

TAXATION COMMITTEE
45TH LEGISLATURE

The House Taxation committee met in a joint hearing with the Senate Taxation Committee in room #415 of the Capitol Building, Helena, MT., on January 20, 1977, at 8:00 a.m. All members were present. Senator William L. Mathers was chairman of the joint session.

This meeting was for the purpose of considering means to set up a trust fund that would maximize income consistent with safe and conservative practices of investing the money derived from the coal tax. The question of whether the principal should be invested to accomplish some social purpose other than welfare or unemployment was to be discussed.

At present it is set up as a trust account in the Trust and Legacy fund. (See letter dated January 17, from Mr. James R. Howeth, Investment Officer of the Board of Investments.) There are problems in mingling this fund with the T&L fund because 3/4 of each house of the Legislature could invade that fund and spend the principal in case of an emergency. This allowance comes from the coal tax trust fund present law. These funds cannot be handled the same as long-term funds as there may be a demand for them. He proposed an amendment to Article IX of the Constitution, section 5, as shown in his letter. This is enumerated in section 79-310. The amendment would allow the coal fund principal to be utilized without jeopardizing the rest of the commingled funds which upon emergency demand could cause a loss of principal. This would allow for investment in common stocks. Retirement funds can only be invested in common stocks and he is not sure if the coal tax funds can be invested that way also.

Rep. Steve Waldron asked if this sets up an economic funding institution which makes decisions on investing the funds in Montana or however we want to go. The major portion of money invested is in out-of-state corporations. The coal tax money represents something that is going to be a permanent loss, consequently, we should invest that money in Montana for something very permanent that puts money into Montana by investing it in Montana businesses, farms, housing, etc.

Rep. Fabrega feels that it should be invested in Montana. He recommends it be used basically for housing, and not necessarily maximizing it for income. It would not put the state in the lending business, thereby the funds would be put to the greatest needs, first for housing which should help the unemployment situation in the construction area.

Rep. Lee Tower, District #18, believes the trust fund portion of money should be kept pretty liquid because 3/4 of the Legislature can get it out. It should be kept in Montana. The trust fund was presented as being the best thing for the people of Montana. The money should be made available to banks and savings and loans on certificates of deposit, etc. This doesn't maximize income because they are the most prudent investors in Montana. This would take the least amount of administration, and wouldn't require an additional board. (He is in the feed and grain business). At present farmers and ranchers and other businesses don't have enough money to stay in business and keep capitalized. This money should be available to Montana banks and savings and loans.

Senator Mathers advised there will be a series of bills which will implement the conservation recommendations from the Lieutenant Governor's office in connection with energy studies. These bills could keep money in Montana, but can't get the same rate of return on that money as you can out-of-state. More importantly, the money would be used to secure low interest loans for both industry and residential people for the purpose of retrofitting their houses and industrial plants with insulation. He recommends the money be used for conservation purposes in Montana.

Pat Binns recommends that the coal tax trust fund be set up as a separate fund to be managed by the Board of Investments according to specific rules defined by the 45th Legislature. Those rules should require the funds to be invested within the state, particularly in low interest certificates of deposit with banks and savings and loan and credit unions in Montana. These time deposits should be used for low interest loans for all types of energy related investments. He also recommends that another portion of the fund be used by the state to purchase local bonds issued for energy conservation related activities for industrial, commercial and private citizens. These industrial revenue bonds, LIDS, school improvement bonds, and other local government purpose bonds should be at a low interest rate. There are hidden benefits other than the interest rate.

Senator Blaylock is very much in favor of setting up this coal trust fund, and would hope they would take a look at a program that we have studied which has cost \$200,000 on solid waste management. We may be able to set up three solid waste areas in the state. He recommends allocating \$500,000 to \$2½ million dollars to cities for the time which it will take to start planning until they could sell their bonds, and then possibly purchasing the bonds after the cities have decided to go into the solid waste management program.

Senator Margaret Warden advocates the allocation for solid waste management as a source of energy in Montana that is not being utilized.

Terry Carmody advised that this program could conserve energy and do away with solid waste. It will take from \$12-\$27 million dollars for the implementation of the total program. He recommends some of the coal tax funds going back to local governments to help people in local areas.

Rep. Peter Meloy advised this would provide the very kind of bonds that are being talked about.

Rep. Esther Bengston recommends taking 30% of the income from the trust fund and designating it for education. This would suggest that the trust fund be invested for maximum yield rather than for social services.

John Blake, School Association, said they had formed a coalition with Montana school administrators, and their state office is attempting to press the need of higher education funds. Higher education takes a large portion of our tax dollars. There are 180,000 students in Montana and one-quarter of the persons in the state is engaged in public education.

Louis Forsell, Counsel for the Education System, suggested an allocation of 30% of the income be divided - 75% to go for support of higher education, and 25% of the 30% to be handled by the Board of Investments for support of the University

System. By 1985 it will cost \$87 million a year for the Universities of Montana. If these funds were allocated this way, the 6-mill levy for the university system could be lowered. The 6-mill levy has to be voted upon and there is no assurance that it will be continued.

Rep. E. N. Dassinger is dismayed at the lack of confidence of our present system of handling funds as the Board of Investments is educated to invest, and he feels that appropriations according to the present investment practices should be continued.

Rep. Waldron expressed his opinion investing in Montana is not spending the money - it is investing it.

Jim Ogler, executive director of the Montana Coal Council, an association of coal companies and businesses, asks that some of the revenue from the coal tax be returned to the impact areas in which the coal is mined for roads, and for reimbursement to the people who were promised funds for losses due to the coal being mined, but who as yet have received nothing. He believes the money should go to the general fund and then the funds requested be appropriated. Funds could be earmarked and set up into side trust funds.

Jim Howeth, investment officer, advised that the funds are statutorily put into the Trust and Legacy fund along with other funds, the income or benefits from which the school districts receive 90%, and these other funds statutorily can not have their principals disturbed - in fact, it is written that you can't sustain a loss in the Trust and Legacy fund. The new Constitutional amendment when it was voted in, in the heading to the amendment it says "a permanent trust fund". "The principal of the trust shall forever remain inviolate" - unless it is appropriated by the Legislature by a 3/4 vote by each house and this would make it relatively hard to manage. If the Legislature spent the principal, it might have to invest it in short-term securities in case the principal is called for. He would suggest that it be in a Trust and Legacy fund by itself and that the coal tax fund would be a separate trust fund because the Constitution statement makes it impossible to override and we can only do the best we can in how it is invested.

Rep. Fabrega said that whatever is decided now will only last through the next biennium as this Legislature cannot mandate the next Legislature.

Rep. Melvin Underdal feels that any future Legislature should be restricted from spending any of this fund.

Senator Towe stated he thought, with the necessity of a 3/4 approval by the Legislature, the principal is pretty safe from being spent. He thinks it should be put into a permanent trust. There is a great deal of concern about investing the money in Montana - are going to set up a great big fund which would then be largely invested out of state and not help the people of Montana? He recommends funds first for education; second, for energy conservation. He does not want to monkey with the investment possibility and just use income from the principal - 30% of the income for education (3/4 for higher education; 1/4 to lower education); 1/6 of the income to energy conservation; use some of the capital for loans to Montana institutions.

Mr. Howeth advised, presently, they invest \$650 million dollars now, and this is represented by some 60 different funds. Statutory laws vary according to how the funds we have may be invested. There is a substantial portion that is invested in Bank CDs and Montana mortgages. You may say the amount invested in Montana is too low, but it would be impossible to invest the whole \$650 million dollars in Montana. We do this to the best of our ability by investing in trust funds. There is a "prudent man law" which we also have to contend with in investing the funds. If we were to subsidize at a low rate of interest loans or something like this, we would be in jeopardy of the prudent man rule which does not take into consideration such subsidies. So you have the responsibility of investing trust funds which doesn't take into consideration social responsibility such as low-cost housing. You do have a housing authority that is not operating yet, but it should go to the area of subsidizing low income housing which is fine because it is separate from the investment responsibility. When you try to shove a social responsibility into an investment, it is hard to regulate. You say to invest the money in Montana, but there is only so much money you can reasonably invest in Montana because it is impossible to do this because of lack of need or demand.

If you invest outside of the state, the income is returned to Montana. A General Motors bond has investments in Montana even though the corporation headquarters is outside of Montana. You can't make Montana an island.

Senator Watt advised the 3/4 rule was put in as it was considered to be a very unusual circumstance that would require its use. He feels it should be kept in. He feels the investment of the fund should be diversified so that some of it would be available on short notice.

Rep. Verner Bertelsen, Ovando, advised that regardless of how we feel about that 3/4 rule, a bonding company is not going to look at it from our point of view. If we open this to social programs for use to support and push a certain program, we will have made a serious, dreadful mistake. This money should be treated as our state lands. These funds are going to earn a revenue and this revenue should be wisely spent, but in no way should the principal be spent.

Roger Tippy advised that the placement of this fund in the Trust and Legacy Trust fund was just a placement for the sake of government.

Current investment laws cover all state funds. SB 44 requires fund to be deposited in the Trust and Legacy Fund, the principal of which is permanent. You still have it if part of the coal funds are invested. If in the future the Legislature allocated some of this principal, this would affect the principal of the Trust and Legacy fund as well as the coal fund principal.

Sen. Towe advised that by putting it in that pool, there is more liquid money available at all times.

Mr. Howeth advised that putting the coal trust fund into the Trust and Legacy Fund the principal of which is \$75 million dollars, it would be made to look like a mere pittance. The T&L fund grows very little each year while the coal trust fund in a short time would be a billion dollar fund.

Rep. Fabrega said that rather than hold a special election to use the principal of this fund in case of an emergency, he believes the Legislature should be able to use it quickly and it should be a separate fund. There will be \$25 million dollars by the next biennium, and he doesn't see any need to tap the principal in this two year period. This Legislature should lay out a general criteria that any Legislature can act upon later.

Sen. Towe said whether there is a separate trust fund or not, where the \$25 million is to go should be decided this year. Once a decision is made, it will be very difficult for future Legislatures to change it unless the change is very stringent.

Sen. Turnage thinks it should go into the Board of Investments like any other money, but it should be a separate fund. As to spending the money, he thinks it should go to the general fund in accordance with the Constitution. The whole Constitution is written on the theory that the Legislature is where the people go.

Rep. Fabrega recommends latitude of the Legislature in investing this money since it is a new funding. It is necessary to fund local impact and see that the necessary funds are there.

Neil Lynch, attorney for the gas and coal counties, advised direct aid for impact relief for highways; and the coal counties agree with anticipation of receiving federal money. Under Sen. Manning's proposal, 3% went to highways. He asks that at least 1% be retained by the coal producing counties. Persons absorbing the impact are not receiving anything at the moment, but they should be doing so.

Roger Tippy mentioned that the home loans offered by a local bank for insulating homes were not used as it seemed people had the cash to pay for this purpose. It was not accepted very well.

Sen. Towe mentioned there is the possibility of using permanent coal trust funds for social purposes. There is some precedent in using that fund for emergency relief for farm mortgages. In the Depression years, the Trust and Legacy Fund was used for farm mortgages; however, this was strictly unconstitutional since the wording of the T&L fund is that the "principal of the trust fund shall forever remain inviolate", and if this is followed to the letter of the law, you could not invest these funds in private corporations. It would be hard to use this money since the prudent man rule would have to be observed.

Mr. Howeth advised that there are over 60 different funds which are segregated statutorily. The principal is invested and the income goes directly to the treasurer as cash unless otherwise earmarked -- this income goes into the general fund pool. The question is whether we should invest in Montana or put the interest income back into that fund also. He agrees that the fund should be kept as a separate fund with interest to go back into the general fund. Something should be made available for the present and not all for the future.

Rep. Lee Tower suggested taking the trust fund and spreading it around Montana in banks to be loaned in mortgages in Montana. There is already \$45 million in CDs in Montana banks or savings and loans. Sometimes banks will not always buy CDs when they can get money to relend cheaper elsewhere.

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Rep. Lien advised that there is a discrepancy between bills going through the Taxation Committee and what is being presented here.

Mr. Howeth further advised that the Board of Investments can only invest in high quality loans because there is no reserve for losses and so quality has to be taken into consideration and adhered to. Thereby they shut themselves out on a quality basis in many instances.

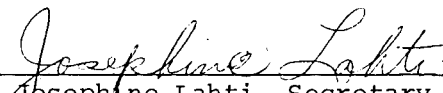
Rep. Waldron said the problem is, if we are going to invest in Montana, we are going to have to accept a high risk and he doesn't believe the Board of Investments is going to be able to do this.

Rep. Fabrega feels short-term capital should be available with only a very limited amount for long-term investments.

The meeting adjourned at 11:00 a.m.



REP. HERB HUENNEKENS, CHAIRMAN



Josephine Lahti, Secretary