

HOUSE TAXATION COMMITTEE
46th Legislature

Chairman Herb Huennekens called the hearing to order in the Old Highway Building auditorium, Helena, at 8:30 a.m., March 2, 1979. Representatives Dassinger and Sivertsen were absent - all others were present as was the staff attorney, Randy McDonald.

Bills to be considered today were HB 873, HB 830, HB 814.

Rep. Huennekens opened the hearing by stating proponents and opponents of HB 873 would each be allowed one-half hour to present witnesses and evidence, and then there would be questions from the committee.

It had been brought to the attention of the committee that other health insurance companies were taxed at 2 3/4% on the premiums which were paid to them and the "Blues" were not taxed. There was an inequity. There could be two routes to go - one would be to remove the tax from private industry and the health insurance field. That would lead to proposals to remove the tax from all insurance. Or to tax the Blues.

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The essence of a taxation system is that it be broad based and everyone shares in the tax burden and that's one reason why insurance is taxed. The committee decided to review the alternative possibility that the so-called "Blues", Blue Cross and Blue Shield, did have an unfair advantage in that their policies were not taxed. That resulted in the preparation of HB 873, which is a committee bill.

The discussion was then opened to any members of the committee who cared to speak as proponents.

Rep. Fabrega said you have pointed out what brought about the problem, and the reason the committee needs to take a look at HB 873 to determine which way to go. At the present time there is \$125 million of accident and health insurance written in Montana, and \$48 million of accident and health insurance written by Blue Cross and Blue Shield, leaving some \$77 million worth of premiums that are taxed at 2 3/4%, which bring in a revenue of \$2,109,000 to the state. Part of that money obviously goes to operate the office of the Commissioner of Insurance, which, among other things, provides some services for each individual policy holder when the policy holder has difficulties with the insurer as to how a claim is settled or in other areas.

I think Blue Cross and Blue Shield made a very good point. The tax is passed directly to the consumer whether that be in a non-profit or profit corporation. Obviously, it becomes a part of the corporation doing business. And so, the question that the committee is faced with, because we recognize the necessity of health insurance, is whether we should go in the direction of passing HB 465, and not taxing health insurance to anyone. Or whether, as the chairman mentioned, that would lead to the fact that other insurances - life insurance, fire insurance - all of those things are also a prime necessity of life, were removed from taxation, then we are getting into closer to \$12 million in revenue that would be dropped off.

At the same time I have introduced HB 646, which is a variable schedule on the premium tax. It is aimed and designed to help domestic insurance corporations or health service corporations. By domestic, I mean that are incorporated in Montana, and if they invest their assets in Montana, depending on the degree but it drops down by 1/2 percent of the tax until it gets down to 3/4% if the assets are invest 100% in Montana. So one of the things that the committee needed to look at was whether Blue Cross and Blue Shield would be in a position and willing to invest their reserves and assets in Montana and thereby reduce their tax load to 3/4%.

Now, at the present time Blue Cross and Blue Shield pay 20¢ per policy holder as a fee to the Commissioner of Insurance for the services that the Commissioner's office supplies. Whether that is enough to cover the cost of what they do toward the subscribers of Blue Shield and Blue Cross, we haven't delved into - I believe there is another bill dealing with that.

And so really the question in the sense of equity which this committee has dealt with very much, is whether we should remove the taxation on all health insurance - whether the state can afford to do that - or whether we should provide an alternate means of taxation as I discussed in HB 646 which would in fact put a very small burden, but just the same a burden, and in looking over the annual statements of Blue Cross and Blue Shield, the amount that was put into reserve for this year as of the last report, a 3/4% tax would not have amounted to one-tenth of the amount that went into the reserves.

So eventually I suppose it would have to be passed on but that is really the question - which way do we go? In time I suppose if the competitive advantage of the 2 3/4¢ tax is sufficient, Blue Cross-Blue Shield should just about have 100% of the premiums so there will be no tax. So maybe that is the direction in which to move. But at the present time, two out of three Montana families that carry health insurance are paying the 2 3/4% tax - those that are with private carriers.

Now the same problem is also addressed to the Workers' Compensation Insurance. The State of Montana has Plan 3 of the Workers' Comp which provides workers' insurance or industrial accident insurance. The state itself is not subject to the 2 3/4%, but all of the private carriers are. Again, as a cost of doing business to any business man who provides the Workers' Comp insurance, it is required by law - and again it is a matter of equity and fairness - either the state fund should pay that tax or again we should remove that. At the present time the Workers' Comp premiums written by private carriers amount to close to \$28 million with about \$760,000 tax. And I understand the state fund writes some \$20 million of insurance. Again, I suppose that the 2 3/4% is the factor and the cost of providing the coverage of the state fund will eventually move into a monopoly position in providing Workers' Comp and so there would be no tax collected if we let the system go the way it is. And I think that is the rationale of having provided the bill so that we could have this visit with you.

Because it is really a decision that the committee has to make in that direction, I would have to say that since I requested the committee approve calling for a committee bill that I perhaps may be responsible for the fact that I thought, in conjunction with HB 646 with its flexible schedule, there was a possibility of bringing a sense of equity and also 646, in my mind, is a very desirable bill because it will encourage the creation of a larger insurance

industry in Montana. Montana has only 9 domestic insurance corporations as against North Dakota with 29 because they do have a flexible thing and I believe the insurance industry is a very desirable industry for Montana, so a combination of those two bills brought about the third bill and the visit this morning.

Rep. Huennekens asked if there were other members of the committee who would care to speak as proponents on HB 873.

Rep. Lien said he would like to add more to the comment of Rep. Fabrega. The committee is sitting here working and trying to set equitable taxation. However, Rep. Fabrega will find that as far as the citizens of Montana are concerned, tax equity is the tax paid by someone else! Are trying to resolve all tax laws and so are looking into this matter. HB 873 is just another step along this road.

The chairman asked if any other committee members wished to speak. He then asked if there are proponents in the audience who wished to speak - they could speak from their seat or use the microphone.

Jim Murphy, Assistant Administrator of the Division of Workers' Compensation, and I have several amendments for your consideration. Under proposed language, it would appear that the commission would be out to collect the pertinent tax from each employer each and every time that the employer is billed on the regular premium on the Workers' Compensation coverage. We do not feel this is necessary and we think this amendment will allow the base premium tax on the earned premium to be paid at the end of the year, which is the same as any other insurance carrier does. They figure out their premiums and remit one check to the Commissioner of Insurance and this is the way the policy of the commissioner has been. See amendment proposal attached. Exhibit #1.

The fiscal note shows a figure of some \$33,000 - if this language I propose as an amendment is put into the bill, that \$33,000 can be scratched since that is about what it would take to do computer programming and readjust forms if it were necessary to bill each employer each and every quarter. The net effect as far as premium tax collections in the amount shown in that fiscal note, and the state fund, would be the same. We would support the portion of the bill dealing with the state fund and the House amendment if the state fund operates as a mutual insurance carrier. If amended, this bill, the Workers' Comp Insurance and state fund should be placed in an equitable position. Would be glad to answer any questions.

Rep. Huennekens asked if there are any other proponents?

There appeared to be none present.

Don A. LaBar, partner in the law firm of Church, Harris, Johnson & Williams, representing Blue Cross of Montana, opposes HB 873. See his testimony attached - Exhibit #2.

James Tom Harrison, Jr., representing MPS (Blue Shield), opposes HB 873. There seems to be a concern about an advantage or a favoritism to companies such as Blue Shield or Blue Cross because they do not pay the premium tax that private carriers do pay. That is really not unique to the insurance industry.

The real question of inequity, if there is really an inequitable situation, should be addressed broad-faced and not miss the difference in non-profit and profit organizations. They are provided for not only in the Montanan's Business Code and Regulations, but in the Internal Revenue Code of the United States and then, most if not all, in codes of other states. So that inequitable situation, if that's what you want to term it as, exists between co-ops, between many institutions that are throughout the business community in Montana and the nation. As the committee knows, the Blues have been looked into and this tax considered over the years. Similarly, that change for co-ops versus profit corporations has been considered on numerous occasions and each has come to the same conclusion. The premium study during the 1971-72 interim mentioned by Mr. Labar resulted in the present legislation enacted in 1973 and a specific disavowal of putting a premium tax on the Blues for the various reasons that are being discussed.

The provisions of HB 646 mentioned by Rep. Fabrega wherein the effective rate of 2 3/4% premium tax is reduced to 3/4% if all investments by insurance companies are made in Montana, has a lot of attraction to private industries. They have the people that can handle the money. They have the people that can invest in mortgages; they have mortgage departments; they are, in fact, in the real estate business in Montana and throughout the nation. The big companies - Hartford, Aetna, Prudential, Connecticut, General - they finance many ranchers in this state. They finance many buildings, etc. They have department personnel, actuarial people, economists, etc., to handle all that.

Blue Shield is not in the money business. We are not in the real estate business and do not want to be in the financial finagling business. Do not want to hire those people in order to take advantages, if there are advantages in HB 646 and it is passed, of any possible reduction of tax by having a real estate department and a financial department, and increase really the cost of administration and take advantage of that, and then pass that cost on into the tax. Just don't feel they want to make that move into the real estate market. You may look at that and say that would still be good for Montana in that we would be putting some money into Montana industry, Montana farms, and that may be true, but the truth of the matter is that we are not in that business and we prefer not to get into that business.

Think the comment most appreciated is that the insurance industry is good for Montana, and would like to make it attractive. The insurance industry, if you are talking about taxes, is in Montana - these people are Montanans - they all work here, pay taxes here, their jobs are here - they have an interest in Montana.

The thrust of this bill seems to be a grand statement that we like the insurance industry - to make insurance appealing and more attractive to the people who live in Chicago. We are here now and we have people throughout this state so that if someone has a complaint or concern or an inquiry, they can make it in their home town in most cases and they don't have to get on the hot line to Chicago. So, as far as advantages are concerned, if there is this disparity and advantage to the Blues, why are the figures of \$78 million written by private companies versus \$48 million by the Blues used? If the trend is towards a monopoly, why aren't the Blues capturing more and more of that market? Because those disadvantages are not present when you go through the practical steps of not only the profit corporation and the other investments they can make and the parameters that are set upon the Blues because they are non-profit, although they appear to be present, are illusory.

Montana is an attractive state for private insurance industry, but the private companies are not here advocating this bill as proponents in an attempt to cure this apparent discrepancy - and it is only an apparent one.

Mr. Harrison commented on the conversation he had with Rep. Fabrega yesterday. There was apparently some concern on the reserve and how the reserve had grown in the past year in the Blues. Addressing only to the Blue Shield portion, nationally over the calendar year of 1978, all plans - not only the blues, but private carriers and so on - had anticipated an increase in medical care costs of about 18%. It has been running between 15 and 18% for several years. Fortunately the providers and medical people had got the message on the increased costs because across the nation the year turned out to run between 9 and 11%. The cost had been set - or the premium charges have been set on 18%, and there is no question about it, the reserves grew as a result of that year. If the medical costs remain in line with the 9 to 11%, the premiums will reflect that in the type of growth to the reserves will not be present. However, as to the magnitude of its growth, in 1978 the Blue Shield reserve did grow about \$2.5 million. In 1975 it lost \$1 million; in 1976 it lost \$.8 million, so this is a balancing thing and to take a particular year when you are attempting to accumulate a reserve for an organization such as this, which will hopefully last for hundreds of years, and say you had too much in reserves, is not quite right. It is true you can single it out, but you should look at the overall total growth of the reserve in order to have a handle on them. The reserve right now stands at \$4.8 million and that represents 2.05% of income. The underwriters tell the Blues that ought to be 3%, so don't think there is any economic indication that the reserve is too large at this time although it did grow substantially in 1978, which is not as high as it ought to be and is not as high as would be necessary to meet several years where a million dollars would be lost. Thank you.

Rep. Huennekens asked if there are other opponents.

Virgil Miller, president of Blue Cross of Montana, appeared in opposition to HB 873 - see his testimony attached, Exhibit #4.

Other opponents:

Emery W. Geyer, speaking for the retired private citizens, is in opposition to HB 873. You are saying that Blue Cross and Blue Shield have an advantage due to the fact that they are not taxed. Am a member of Blue Shield. A retired citizen living on a limited income must find places where some protection can be obtained. The senior citizens are entitled to some advantage, or don't know who is. That's why Blue Cross is carried as a supplement for medicare insurance. Medical expenses have expanded tremendously in the last few years, as has the cost of insurance. Cost of MPS has increased from \$13.50 four years ago to \$31.42 as of today. That is as far as I can go. If I don't carry some kind of insurance, I am sunk. Blue Cross, Blue Shield is the only one I have found that can afford at all. Thank you.

Curtis O. Peterson, Aluminum Workers Trades Council, Whitefish, MT, chairman of trades council that covers all of Montana, opposes HB 873 for one reason - A cap on amount the company will pay for insurance is set when negotiations are made. If HB 873 passes the extra money will have to come out of their own pockets or benefits will have to be cut. See testimony attached - Exhibit #5

Ray M. Benegas, Oil Chemical and Atomic Association, Great Falls, on behalf of members is opposed to HB 873.

On behalf of Local 2-470 O.C.A.W., Billings, Earl Taylor, President, stated they are in opposition to HB 873. See testimony attached - Exhibit #6.

Glenn A. Roush, representing Local 2-493, Oil, Chemical and Atomic Workers Union, Cut Bank and Shelby, are opposed to House Bill 873, and urge its defeat. See testimony attached - Exhibit #7.

John Kaiserman, was sent by Local 2-442, O.C.A.W. (oil workers), Laurel, MT, to oppose HB 873. See testimony attached - Exhibit #8.

James Schmauch, A.W.T.C., Columbia Falls, president, opposes HB 873. See witness sheet attached - Exhibit #9. Members of Blue Cross - 1100 members.

There were many other persons present who were opposed to HB 873. See the witness sheets and list of names which are attached.

Rep. Huennekens asked for any other opponents. There seemed to be none. The normal procedure in hearings is to have the proponents close. Speaking as Chairman of the committee, we do appreciate the opportunity to hear your views on this matter and I can assure you that the committee will give full consideration to the points you have made. Would you care to close Rep. Fabrega? No, I think you have said it. Thank you then.

Are there questions from the committee?

Rep. Burnett - Mr. Harrison, you mentioned \$4.8 million in investments - what kind of investment do you do with that? Harrison said someone in the room should be able to answer that so Mike Donovan, President of Montana Blue Shield, said investments are in a portfolio divided between stocks and bonds - 50% is in corporate and government bonds and the balance is in securities of companies that are considered to be trustworthy investment quality, in addition some real estate, \$900,000, on which property tax is paid.

The president of Montana Blue Cross said their investment committee was putting approximately half of their reserves which are about \$5.6 million as of today into Certificates of Deposit with Montana banks. The remaining amount of it is invested in Grade A or better grade of corporate bonds and Grade A or better corporate stocks. A small portion of it is in small corporation stocks.

Virgil Miller, President of Blue Cross, said their investment committee consists of 3 board members and himself and they use an outside investment firm for advice.

Rep. Reichert - Mr. Harrison, are the Blues taxed in any other states that you know of? Terry Meagher, Montana Insurance Department, Helena, said he was aware of them being taxed in 6 or 8 other states. Mr. Harrison did not know of any. Mr. Miller shook his head Yes.

Rep. Reichert - Mr. Harrison, I am interested in the administrative cost. Could you tell us what the top administrative salaries are for Blue Shield people? Mr. Harrison couldn't and explained his position: I represent them during the legislature and do not represent Blue Shield during the course of the year. Rep. Reichert: Does the president of the group have that informa-

tion? Mr. Donovan stated currently administrative expenses are 10% of premiums received. Salaries are commensurate with what is paid for other such companies. Rep. Reichert asked if he would say that they are between \$50-\$100,000 per year at the top level? (No definite answer was given) It was intimated they were closer to \$50,000, however, by Mr. Miller.

Rep. Harrington - Tom, because of the fact, as you stated in your testimony, the actual costs ran lower, is there possibly some group insurances that will not be increased? Mr. Harrison said he hoped that would be the case, but in all honesty the cost is not based solely on what occurred last year. I think as you would recognize, that because of the growth of reserve (but also because we would have to have a consideration of what the underwriting cost would be for next year) assuming a stable market, we would assume what you say is true.

Rep. Nordtvedt - Have a question for the insurance examiner. Does this 10% administrative cost of the Blues compare with comparable other insurance companies? Mr. Meagher said he would have to really make an analogy.

Rep. Fagg - Mr. Donovan, assuming an analogy, what is 10%? 10% equated to what? \$90,000; \$200,000? Mr. Donovan said 10% of \$29 million - administrative costs were \$2.9 million.

Rep. Huennekens - Mr. Harrison, you did state that Blue Cross, Blue Shield preferred not to go into an investment program, but you do have, according to the testimony, an investment program - quite a program right now. Please expand on that. Mr. Harrison - well, I guess to expand on that, the program we have right now is just a traditional investment program that anyone can have administered by a trust department of a bank. Rep. Huennekens - so it is not a trust program particularly one keyed to taking advantage of peculiarities of the tax equation? It is just a trust program which is the same as I suspect many people in this room have. Would you see any vast increase in effort to make the investment in Montana corporation securities as opposed to non-Montana corporate securities? That would be merely a matter of judgment on the part of the investment board? Certainly it would, but I think you would have to examine the investment quality of Montana corporations, not from a local standpoint, but from standpoint of qualified investment advisers. After you get out of Montana Power, I think that list would be rather brief.

Rep. Huennekens - Mr. Harrison, who chooses the board of directors and what is the composition of the board as far as occupation? Mr. Donovan, said he could only speak for Blue Shield. The board has 19 people chosen from throughout the state - 10 are physicians, 9 public members are chosen by the same body. The same public members are chosen by the industry who are physicians chosen by local medical people who then choose the public members. Huennekens - in essence then, the medical profession chooses the physician members to start with who then choose the public members? The public members are chosen by the same body. Huennekens - essentially it is an operation with Montana medical profession.

Rep. Huennekens - I would like to ask the same question of Blue Cross. How are your board members chosen and what is the make-up as far as occupation? Mr. Miller stated we have a 13-member board and the board is chosen by the contracting hospitals in Montana, all of which are non-profit contracts, with the exception of two. Of the 13 member board, 7 represent the general public.

They serve without pay, they get nothing whatsoever for their services. There are 5 hospital members on the board and 1 physician. This board of trustees is chosen by the contracting hospitals - there is a contract with every hospital in the state. Rep. Huennekens - in other words, the hospitals choose the board in essence? Yes.

Rep. Huennekens - Mr. LaBar, where would you find the difference in profit between a mutual insurance company and the Blues? Mr. LaBar said there is a difference in operation in terms of whether one or the other is for profit. Requirements to be a health service organization are set forth in a particular section of our law, and are fairly detailed. Requirements do not apply to the mutual insurance companies. Another difference is, of course, the difference in administration costs. Difference in the investments that these companies can make - health services corporations as opposed to the mutual companies. It may be that mutual companies may have other lines of business that may be underwriting this particular business. In Blue Cross and Blue Shield you have only one business that the company is in and that is to provide health services to the people of Montana. We don't have an opportunity to carry comparable lines or underwrite on a comparable basis. With these companies it depends upon the operation from year to year. In terms of non-profit and profit, you may say that both of these may be non-profit, but in a larger sense there is a substantial difference.

Rep. Huennekens - you mean in the larger sense they are making a profit? Mr. LaBar said in the larger sense there is a substantial difference between the way these two companies do business. Rep. Huennekens - But not in the matter of making a profit? Mr. LaBar said whether or not they make a profit, you should look at the administrative costs. That is the way of looking at whether or not they make a profit because if a company, for example, invests 40% of its income dollars in administration costs compared with one that invests 10% - frankly, he said he didn't have the statistics on mutual companies and that may not be a fair comparison, but he understands there is a substantially larger administrative cost for those companies - he would say that the difference in whether they are non-profit is questionable, because it costs more to operate those companies than it does for companies like health services organizations.

Rep. Huennekens - Mr. Meagher, off the top of your head would you say that there is a great difference in the administrative cost between a mutual company and a non-profit company? Mr. Meagher said he really didn't think so.

Rep. Fabrega - Mr. Donovan, you mentioned your operation cost is about 10 or 11% and looking over your last year's report to the Commissioner, it looks more like 11 1/2% on that - the private sector is considerably higher. Is it more than 2 3/4% higher? Mr. Donovan said they will furnish the committee with an annual study with a chart which lists income and expenses of larger companies. It is higher. Rep. Fabrega - so actually, the 2 3/4% is being passed on to the users of the service? Mr. Donovan assumed so.

Rep. Reichert - Rep. Fabrega, relating to testimony given by Virgil Miller, I believe Mr. Miller said Blue Cross had a reserve of \$5.6 million and that approximately half of that or \$2.8 million is invested in CD's in Montana banks, if HB 646 passes, would that money be eligible for 3/4% tax because it is invested in Montana? Rep. Fabrega said that would be his understanding.

Rep. Reichert wondered how the Blue Cross and Blue Shield would feel about the 3/4% if the money invested in Montana would apply to all insurance. She asked Mr. Miller if their feelings would be quite as strong as they are about HB 873. Mr. Miller said they would be at least 2% less. He had not studied HB 646 because he did not realize he would be asked questions concerning it. They try to keep their investments in Montana. We are Montanans.

Rep. Reichert asked someone in the back of the room if they had a question. They offered some light on the question of profit - they did not use all the money paid to them - they made a profit last year, however, they would not ask for any increase because of inflation.

Rep. Dozier - I have a question along that same line because I got quite a few calls - one of the big points that was brought out to me is that in the last 4 years some of these people have had their rates go up 250 to 300%. Did the cost of medical care go up that much or can someone explain why these costs went up that fast? Does anyone want to answer that question?

Mr. Donovan explained there may be a group that had a 300% loss, so the rate might have gone up - it went up 10-12% on an individual. On a specially rated group, it could have gone up 250-300%. The rate depends on the kind of usage they have had. Medicare supplemental insurance is a different breed of cat. The federal government has reduced benefits on about 9 classifications. The health insurance companies fill in the amount the government is no longer covering, and thus have to raise their rate.

We have talked here today about reserves as compared to investments. Investments is larger than reserves because there is provision for emergencies which runs about \$4 million. This isn't money that we are going to have to come up with in 30-60 days. Other investment is approximately \$13 million. Have \$4 million also in CDs in various banks. Blue Cross has some CDs in Montana and some outside the state. Always try to get the highest interest rate.

Rep. Huennekens - Would like to address a question to both Blue Cross and Blue Shield. It has been a matter of governmental policy for some time to address the problem of retired senior citizens, particularly those with fixed or lower income, by providing a special relief procedure. For example, reduction of property taxes on homes and recreational vehicles, and in the private sector we have reduced rates on prescriptions, etc.

One big problem that has been brought to light in connection with this particular bill, and that is with retired senior citizens. Would it be utterly offensive to the Blues to make a provision for retired senior citizens of lower income that would eliminate the burden of this 2 3/4% tax to them and solve at least a part of the problem that has been raised here today? Can someone answer this question?

Mr. LaBar said he didn't think there would be any objection to such a deduction. But because of the nature of the health care services, we do not feel that this is a tax that should be imposed on any of their members. They do as good a job as possible for all of the people who are part of their plan. Senior citizens are a very important part of our program.

Rep. Huennekens - Mr. Harrison, would you care to answer to this better to the Blues, specifically referring to the senior citizens and their problems? I

would like to hear your answer. Mr. Harrison said he did not think that there would be any concern from them specifically as to a particular group; however, our concern might well be whether or not by creating this special category or whatever you want to call it, that there might be some antitrust, even criminal problems, that we could get into by creating something that couldn't be justified across the board, unless possibly it is legal. Rep. Huennekens reminded him that the question was whether it was offensive. He then answered No.

Rep. Huennekens - Would you think that you have a problem different than that of the pharmacists who provide at lower cost to the senior citizens? Mr. Harrison said he just didn't know the answer to that question.

Rep. Fabrega said obviously the committee has to look at both HB 873 and 465 - would there be any objection from the Blues on doing away with the premium tax on private providers, and if so, how would it affect you? Mr. Donovan said they would have no objection.

Rep. Burnett - Mr. LaBar, on Blue Shield, you said the total reserves were approximately \$5.6 million and your portfolio is about \$8.7 million? (Tape did not record his answer.)

Rep. Vinger - I have a question for Mr. Miller or Mr. Meagher. You mentioned 6 or 8 other states are now taxing Blues. Do you know who these states are and if so, what percentage is being taxed, do you have any idea? Rep. Huennekens asked if Mr. Meagher would know. Mr. Meagher said they had just done a study and the main two variances they found would be in Alaska and the State of Alabama. They take the total income in fees collected and deduct the claims paid, then tax at a rate of 6% on that underwriting cost. Another state is doing it similarly as to rate and tax, etc. Montana and most other states as well as Utah tax at 2 1/4% of net premiums received. That being total gross premiums received less refunds, and then calculate at rate set. Those are the two main returns we got.

Rep. Fagg - We heard from Blue Shield as to what their administrative costs are, what are Blue Cross administrative costs? Mr. Miller said their administrative costs run between 10 and 11%. Rep. Fagg - yes, but what does that run in dollars? Mr. Miller said they handled roughly \$30 million the past year. Their administrative costs would be a little over \$3 million. Rep. Fagg - what is the top salary paid by Blue Cross? Mr. Miller said in excess of \$50,000 - one person is in excess.

Rep. Huennekens - Mr. Meagher, I have seen the list for as many as 30 or 40 different health plans that vary in fees for the same services - do you have any opinion on the relative costs for similar services between the Blues and private insurance companies whether mutual or stock? Mr. Meagher said he was not sure whether he understood the question. Rep. Huennekens repeated - whether or not the same benefits are provided for the same premium? Mr. Meagher said he really didn't know how to answer that question. Rep. Huennekens - then you would say that there really isn't all that much difference despite the 2 3/4%?

The chairman said if there are no further questions from the committee, the hearing on HB 873 would be closed. He thanked all for attending.

Hearing adjourned to usual room 434 in Capitol Building to hear other scheduled bills.

Rep. Burnett, District #71, Luther, MT, sponsor, explained HB 830 is a bill that would transfer all property to a surviving spouse without any inheritance tax. It provides for a 15-year deferral of any tax due because of transfer of property to a child and allowing a credit for the number of years the farm or business is owned by the child.

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830 Rep. Burnett thinks a wife's name should be included on any property and why a man does not do this, he cannot understand. Because of this, this law would recognize a wife had rights. This recognition has not been made previously and he thinks it has been a most unfair tax. Also a son or daughter has to buy back any land or business when it is inherited and many times the farm has to be sold to pay inheritance taxes.

This bill is based on a 15-year period allowance that the property must be kept as a farm or ranch in order to have the benefit of inheritance tax deferral. Otherwise, the proportionate amount of tax due must be paid when property is sold.

Mons Teigen, Montana Stockgrowers Association, said SB 508 would insert federal language into state statutes to accompany this. He would like the committee to remember that there is other legislation coming and would hope that when they all get across the two houses, you can work something out that would be of benefit to farmers and ranchers and small businessmen. This affects small businessmen just as well as it affects farmers and ranchers in preserving the family farm. The best way is to have some corrective in the inheritance field to keep families on the farms. It would be better to keep people on the farms through this way than through any other way.

Tom Stohl, administrator of the Inheritance Tax Division, of the Department of Revenue, does not oppose HB 830 at this time. There is a Senate Bill 508 that will probably come over from the Senate. The committee should be aware of HB 510. He recommends at this time HB 830 be held for final action until all bills are before the committee to decide if any one is better than all three.

There were no opponents.

Rep. Burnett closed saying he feels the committee needs to have all bills before them and correlate to come out with one bill. He indicated when he had it researched that all bills should be put into one at that time. Do need to pass some bill.

Rep. Edward Lien, District #49, McCone County, sponsor of HB 814, explained this bill would abolish the Montana inheritance and estate tax for decedents who die after December 31, 1978. This bill is the most severe as far as revenue from this type of tax is concerned.

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814 An amendment to change December 31, 1978 to December 31, 1980, and to change January 1, 1979 to January 1, 1981 was offered by Rep. Lien. This bill eliminates unpopular and unsavory way of funding the general fund. Treats everyone equitably. There would be no inheritance^{tax} if the bill prevails. It would reduce state revenue \$6 million per year - \$12 million in the biennium.

Are trying to get Montana completely out of this tax. It will take effect after December 31, 1980 and then will be 18 months after that before the effects takes place and the state feels the effects.

Sharon Peterson, representing WIFE, W.F.U.N.F.O., Farm Bureau, Grange, Montana Cattlemen's Association, Helena, which have about 80,000 members who are Montana citizens, asked for passage of HB 814.

Lucille Anderson, speaking for 1800 Montana Cowbellees, feel Montana inheritance tax laws are unnecessary and unfair. See her testimony attached.

Nora Hanson and Howard Hanson, Big Timber, are family ranch owners and are in support of HB 814. They explain their sentiments regarding inheritance taxes on attached testimony.

Gene Spilde, Big Timber, thinks this is a bill that is long overdue.

Steve Doherty, Northern Plains Resource Committee, is concerned about the effects of this subject, HB 814 and on HB 830. He thinks it is time those taxes were carefully looked at. Pressures are hard enough and if we want to keep land in Montanan's hands and operated by Montanans, he thinks it is time to do something about it.

Alice Fryslie, Montana Cattlemen's Association, Helena, supports HB 814. See testimony attached. Other proponents are listed on attached visitors' register.

Bill Groff, Special Legislative Adviser for the Department of Revenue, told the committee they set the policy. There are some errors in this piece of legislation. Life insurance policies are still included in the tax. Some things on the transfer of the property that have to be considered on this. He would like to work with a subcommittee on this since there are some errors in the bill.

Tom Stohl, administrator of Inheritance Division, DoR, agrees with Mr. Groff. There is one problem - the Montana estate tax. There seems to be a great deal of confusion. The Montana estate tax does nothing more than to pick up the federal credit on 706. The maximum credit if you do not pay the State of Montana on a \$2 million estate will not be saved - it will go to the federal government because of a deductible allowance.

Rep. Lien closed saying HB 814 was drafted as a repealer, but it ran into problems. Will have to be fine tuned. This has been an absolute bonanza for life insurance companies. Thinks the tax should be equitable on all forms of business.

Questions -

Rep. Bertelson asked Mr. Stohl if the estate tax were deleted from this bill we would continue to pay the same tax. It would just be going to Montana not the federal government. Mr. Groff said about \$2 million, in excess of \$1.5 million, but not exceeding \$2 million would be taken out of Montana's funds and given to Washington. If you have not paid the State of Montana that amount, they remove that credit and you have to pay it to the government.

Rep. Fabrega said the credit for state death taxes - first of all there is a \$30,000 unified credit applied against the tax and then as it becomes taxable (on a federal schedule - is charted by federal government) it comes into being with no surviving spouse probably at \$400,000; with a spouse, probably at \$800,000.

Rep. Johnson asked Mr. Stohl if, under HB 830, only the amount that exceeded the credit could be deferred. He said the Montana state tax requires that that amount be paid within that time.

Rep. Vinger: If an individual owns a house in town, the man passes away and the wife passes away - can that child inherit that house free even if she lives at college? Just follows the line of decedent.

EXECUTIVE SESSION

HOUSE BILL 524 - This bill deals with the problem of federal law regarding railroad taxation, Mr. Jim Kenaley, Regional Tax Manager for the Burlington Northern, Billings. Needed material from the department and railroads as to the results when applied to the federal preempt law. Let railroad go ahead or let railroad follow is the question. He turned this over to Rep. Dassinger for questions.

Rep. Dassinger moved that HB 524 DO PASS. A one page synopsis of 1978 BN's overall indicators was handed out. This goes into the taxation of BN.

Rep. Huennekens said he would prefer a five-year average to see if they were able to keep that stability. Could the department change that formula and end up with the same figures at the bottom? We are talking about the transportation of BN in this bill. If the railroads get a classification break, would we have to do it for all utilities?

Mr. Delano said he had worked up a sheet on BN taken from the Interstate Commerce Commission report showing their rate of return on the transportation property. If their rate of return goes down, then their rate should come down.

Rep. Nordtvedt mentioned the manager's analysis value shows a book value of \$1.3 billion. What kinds of operation are included in those figures? 800,000 acres with timber on it that is producing oil and gas is owned by BN. Would be looking at these rather than the transportation portion of it. He wanted to divorce and have two operations figures. Resources enable them to borrow money on capital improvements for the railroad. Subsidies carry the railroad.

Mr. Kenaley said the conclusion of value is the total of the three above indicators and is weighted. Rep. Nordtvedt thinks the cost indicator is a poor indicator. Mr. Kenaley said in valuing using utilities, you use the work in progress figures.

Rep. Vinger asked if the railroads do any short-term financing. Mr. Delano told him they have a \$60 million revolving fund provided for this. 60¢ of the coal car fleet is owned by the private facilities that they serve. Rep. Vinger asked if the rate of return is your ability to repay your borrowed capital? Mr. Kenaley said you are getting into another area when referring to rate of return on investment.

Railroads are being divorced from the original intent - when given land grants, those grants were an incentive to turn them over to the homesteader as an incentive, and now they get their main income from these granted lands - coming from timberlands. It seems these should be considered as a factor in the total income, total revenue of the railroad should be included.

Mr. Mantz, DoR, said values on certain operating properties are not considered at all.

Rep. Fabrega mentioned at the time the land grants were given, they were for building the road and without other land figures of revenue would almost be in

the shape of the Milwaukee. The depreciation investment of \$2,588,899 - does that agree with the DoR?

Rep. Reichert asked if it would be feasible to have a transportation division and a resource division. Couldn't do what Pennsylvania railroad did could they? Mr. Mantz said the department handles taxes for both sides. No, it shouldn't happen to us unless the people who own the company would turn us around.

Rep. Williams said the bottom figure of 2.25% rate of return on the transportation division shown on the attached sheet, Exhibit #1, applies only to that division; what would be the figure under a combined percentage? Regardless of the value of the transportation division, what is the total BN operation for 1977? Mr. Kenaley said would probably be about 5%.

Rep. Huennekens asked if the railroad would object if HB 524 should pass and if they are assessed at 12% rate to be equitable with other utilities, and if the valuation is fixed so their income is about the same at the present. Would this alleviate any lawsuit possibilities.

Mr. Kenaley said classification could be in that class, but leave off the second portion. He asked if it were possible to review and change somewhat your approach so that the yield would remain about the same. Otherwise there might be grounds for appeal process.

Mr. Burr said the federal law isn't really to help railroads - it is to prevent states from taxing them inequitably. He doesn't think HB 524 would do anything - takes from 16 to 12%, or whatever, and doesn't affect assessment. If looked at, commercial property is being appraised at 50% of market value. If market value is used, would still want 55% of face value and then 2% in the next bracket. There is some question as to whether a state can have a classification system. Doesn't think this is a good ground for a case at the present time. Montana is one that is probably liable to a tax court case. Section 306 says can't discriminate against railroads is an infringement against states' rights to tax. Have to prove we will not be looking at the depreciated cost and things like that where we take a commercial property and assess it on depreciated cost. Assessment of 1.3 is just about half of cost. A lot of facts have to be established before a case can be tried. Eliminates discrimination that is found in other states. When looking at commercial and industrial property, we are looking at property that does not sell on the open market. Utilities don't sell either, and use the same method of evaluation, which is at 100%. If the court decided against the state, they wouldn't just put them in an 8.5% class - they might tell us to take the \$1.3 billion and take 55% of that. Doesn't really deal with the assessment of property.

Rep. Huennekens said statements at the hearings said 21 states were being in a discriminatory position.

Rep. Reichert mentioned there is a question of whether railroads should be in a class by themselves,

Rep. Dassinger said if the railroads won a case, the other property in that same statutory classification would be in the same position.

Rep. Nordtvedt asked Mr. Burr if replacements costs depreciated is the basis for tax on mainstreet hardware stores.

Rep. Fabrega explained regarding the replacement cost depreciated. If put at 8.55%, you could simply take 55% of that \$2,206+ million and that would be more defensible than the unitary method of assessing on income. Replacement of railroad would not be as it is now. When does value on unit value include land, etc.? Even if the classification system were the problem, their composite would be different than 8.55. Would be assessing locomotives, right-of-way, etc., in each class in which that type of property is assessed.

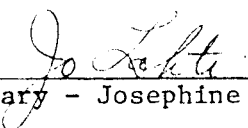
Bill Groff said most states are using a similar system that Montana is.

A great many railroads are not land grant railroads, Rep. Dassinger mentioned. The intent of the land grants was that it be sold to homesteaders.

Meeting adjourned at 12:00 noon.



REP. HERB HUENNEKENS, Chairman



Secretary - Josephine Lahti