

MINUTES OF THE MEETING
TAXATION COMMITTEE
MONTANA STATE SENATE

January 30, 1985

The seventeenth meeting of the Taxation Committee was called to order by Chairman Thomas E. Towe at 8:05 am in Room 415 of the Capitol Building.

ROLL CALL: All members of the committee were present except Senator Brown.

CONSIDERATION OF SENATE BILL 64: Chairman Towe recognized Senator Gary Aklestad from Senate District 6, chief sponsor of the bill. He explained that in past years a 20 percent reduction has been allowed in the valuation of farm homes. He said that action of the court has changed that practice and that the practice is not now consistent among Montana's counties. He said the reduction is justified by the increased cost to build a farm home and its decreased resale value. In addition those homes must provide their own sewer, fire protection, etc.

He submitted amendments to the committee which would change the green belt legislation by clarifying that the deduction is only to go to a true agriculturist and not to rural subdivisions. He said the amendments would generate revenue for the state and that the fiscal note accompanying the bill does not reflect the added revenue produced by the amendments.

PROPOSERS

Alan Eck, representing the Montana Farm Bureau Federation, said his organization supports SB 64. He submitted a written statement (Exhibit 1).

Mr. Gordon Morris of the Montana Association of Counties, also rose to support the bill because the amendments would increase the property tax base of local governments.

Mr. Greg Groepper, Administrator of the Property Assessment Division, Department of Revenue, said that Director of the Department, John LaFaver, had already sent the committee a letter on some of those issues. He said the Department has no position on the bill, but supports the amendments which close the current loophole in the green belt law.

OPPOSERS

Mr. Phil Campbell of the Montana Education Association said that his group opposed the bill as drafted because of its impacts on education funding, but that the amendments would likely change their position on the bill.

Questions from the committee were called for.

Senator Severson asked for clarification on the 6.84 percent figure.

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Senator Aklestad said that the main purpose was to give the 20 percent reduction on farm homes and that if a formula would do that better in relationship to other legislation, he would accept that.

Senator Goodover asked where the additional revenue produced by the amendments would come from. Senator Aklestad said that homes on the edges of town currently falling under the 20 percent reduction would no longer be able to claim that.

(Senator Brown joined the committee at 8:18 am.)

Senator Neuman asked how much increased revenue would be produced. Mr. Groepper estimated that the increase in valuation would be \$51 million and that the increase in revenue would be about \$12.5 million.

Senator Mazurek asked why fair market value cannot be used with agricultural residences? Senator Aklestad said that hopefully this would do that. He pointed out, however, that few farm homes are sold just as homes and that normally they are included in the price of a total farm.

Senator Eck said that another inequity was to compare farm homes with surrounding subdivision houses. She then asked questions about the specifics on the production quotas in the amendments. Senator Aklestad said that he tried to hit the middle production estimates between irrigated and nonirrigated land.

Senator Eck asked if some subdivision residences would be able to maintain agricultural classification with those amendments. Mr. Groepper said that while there could be isolated instances of that, the amendments presented a good, fair test of the agriculturist. The Department, he said, would be satisfied.

Senator Hirsch asked if mobile homes in the country would be eligible for the deduction even though they are moveable and saleable. Mr. Groepper responded that mobile homes all over the state are valued in the same way. He said they pay on the evaluation less depreciation and that if they are on a permanent foundation they are taxed as real property, if not on a permanent foundation they are taxed as personal property.

Senator Neuman asked about a farm where the residence is not on land contiguous with the rest of the farm. Mr. Groepper said that the test is use, not ownership, and that such a residence would not qualify for the 20 percent reduction even under current law.

Senator McCallum asked if the production rate would be a problem for poorly producing land. Mr. Groepper said those problems were handled by the income threshold.

Senator Severson asked about folks who live in town, but lease the farm property. Mr. Groepper said again that green belt is a

use law, not an ownership question. If it is used as agricultural land, the deduction would apply.

Senator Towe asked if Mr. Groepper felt comfortable with the \$51 million and the \$12.5 million figures. Mr. Groepper said, yes, his Department had originated those numbers. He explained their basis to the committee.

Senator Towe asked for an explanation of the effective date which was made to be consistent with the new appraisal cycle.

Senator McCallum asked how this applied to timber land. Mr. Groepper said the test for timber is different and requires active management for production to fall under the green belt law now.

Senator Lybeck wanted clarification of the threshold for management of the timber and Mr. Groepper said it would be 1500 board feet as of 1967.

Senator Lybeck inquired about the actual tax dollar difference in a home of equal value under the green belt and one not under that law. Mr. Groepper said that it would be a 20 percent difference. Senator Severson further clarified it by saying that the land was valued at market value as agricultural land and Mr. Groepper said that the \$51 million estimate was clearly based on land.

Senator Towe said the tests and thresholds in the bill might be difficult for some in the eastern part of the state. He inquired about putting in a acre limit. Senator Aklestad said the bill would not solve every problem and that those with 20 or 30 acres not producing should not qualify for the deduction. Mr. Groepper agreed saying that if they were truly agriculturists they would meet the gross income measure somehow.

Senator Eck said she wanted to rule out subdivisions, and keep in only the bona fide farms. Senator Severson agreed saying that a part-time farmer would have to meet the \$1800 gross income threshold.

Senator Aklestad closed saying that he wants the bill written to achieve the 20 percent reduction to true agriculturists, and that it would also improve the green belt law. If the committee preferred to further amend the bill with a formula rather than the 6.84 percent figure that would be acceptable.

FURTHER CONSIDERATION OF SB 48: Senator Towe called the attention of the committee to the gray bill incorporating his suggested amendments. Exhibit 2 was also distributed as further explanation of SB 48. He then proceeded to go through the amendments.

Senator Towe included in his remarks a discussion of the formula that would be plugged into SB 48 with these amendments. Basically the formula is:

$$P = \frac{8.55}{B}$$

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Where:

B = a certified statewide percentage of increase.

P is rounded down to the nearest .01 percent.

And:

$$B = \frac{x}{y}$$

Where:

x = the appraised value as of January 1, 1986
excluding new construction.

y = the appraised value as of January 1, 1985
excluding new construction costs.

B is rounded down to the nearest .001 percent.

Senator Towe gave an example of the working formula based on an increased valuation of 130 percent. If $y = \$10.9549$ billion and $x = 4.7630$ billion; then $B = 2.3$, and $P = 3.71$ percent.

Discussion followed which covered the following areas: 1) The formula would be the same for residential and commercial classes, though the numbers for x and y would be different, resulting in a different percentage of taxation. 2) This would not effect utilities. 3) The Department of Revenue had a handout (Exhibit 3) which plugged projected figures into the formula. 4) Real figures would be impossible to have before voting on the bill because the new valuation cycle was not yet in play. 5) The formula itself does not address the issue of separation of the commercial and residential classes. 6) The effect of combining those two classes can be roughly determined by adding twice the residential percentage to the commercial percentage and dividing by three.

The committee then turned to the issue of the importance of the bill in relationship to taxation of the railroad. Chairman Towe explained that annual appraisal was necessary to keep the railroad from deducting inflation from their taxable valuation. He also explained the unitary system which allows the railroad appraisals to come in based on cost, income, and debt (i.e. stock and debt). The Department then uses a formula to decide the most important reflection of value by percentage for each of those three prongs and thus arrives at what the courts would agree was "fair market value". Senator Towe said the floor beyond which railroad taxation should not drop was salvage value of the property. He said that currently Burlington Northern is taxed at one-tenth to one-half of salvage value.

The adjustment for inflation across the classes cannot be applied to BN because of the unitary system which the Revenue Oversight Committee has endorsed for railroad valuation. That is, the rail-

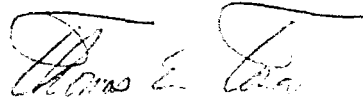
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road valuation. That is, the railroads are using the unitary system and the others are using true market value which causes confusion in equitable handling of taxation. Chairman Towe said that AT&T for example uses a formula weighted at 40 percent for cost and 60 percent for income, with no credance whatever given to stock and debt. He said doing this alone would increase railroad valuation up to \$15 million.

Senator Goodover inquired about the possibility of freezing the unitary system and applying the same formula to all.

Mr. Groepper suggested that the committee invite Denny Moreen, the state's attorney in the case against Burlington Northern, to come and explain the complexity of the issue to the committee.

Senator Towe adjourned the meeting at 10 am.

A handwritten signature in cursive script, appearing to read "Thomas E. Towe", is written above a horizontal line.

Chairman

ROLL CALL

SENATE TAXATION COMMITTEE

49th Legislative Session -- 1985

Date

January 30

Location -- Room 413-415

Name

Present

Absent

Excused

Senator Brown		✓	
Senator Eck	✓		
Senator Goodover	✓		
Senator Hager	✓		
Senator Halligan	✓		
Senator Hirsch	✓		
Senator Lybeck	✓		
Senator Mazurek	✓		
Senator McCallum	✓		
Senator Neuman	✓		
Senator Severson	✓		
Senator Towe	✓		

References

SB-64

VISITORS' REGISTER

[illegible]

(Please leave prepared statement with Secretary)

NAME Clayton Bain BILL NO. HB 88

ADDRESS Helena DATE 1-30-85

WHOM DO YOU REPRESENT Board of Crime Control

SUPPORT ☒ OPPOSE ☐ AMEND ☐

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Comments:



502 South 19th

Bozeman, Montana 59715

Phone (406) 587-3153

TESTIMONY BY: Alan Eck

BILL # SB #64 DATE 1/30/85

SUPPORT XXX OPPOSE

Mr. Chairman and members of the committee; for the record my name is Alan Eck. I'm representing the Montana Farm Bureau. We would like to go on record as supporting Senate Bill #64. We feel this bill takes into consideration the fact that farm dwellings are a different kind of property than urban or suburban homes and the bill makes allowances for this with regards to property taxes. We ask that the committee give Senate Bill #64 a "do pass" recommendation. Thank You.

Exhibit 1 - SB 64
January 30, 1985
Senate Taxation Committee

Alan Eck
SIGNED

SENATE BILL 48

Revision of Property Tax Classification System

PURPOSE

Senate Bill 48 attempts to do several things. First, it simplifies the property tax classification system reducing from 22 to 11 the number of classes of property subject to property tax.

Second, it defines commercial property and places all personal property into the same class. This is beneficial for two reasons. First, it enables us to comply with the federal law prohibiting the taxation of railroad and airline property at any higher rate than all other commercial property in the state. Second, it eliminates future lawsuits by persons who may contend that their property is taxed at a higher rate than other property when there is no justification for any distinction between the two kinds of property.

Third, Senate Bill 48 is intended to equalize and make the property tax system more fair, thereby eliminating the potential for costly and time consuming lawsuits in the future.

FISCAL IMPACT

Senate Bill 48 is not intended to have any impact on anyone's taxes--with the possible exception of the Burlington Northern Railroad, who will receive a gigantic tax break if the bill is not passed. Inevitably, however, with this major change in the classification system there will be some adjustments. The subcommittee and interim committee did a marvelous job keeping these adjustments to a minimum. Whenever any major impact was required, the adjustment is downward to reduce taxes for a particular group rather than upward. For example, agricultural equipment will go from 11% to 11.1%; most heavy vehicles will be reduced from 16% to 11.7%; electrical operating property will increase from 12% to 12.8%; and telephone operating property will decrease from 15% to 12.8%. (It is pretty hard to justify taxing Mountain Bell's telephone operating equipment at a higher rate than Montana Power Company's electrical operating equipment.)

The bill will raise \$2.5 million additional revenue from the railroads for local governments (\$650,000 of which will come to the state in the University levy and Foundation Program). Otherwise, as amended, the bill will have only minimal effect on revenues.

SEPARATION OF COMMERCIAL AND RESIDENTIAL REAL ESTATE

The interim committee supported the bill unanimously, with one exception. The Democrats and Republicans disagreed on the separation of commercial real estate and residential real estate into two separate classes. Republicans argued that keeping the residential property in the same class of commercial property would act as a check or brake on increasing taxes--legislators would be less inclined to increase the tax if it affected residential property as well as commercial property. Democrats argued the reverse--that legislators would be less inclined to increase residential property taxes if commercial property will similarly increase.

Unfortunately, however, we cannot afford the luxury of either argument. Failure to separate the two categories of real property would require either (1) re-appraising all residential property as well as commercial property each year (in order to make it comparable to railroad property which is already re-appraised each year) at a minimum cost of about four million dollars in the next biennium; or (2) allow railroads a 2.3 million dollar break in property taxes. With the tight financial picture this session, we simply cannot afford the luxury of combining the two categories of property for philosophical reasons. Further, by retaining the two categories of real property tax in the same classification we are almost certain to have a repeat of the 34% cases that plagued the courts and tax collections during the last re-appraisal cycle.

HB 240 BY REPRESENTATIVE RAMIREZ

The only difference between Senate Bill 48 and the bill introduced by Representative Ramirez (HB 240) is the separation of these two categories of real property. The re-appraisal adjustment to allow for reduction of the classification numbers to conform to the new values resulting from re-appraisal were included in HB 240 as originally prepared and are being added to Senate Bill 48. These are necessary to prevent a 100% increase in nearly everyone's property tax as a result of the re-appraisal that will take effect January 1, 1986.

AMENDMENTS

Additionally, both bills originally contained (1) a provision for separating farm residences to allow taxation on a market value rather than reproduction value; (2) a provision for use of retail value instead of wholesale value; and (3) a requirement that replacement value depreciated be used instead of original cost. All three of these items have been removed from Senate Bill 48 and probably will be removed from HB 240. While the initial attempt of these provisions to equalize and make the system more fair is laudable, they do constitute substantive changes, which the committees wanted to avoid as much as possible.

CONCLUSION

As anyone familiar with our property tax system can attest, we have been plagued with numerous lawsuits for many years. Some of these lawsuits have tied up millions of dollars, making them unavailable for use by local governments. The result has been that the rest of us are required to make up the difference--largely through assessment on residential homes or agricultural land. With Senate Bill 48 (or HB 240) we should avoid most of these lawsuits in the future. Without either bill, we will embark on at least five more years of constant and expensive litigation.

THOMAS E. TOWE
Senator-District 46

TET/jim

Estimated as of 1/21/85

At the request of the Senate Taxation Committee, the Department of Revenue attempted to estimate the effect of reappraisal on residential real property and improvements and commercial real property and improvements.

CONCERNS

1. This estimate was not constructed in a statistically valid fashion, was not tested for statistical validity and should not be considered to be statistically valid.
2. The estimates presented are general in nature and produced to provide the committee a general idea of what is expected. It should not be construed, in any way, to infer a relationship between certain types of properties in certain locations.
3. The estimates were arrived at by reviewing information contained in the computer on 80,549 residential properties out of a statewide total of 283,763 properties and 9154 commercial properties of a statewide total of 42,195 properties. That information was cross checked with each of the Department's 8 Area Appraisal Managers to see if it was consistent with their experience. No other tests were done.
4. Land values were set based on actual sales information. Structure values have not yet been compared to actual sales (estimated completion of that phase is August 1985). When that comparison is completed the estimates provided may change.
5. In summary, our best estimate at this time, not adjusted for sales information except on land values, would be:

Residential improvements and land
Weighted average increase 119%
from 1972 to January 1, 1982

Commercial improvements and land
Weighted average increase 93%
from 1976 to January 1, 1982

No estimate is available for January 1, 1986
value for commercial property.

Using the formula contained in SB-48, as amended, the derived tax rate for residential real property and improvements would be:
3.897%

Similarly, the derived tax rate for commercial real property and improvements would be: 4.428%