVENCY OF LIFE OF MONTANA.

7. THIS OFFSET OF ASSESSMENTS AGAINST PREMIUM TAXES WHICH FORMS AN ELEMENT OF THE CONTRACT BETWEEN THE INSURERS AND THE STATE OF MONTANA WOULD BE REPEALED BY HOUSE BILL 11.

8. THAT REPEALER HAS NEARLY A 100% CHANCE OF BEING CHALLENGED BY THE INSURERS DOING BUSINESS IN MONTANA OR BY THE MONTANA LIFE AND HEALTH INSURANCE GUARANTY ASSOCIATION ITSELF.

The American Council of Life Insurance urges the House Taxation Committee to give House Bill 11 a DO NOT PASS reccommendation.

HOUSE TAXATION

EXHIBIT # 4 7/8/92

"I Steve Browning for State Farm Insurance Companies before House Taxation Committee 7/8/92

MEMORANDUM

DATE: July 7, 1992

TO : Steve Browning, Lobbyist - Montana

FROM: Dave Adams, Assistant Counsel

RE : Montana - Special Session - HB 11

Steve, I have requested figures on how much State Farm might lose if HB 11 passes and the premium tax offset for life and health is abolished. I will send these to you as soon as they come in, however, the amount will certainly be around the sum of $275,000. The following points may be useful in exposing the weaknesses of the proposal.

Question #1 -What is a Guaranty Association and why does it exist?

Answer -Guaranty associations were originally set up to protect individual policyholders of failed insurers. Typically, when an industry competitor becomes insolvent, insurers in the same line of business are taxed by the state and make what amounts to an interest-free loan to the state. They are assessed for the claims paid on behalf of the insolvent competitor and allowed to recoup the "loan" by means of a 20% tax offset over a five year period. The original structure contemplated the burden for insolvencies rightfully resting on the general public and not only on that portion of the public holding health and life insurance policies. After all, guaranty fund assessments benefit Montana resident policyholders and not the insurance companies which pay the assessments.

Question #2 -What is HB 11?

Answer -It is a new tax specifically aimed at Montanans who have purchased life or health insurance. HB 11 worsens an already bad situation and translates loans forced from insurers by the state into a raw expropriation of funds by the state. However, ultimately it is the Montana policyholders of solvent companies who will be stuck with the bill for the claims owed by insolvent companies.

Question #3 -Is it unfair to make solvent insurers alone pay for claims against failed insurers?

Answer -Yes, because only the regulator has the ability and

Ex. # 4 HB 11
7/8/92

responsibility to regulate for solvency. The people of Montana elected both the Insurance Commissioner and the legislature: the Insurance Commissioner to regulate and the legislature to give the Commissioner the tools to do the job. The Montana Insurance Department has authority to examine foreign and domestic insurance companies, issue cease and desist orders or suspend certificates of authority for poorly-managed companies doing business in Montana. Assuring that a company will be there to pay the claims of Montana policyholders and other claimants should be the regulator's primary responsibility. The legislative goal should be fewer insolvencies so there is no need for a guaranty fund assessment in the first place and if the tools are not there for the Commissioner, the legislature should get them. Why should life and health insurance consumers, rather than all Montanans, pay for regulatory failures of officials elected by all Montanans?

Question #4 -Will the elimination of premium tax offsets provide insurers with additional incentives to pressure competitors to do a better job of management?

Answer -No. There may be other companies currently verging on insolvency of which we are not aware and if there are, insurers can only depend on the regulator to act. Insurers have no control over the operations of their competitors, and if they were to involve themselves in these operations, the management of the solvent company likely would be responsible for the violation of the Federal and State Anti-Trust laws.

Question #5 -Might there be other negative effects of abolishing the offset?

Answer -Yes. The following list illustrates some possibilities:

-Insurers may become less solvent. The current system demands interest-free loans. If premium tax credits are eliminated and insurers can not recoup assessments, the entire burden shifts to the insurance companies.

-Well-managed insurance companies might be hurt at several points in the insurance process. First they might lose initial business to poorly-managed companies that secure business by offering unrealistic returns. They may be forced to lower their rates to compete with poorly-managed companies. Finally, they are expected to pick up the pieces and pay the claims of the insolvent companies when they go out of business. But it is the Montana policyholders of solvent companies who will be stuck with the bill for the claims owed by insolvent companies. A consumer who has carefully shopped to find insurance with a well-managed, secure insurance company still will bear the burden for the poorly-managed company.

-Some companies will not be able to recoup their assessments in any way. An insurer can not change the premium it agreed to accept as a part of the original contract with the policyholder. A participating company may be able to lower dividends or interest rates to accommodate the extra loss. Non-participating companies can not. This places an unfair and perhaps unconstitutional burden on those companies which can not adjust to an unexpected loss.

-Montana's insurance Market may shrink. Life and health insurers doing business in the state of Montana already pay substantial taxes. The proposed removal of the offset, which amounts to a new tax, will further burden marginal insurers and increase their risk of insolvency or departure from the market.

-Selling Life insurance in Montana could become more difficult. No longer would life insurers be able to represent to business prospects that they would be buying protection, since people buying policies would be both buying protection and paying off insolvencies. Furthermore, if premiums were raised for future policyholders alone, they would bear the cost of present insolvencies while present policyholders would not.

-Life Insurance sales could be driven out of Montana. Simple economics dictates that wise business prospects will prefer that all of their dollar be spent on insurance product alone rather than on a reduced amount of product and taxes to cover the claims of insolvent insurers.

Give me a call if you have any questions about these points.

Dave

Dave Adams

cc: Ron Ashabranner By FAX
Dave Hill

House Taxation Committee, July 8, 1992

SOFTWARE TAXATION CONSIDERATIONS

A Statement in opposition to HB 16 by Steve Browning, for IBM

Ex. # 3 HB 11
7/8/92

The increasing prevalence of computers in businesses has elicited much consideration of whether computer software should be clearly excluded from those classes of property subject to ad valorem personal property taxation. Three major views of the issue have emerged.

One view would allow the imposition of property tax on all types of computer software. This view creates economic disadvantage for the taxing jurisdiction. In a software transaction the owner licenses the use of copyrighted intangible information to its customer A wide variety of methods may be used to transmit this information. The licensor may distribute the information via common disk or tape media; or, the licensor may send the information via satellite, telephone line, microwave, radio signal transmission, or even by a human being. By any method, the essence of the transaction is the communication of knowledge. Imposition of a tax on the free flow of knowledge places the taxing jurisdiction at a competitive disadvantage with other states and potentially with other jurisdictions within the same state. In a time when states compete with each other for clean, high-tech industry, each state must carefully consider the adverse impact software taxation would have on the state's ability to attract and keep business.

Most companies do not keep an internal inventory of software licensed, used, and developed. Therefore, sophisticated and expensive record-keeping systems would be required to account for the software. These software inventory problems, along with valuation burdens, would make compliance with a software property tax difficult and inequitable from both a taxpayer and a tax collector's perspective. Sound tax policy requires fairness in application, consistency among taxpayers, and val-

uations which can be audited by the assessor. Property taxation of software fails all three of these standards.

A second view of the the software taxation issue suggests taxing some, if not all, software. Most of the proposals that have arisen under this view attempt to distinguish between "canned" software, which would be taxed, and "custom" software which would be tax exempt. Unfortunately, software is not so easily or neatly classified. Given its dynamic nature, classification of software can neither be done readily or with certainty. Any classification is necessarily temporary and should not be governing for tax purposes. It is neither meaningful nor equitable to differentiate "canned" from "custom" software for tax purposes.

Tax legislation must fundamentally be understandable and administrable. Trying to distinguish in an age of advancing technology between what is customized or canned software would result in administrative conflict and endless litigation. Such a policy would not be administrable or cost effective. Such a policy is not rational tax policy and ultimately impedes sound business decisions.

A third view, and most advantageous to long-term state interests and taxpayer fairness, is that all computer software should be explicitly exempted from property taxation. This is the position that has been taken by states that can correlate the success of the state's economic growth plan with the growth of the state's high technology industry. Software is synonymous with "high tech". A jurisdiction that chooses to impose a software property tax sends a very strong negative message to the business community and to computer software companies in particular. Indeed, after diligent consideration, Colorado, Connecticut, Michigan, and Mississippi recently chose to exempt the property taxation of software.

Attached is a timely article describing the current "Canned" software available to Business.

As the former Chairman of Montana Science and Technology Board, I can state that this bill is the wrong [illegible] for business. They are not able to handle high

** TOTAL PAGE.003 **

Ex. # 5 HB 11
7/8/92

America's Small Business Magazine

IB Independent Business

July-August 1992

BEST PROGRAMS FOR YOUR SMALL BUSINESS

SUPER SOFTWARE

■ Lease Land Mines To Avoid

hat You Can't Say In Your Ads

w! IB Idea Exchange

e You A Trade Show Dud,

r A Dynamo?

■ Should You Add Another Location?

**********5-DIGIT 59624
123572 16 000 01
STEVE BROWNING
BROWNING-KALECZYC-BERRY-HOUE
P O BOX 1697
HELENA MT 59624

Published for the independent business owners of the NFIB

Amendments to House Bill No. 12
First Reading Copy

Requested by Representative Bardanouve
For the Committee on Taxation

Prepared by Valencia Lane
July 7, 1992

1. Title, line 7.
Strike: "NOVEMBER"
Insert: "DECEMBER"

2. Page 2, line 5.
Page 2, line 8.
Page 2, line 11.
Strike: "November"
Insert: "December"

3. Page 2, line 9.
Strike: "December"
Insert: "January"

House Taxat. 8:30 Wed 7/8

HOUSE BILL NO. 12

INTRODUCED BY BARDANOUVE

A BILL FOR AN ACT ENTITLED: "AN ACT REVISING THE TIME IN WHICH THE COUNTY TREASURER MUST REMIT MONEY BELONGING TO THE STATE AND COLLECTED BY THE COUNTY TREASURER DURING THE MONTHS OF JUNE AND ~~NOVEMBER~~ DEC; AMENDING SECTION 15-1-504, MCA; AND PROVIDING AN IMMEDIATE EFFECTIVE DATE."

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF MONTANA:

Section 1. Section 15-1-504, MCA, is amended to read:

"15-1-504. Settlement of county treasurer with state treasurer. ~~The~~ (1) Except as provided in subsections (2) and (3), the county treasurer, between the 1st and 20th days of each month, shall remit to the state treasurer all money belonging to the state that was collected by the county treasurer during the preceding month. The remittance must be accompanied by a detailed report upon a form that the state treasurer prescribes. The state treasurer may assess counties an interest charge of 10% a year on all money not remitted within 5 days from the time required by this section.

(2) By June 20 of each year, the county treasurer shall remit to the state treasurer all money belonging to the state that was collected by the county treasurer by June 15, in addition to the amount collected during the preceding month. In July, the county treasurer shall remit all money belonging to the state that was collected by the county treasurer during the remainder of June.

(3) By ~~November~~ Dec. 20 of each year, the county treasurer shall remit to the state treasurer all money belonging to the state that was collected by the county treasurer by ~~November~~ Dec. 15, in addition to the amount collected during the preceding month. In ~~December~~ JAN., the county treasurer shall remit all money belonging to the state that was collected by the county treasurer during the remainder of ~~November~~ Dec.."

NEW SECTION. **Section 2.** Effective date. [This act] is effective on passage and approval.

-End-

HB 12
INTRODUCED BILL

HOUSE TAXATION HB 15

EXHIBIT # 6 7/8/92

Amendments to House Bill No. 15
Introduced Bill

July 8, 1992

1. Title, line 6.
   Following: "BY"
   Strike: "USING THE CURRENT TAXABLE VALUE PERSONAL PROPERTY COUNTY IN 1989"
   Insert: "DEPRECIATING THE VALUE OF THE REIMBURSEMENT BY TEN PERCENT EACH YEAR"

2. Page 2, line 6.
   Strike: subsection (b) in its entirety.
   Insert: "(b) The reimbursement revenue must be based on the county's taxable value and mill levies for tax year 1989."

3. Page 2, line 23.
   Strike: section (3) in its entirety.
   Renumber: subsequent sections.

4. Page 3, line 4.
   Following: "levies"
   Strike: "and the current year taxable value of personal property that was taxed in the county in 1989"

5. Page 3, line 12.
   Following: "year"
   Strike: "1990"
   Insert: "1992"

6. Page 3, line 15.
   Strike: "~~(3)~~(4)"
   Insert: "(3)"

7. Page 3, line 16.
   Strike: subsection (a) in its entirety.
   Insert: "(a) on or before November 30, 1992, and on or before November 30 thereafter for the next nine years, the department shall remit 50% of the base amount of revenue reimbursable to the county reduced by equal percentages until no reimbursement is made in the 10th year;"

8. Page 3, line 20.
   Strike: subsection (b) in its entirety.
   Insert: "(b) on or before May 31, 1993, and on or before May 31 thereafter for the next nine years, the department shall remit 50% of the base amount of revenue reimbursable to the county reduced by equal percentages until no reimbursement is made in the 10th year."

Personal Property Tax Reduction Reimbursements (HB20)
Tax Year 1991 Reimbursment

EXHIBIT #7 7/8/92

HOUSE TAXATION

County	County Government	Local Schools	Cities and Towns	State Equalization	University System	Miscellaneous Districts	Total
Beaverhead	51,385	108,398	10,453	23,641	3,546	0	197,423
Big Horn	134,874	272,608	8,879	113,438	17,016	1,574	548,388
Blaine	43,415	86,842	8,712	23,629	3,544	1,639	167,780
Broadwater	30,376	47,710	3,235	18,122	2,718	9,832	111,993
Carbon	35,238	86,078	10,015	19,410	2,911	2,535	156,187
Carter	16,205	27,444	1,248	6,832	1,025	0	52,753
Cascade	195,419	509,763	163,400	91,942	13,791	33,083	1,007,398
Chouteau	84,136	155,949	7,988	39,233	5,885	23,483	316,675
Custer	43,260	127,973	32,196	20,095	3,014	56	226,594
Daniels	38,402	73,813	4,389	14,479	2,172	32	133,287
Dawson	62,384	162,376	27,923	30,258	4,539	597	288,078
Deer Lodge	32,005	43,119	1,242	7,444	1,117	8,541	93,466
Fallon	31,734	117,353	6,661	45,518	6,828	328	208,422
Fergus	73,383	185,557	20,882	37,566	5,635	2,496	325,519
Flathead	239,704	497,986	261,045	72,441	10,866	11,620	1,093,664
Gallatin	178,198	478,755	123,364	96,097	14,415	12,378	903,207
Garfield	20,540	23,915	914	7,730	1,160	0	54,260
Glacier	56,474	108,267	11,669	33,981	5,097	1,429	216,917
Golden Valley	6,175	17,186	283	4,688	703	222	29,257
Granite	21,326	38,889	2,059	9,385	1,408	2,437	75,504
Hill	85,401	195,402	26,602	50,260	7,539	2,826	368,030
Jefferson	83,948	195,085	2,685	52,388	7,858	4,590	346,554
Judith Basin	26,412	47,862	1,058	12,286	1,843	736	90,196
Lake	52,845	109,260	20,859	27,818	4,173	5,781	220,735
Lewis And Clark	138,183	385,256	143,565	69,217	10,383	113	746,715
Liberty	35,013	66,250	1,286	16,775	2,516	456	122,296
Lincoln	91,713	375,246	10,910	78,995	11,849	2,188	570,901
Madison	59,044	143,178	4,558	34,881	5,232	10,492	257,385
Mccone	47,223	61,435	4,233	16,375	2,456	27	131,748
Meagher	11,786	21,515	1,748	6,509	976	783	43,317
Mineral	25,961	61,957	2,479	11,573	1,736	2,157	105,862
Missoula	527,913	1,129,107	296,318	202,891	30,434	103,881	2,290,544
Musselshell	17,575	28,176	2,728	10,214	1,532	57	60,281
Park	39,665	103,207	20,620	25,496	3,824	1,689	194,501
Petroleum	5,307	10,976	56	2,519	378	0	19,236
Phillips	42,977	124,359	6,401	40,153	6,023	1,155	221,067
Pondera	53,862	114,921	9,071	26,693	4,004	3,089	211,640
Powder River	71,252	73,896	1,896	23,387	3,508	694	174,633
Powell	34,758	85,329	4,106	18,127	2,719	311	145,349
Prairie	22,796	22,881	2,184	8,364	1,255	59	57,538
Ravalli	51,716	120,221	22,068	27,971	4,196	4,032	230,204
Richland	115,163	208,606	18,575	76,691	11,504	0	430,540
Roosevelt	52,448	125,072	11,413	38,020	5,703	5,987	238,643
Rosebud	24,283	185,759	6,934	87,708	13,156	7,443	325,284
Sanders	32,397	77,165	7,299	19,702	2,955	527	140,045
Sheridan	50,373	178,567	9,378	54,711	8,207	4,914	306,149
Silver Bow	248,104	492,748	31,365	80,418	12,063	51,273	915,970
Stillwater	56,898	110,439	11,029	31,435	4,715	7,395	221,911
Sweet Grass	18,120	37,306	4,421	8,944	1,342	0	70,133
Teton	57,617	111,533	5,459	25,784	3,868	1,385	205,647
Toole	89,798	118,193	13,724	44,235	6,635	1,924	274,509
Treasure	13,010	24,738	1,089	6,914	1,037	131	46,920
Valley	51,052	156,050	16,681	31,785	4,768	569	260,904
Wheatland	12,533	26,466	1,941	6,244	937	0	48,120
Wibaux	26,372	28,392	2,173	14,127	2,119	150	73,333
Yellowstone	547,213	1,482,350	284,664	311,792	46,769	45,696	2,718,485
Total	4,315,361	10,008,881	1,337,051	2,317,331	347,600	384,790	19,092,096

MISSOULA FINANCE/CITY CLERK OFFI
435 RYMAN ST. • MISSOULA, MT 59802-4

HOUSE TAXATION

EXHIBIT # 8 7/8/92

July 7, 1992
Letter #92-167

Honorable Members of House Taxation Committee
Montana House of Representatives
Montana State Capitol
Helena, Montana 59620

Dear House Taxation Committee Members:

This letter is written to express the City of Missoula's opposition to House Bill 15 as introduced by Representative Ben Cohen. This bill would greatly diminish and ultimately eliminate the personal property tax reimbursement payment to local governments and school districts.

The personal property tax reimbursement was enacted in the special session in June, 1989 to reimburse local governments and schools for the policy decision to reduce the tax multiplier of many classes of personal property to 9% of market value. The Legislature recognized at the time that local governments and schools were subject to the I-105 cap and other budget limitations, thus the loss of revenue could not be "absorbed" by those taxing jurisdictions. The same situation still exists - local governments are still subject to I-105 and the commitment to replacement revenue is no less important.

The City of Missoula receives $170,000 per year in this reimbursement revenue for the general fund and another $80,000 for our tax increment fund. I was told by the Missoula County Assessor that the majority of personal property has a ten year depreciation life, but some has three and five year lives. HB15 would mean that over a ten year period, the entire reimbursement would be phased out. Although it is difficult to calculate the impact, I estimate this decision would probably mean a reduction of $30,000 - $50,000 in revenue for the City of Missoula in the current fiscal year, FY93. Our budget is almost set and it would be very difficult to adjust to this change at this time.

We would encourage you that, if you need to save this appropriation in order to balance the state's budget, you then consider taking away one tenth of I-105 every year for the next ten years or eliminate it completely. You could reinstate the property taxes to their former levels, but that might also be counter productive. We simply ask you not to renege on the partnership agreement you made when you reduced personal property taxes in 1989. Thank you for your consideration.

Sincerely,

Chuck Stearns

Chuck Stearns
Finance Officer/City Clerk

cc: Mayor Dan Kemmis
Alec Hansen, Montana League of Cities and Towns

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HOUSE OF REPRESENTATIVES

VISITOR'S REGISTER

House Taxation COMMITTEE BILL NO. #

DATE 7/8/92 SPONSOR(S)

PLEASE PRINT PLEASE PRINT PLEASE PRINT

NAME AND ADDRESS	REPRESENTING	BILL	OPPOSE	SUPPORT
Steve White	Advance Corp	10	X	
Bruce Larson	Revenue	—		
LARRY AKEY	LIFE UNDERWRITERS	11	X	
Mike Mulroney	MT. Life + Health Insurance Guaranty Asso	11	X	
Tom K. Hopgood	Health Insurance Assoc of America	11	✓	
R. Ashbrenner	State Farm	11	✓	
Jo Mickelson	State Farm Insurance	11	✓	
Russell B Hill	Mont Trial Lawyers Assn	11		
Judy Rippingale	Mt Dept of Revenue			
Steve Browning	IBM State Farm	10 11	✓	
Ted J. Doney	Applied Management Corp	10	✓	
Gordon Morris	MACo	10-12 15	✓ X	
Carl Harrington	County Treasurers Asso	12	✓	

PLEASE LEAVE PREPARED TESTIMONY WITH SECRETARY. WITNESS STATEMENT FORMS ARE AVAILABLE IF YOU CARE TO SUBMIT WRITTEN TESTIMONY.

PATRICK M. DRISCOLL - American Council of Life Insurance 11 oppose

HOUSE OF REPRESENTATIVES
VISITOR REGISTER

House Taxation COMMITTEE BILL NO. _____

DATE 7/8/92 SPONSOR(S) _____

PLEASE PRINT PLEASE PRINT PLEASE PRINT

NAME AND ADDRESS	REPRESENTING	SUPPORT	OPPOSE
Robert Throssell 38 S. Last Chance Helena	America Insurance Assoc	–	–
Owen Neiter Billings			
Roger McGlenn	Independent Ins. Agents Assoc of MT		X
Dennis Burr	MT Taxpayers Assoc	HB10	✓
James Tutwiler	MT Chamber		HB10
Ray E. Gulick	Sales Tax	X	
Charles R. Brooks	MT Retail Assoc		HB10
Leon D. Stolemp	Mt Restaurant Assoc		
J. Shontz	MHAM	X	
Phil Campbell	MEA HB 15		X

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HOUSE OF REPRESENTATIVES
VISITOR REGISTER

House Taxation COMMITTEE BILL NO. HB-15

DATE 7-8 SPONSOR(S) Cohen

PLEASE PRINT PLEASE PRINT PLEASE PRINT

NAME AND ADDRESS	REPRESENTING	SUPPORT	OPPOSE
Alec Hansen	MLCT		✓

PLEASE LEAVE PREPARED TESTIMONY WITH SECRETARY. WITNESS STATEMENT FORMS ARE AVAILABLE IF YOU CARE TO SUBMIT WRITTEN TESTIMONY.