

HOUSE TAXATION SUBCOMMITTEE

46th Legislature

Representative Edward Lien, Chairman of the subcommittee on HB 150, called the committee to order at 8:15 a.m., January 23, 1979, in room 434, Capitol Building, Helena. Representatives Robert Sivertsen, Melvin Williams, Jay Fabrega were present. Harold Pitts, John Cadby, George D. Anderson, CPA, representing Montana Bankers Association; Ed Sheehy, Jr., Attorney, Montana Savings and Loan League; Randy McDonald, Staff Attorney, were present.

According to Department of Revenue, <sup>S&L</sup>~~banks~~ paid \$387,745 in taxes in 1977. If HB 150 had been effective, they would have paid \$200,869 more. Seventeen building and loan companies (two from outside the state) were taxed for 1977.

Sivertsen: Getting back to the S&Ls - are you now saying that we should grant this bad debt reserve deduction for both banks and S&Ls?

Sheehy: Can be given to both - it's constitutional when applied to both institutions.

John Cadby asked if there were any danger at all of there being a legal risk by putting in the reserves for bad debts for banks or S&Ls. Sheehy: It would be unwise to do because it would jeopardize the whole bill.

Sivertsen: If we grant that reserve for bad debts, then in order to raise the amount of money that we think we need, or to try to raise the same amount from this tax, then what would be the rate - what would you say if we raised it to 7-1/2?

Sheehy was not sure raising to 7-1/2 would solve the problem. Their taxes will increase. Would have to see how much revenue you would lose by allowing both to have this deduction.

Mr. Anderson said Mr. Bennett didn't think it would jeopardize the whole bill. Addition of a severability clause would save balance of bill.

Sivertsen: If we leave the bill the way it presently is, and our real main focal point is trying to bring about equity, do you think that by not allowing the bad debt reserve to either would be equity?

Fabrega: Problem is going into corporate license tax - all other corporations are based on actual bad debts. Present law is actual losses can be deducted from profit and if we change that, we have troubles.

Lien agreed every corporation is allowed to deduct actual losses.

Fabrega: The Revenue Oversight Committee did not want a financial institutions bill. One of the things that was proposed at the hearings was that we allow a deduction of 11-1/2% for financial corporations which should be treated like all other corporations.

Sheehy answered that it is a question of how other corporations will react. The entire bill right now is changing procedure of corporation license tax and provides money goes into state general fund. There could be a challenge right there. Have doubts about other corporations coming in and saying this is discriminatory. As long as there is no discrimination within a class it would be alright. No legal problem if no discrimination. Can treat banks and S&Ls alike because they are similar.

Williams: Have to keep in mind not distinguishing between them. Practically all other business corporations paying some kind of an inventory tax.

Cadby: Federal law says you can only impose a uniform non-discriminatory tax on interest income of federal obligations. We are under the rule of that federal law. If you allow a bad debt reduction to banks, are you not discriminating against another corporation who is holding federal obligations and bringing a case against banks?

Williams said the amount of obligations that is owned by other corporations is only 2-3%. This could make for a problem. What is a financial institution? Other corporations don't need reserves as much as banks. It is a very touchy subject. Feeling among corporations that have losses, is that there is a need for reserves.

Fabrega: Question of distribution doesn't pose the same conditional problems in allowing the deduction. The only one person that might take it to court, is the general fund or the school foundation. We can earmark funds. Everything should go into the general fund in his opinion. Property tax would no longer have to go to local governments.

Sheehy: Other corporations could argue.

Pitts: Banks have paid counties for hundreds of years. How tax is figured wouldn't have any effect on where the money is paid. Sheehy advised S&Ls have been paying to counties.

Sivertsen: S&Ls think they should have preferential treatment because of the nature of their business and that is in long-term loans. Banks have short-term loans and turn their dollars over more quickly. S&Ls enable people to have homes through long-term loans.

Cadby: The nature of S&Ls is evaporating - in a few years, won't be able to tell the difference since S&Ls are making loans like banks. Banks sell their loans and don't hold them. They are in the business of servicing accounts. S&Ls make very few consumer loans. Banks make more consumer loans. S&Ls are trying to get checking services. In 5 years won't be able to tell the difference between banks and S&Ls.

Sheehy: S&Ls aren't allowed to have checking accounts in Montana. Some states have started that, but S&Ls don't have master charge, etc. Basically they should be treated the same.

Sivertsen: Reasons why they should be treated differently?

Sheehy said S&L position is not that they should be treated differently. Under this bill they are going to be, in effect, treated differently - not maybe in the way the bill reads, but the "effect" treats differently. Thinks the reserve method is the only way and should be put in for all corporations and justified by basing on the risk that that particular industry has as far as loans, etc, is concerned. Reserve should be set up for all corporations. Reserve based on what the risk of the loan is - not how much you can loan- what the history of that particular industry is in accordance with their losses.

Williams asked what the volume of loans is compared to the tax paid - ratio of loans to tax. Banks can get this figure easily. He thinks that although \$200,000 additional tax will pull a sizeable amount of money off the money market, it will not make much difference in the operation of the S&Ls. The ratio figures are to be given to the committee.

Pitts: Reserve for banks whose loans are 1/3 commercial loans, 1/3 installment loans; 1/3 unsecured loans. Banks have a greater exposure to real losses. Reserve is probably more a necessity in that type of lending. Real estate loans provide good security.

Sheehy: S&Ls increased their business by 15% last year. They have approximately \$31,342,000 in loans, with total assets of \$122,770,000, and feel \$200,000 would have quite an impact on them.

Lien: Real estate security is one of the safer loans. Installment and unsecured lending is more risky.

Cadby: Real estate inflates in value, making for more security. S&Ls have \$3.5 billion in real estate loans, \$4 billion total. 65% is loaned out; 2-1/2 to 3 billion loaned out annually. What is \$200,000 against that? That is loans on homes.

Sivertsen: Problem is answering the question as to why we should treat banks and S&Ls differently. Appears to him that the S&Ls are fighting this thing because they will be paying more taxes. Equity in taxes and this appears to be another step going down that path. Can you give me any other good reasons why you should not be taxed under this bill?

Sheehy: The intent of this legislation seems to carry out that and to replace the property tax loss that is going to happen. The two should be treated equally. With this amendment taxes will still go up and the majority of the banks with this proposal will have a reduction in their taxes.

Sivertsen: This is an equity issue. Maybe banks have been paying too much and S&Ls not enough. If this is not the case, I want reasons why.

Sheehy: Maybe banks have been paying a tax that the state should not have been taxing them for.

Lien: We are addressing equity and try to evaluate that. Doesn't think this is a valid excuse for not taxing S&Ls.

Sheehy: In talking about 160 banks and 17 S&Ls and the impact on those 17 S&Ls will be greater than on the 160 banks. Every one of the S&Ls taxes are going up. Thinks it could be done in a more equitable manner.

Fabrega: Without HB 150 the banks will pay less taxes than they have ever paid. Share taxes was repealed - banks would pay \$900,000 in corporation license tax, so bank taxes are increasing. S&Ls will pay \$200,000; banks will pay about \$3 million more. If we don't do anything, the banks will enjoy the lowest tax ever. Suppose a taxing method based on deposits and loans were imposed. Banking is a business like any other business and should be treated all alike. If you allow a reserve method, allow it throughout the corporation license tax.

Sheehy: Banks will be paying \$3-1/2 million for eliminated bank shares tax, plus what they are paying now. Banks agree with the tax. S&Ls are being faced with making up some of the loss.

Fabrega: Removal of bank shares tax was not Legislature's decision.

Sheehy: Would have to look at that decision again. Should not strictly outlaw the bank shares tax. Any state taxation that requires U.S. obligations to be considered directly or indirectly in computing that tax is unconstitutional.

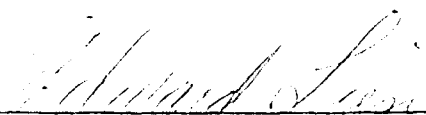
Sivertsen: Just getting back to the main focal point in this whole thing - we are forced to take a look at this issue. Have had a lot of testimony from banks and S&Ls - nobody has been able to tell me that this bill is unfair with any real legitimate reasons. Feeling maybe the S&Ls have not paid their fair share and maybe the banks have paid too much.

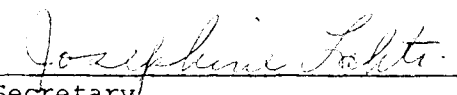
Pitts: The amendment offered by the League of Cities if acceptable to the committee, is fine with the banks. No objection by the S&Ls.

Sheehy: It is within the power of the Legislature to treat corporations differently. Thinks it necessary to have the bad debt deductions. Because of the particular nature of the type of corporations we are dealing with, this deduction although denying it to other corporations, is justifiable and he doesn't think it would face any challenge in the courts. In making this equitable, have to look at where the tax is going to hit. Impact is going to hit S&Ls harder than the banks and that is the reason we are asking for this amendment. Impact will be greater on S&Ls than on the banks. A 53% increase is going to shackle S&Ls.

George Anderson, Accountant, said he doesn't like to see anyone treated differently. Much more dangerous than treating them all the same.

Meeting adjourned at 9:00 a.m. This was to be last subcommittee meeting.

  
\_\_\_\_\_  
REPRESENTATIVE EDWARD LIEN, Chairman

  
\_\_\_\_\_  
Secretary