

MINUTES OF THE MEETING
TAXATION SUBCOMMITTEE
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SPECIAL SESSION III

June 12, 1986

The meeting of the Revenue Estimating Subcommittee was called to order by Chairman John Harp on June 12, 1986, at 8:30 a.m. in Room 312-3 of the State Capitol.

ROLL CALL: All members were present. Also present were Terry W. Johnson of the Office of Budget and Program Planning (OBPP), Judy Curtis Waldron of the Legislative Fiscal Analyst's Office, (LFA), Nancy Nicholson, Governor's Revenue Estimating Advisory Council (REAC) and Dave Bohyer, Staff Researcher from the Legislative Council.

Tape 1:A:000

Nancy Nicholson said that the Governor's Council met May 19 and 20, 1986 and held two days of informational hearings with industry represented along with representatives of the Legislative Fiscal Analyst's Office, the Office of Budget and Program Planning, Shell Oil, the Montana Petroleum Association, Montana Coal Council, Montana Mining Association, MSU Agricultural Department, Montana Wood Products, University of Montana, plus many other persons from state agencies.

The Council decided to focus on the status quo at the time and said it was not their function to look at "what if" situations. The Council came up with approximately a \$5 million difference in the investment and interest account because of legislative action in this session. Income tax returns were coming in at that time and Terry Johnson was able to tell the Council that returns were going to be lower than previously and they took that into account.

Rep. Harp asked Ms. Nicholson to explain how they arrived at the additional 9.7 and 6.1 in audit collections that was to come into the corporate income tax portion. She replied they went primarily from information that they had at that time and said that Terry Johnson would provide more information on that subject as their information has changed since the date of the meeting.

Dave Hunter, Director, Office of Budget and Program Planning (091) gave a more in-depth overview of the Council and said that the estimates before the Committee were the Executive revenue estimates. He explained that there are two revenue estimates in the Governor's Budget instead of one; the current law revenue estimate that is the estimate of the Council and the Governor's policy recommendations segregated from that. He said the Legislature and the State should work towards a common format for economic assumptions so the Governor's Office, the LFA and members of the public who testify

are working on the same format. These offices, in the past, have built assumptions on different bases such as calendar and fiscal years.

At this point in the meeting, Terry Johnson and Judy Waldron were asked to come before the Committee to give their corresponding revenue estimates as requested by Chairman Harp.

(191) Chairman Harp asked Maxine Johnson of the Bureau of Business Research of the University of Montana to come before the Committee. She passed out Exhibit #1, attached to the minutes, which was prepared for the Governor's Council. She said they felt that personal income would continue to lag behind the U.S. over the next two or three years. Their forecast was made within the framework of the U.S. economic outlook prepared by Wharton Econometrics which states that there is no recession in sight between now and 1988 and that there will be a modest economic growth this year, accelerate in 1987 and slow down in 1988. They used a low interest rate and a low inflation rate. They assumed that exports would become more attractive and no rebound in oil prices before 1988. They then made some important assumptions for the state of Montana which are shown on the first page of Exhibit #1. She felt that their projections were a little high and they would be revising them shortly but it would be after the special session.

In answer to a question from Rep. Sands, she replied that there were two revenue estimates; one from the Governor's budget office and their own and said that the Governor's estimates were lower than theirs and suggested that they be used instead of hers.

Rep. Harrington asked how they decided that Montana Resources was not going to open. She said that they came to that conclusion because they had no evidence otherwise. He also asked if they had changed their predictions in view of the recent hirings by Montana Resources. She said that they had not and were in the process of revising these estimates.

Rep. Switzer asked if they used the government agricultural payments as part of the estimation for agricultural economy and if they did how it was figured for 1987. She said that the farm labor income does include the government payments. Rep. Switzer said he understood 1986 is a year of increase in subsidies and 1987 is supposed to be a year of decreases. She said she would defer agricultural income projections to Bruce Beattie of the Department of Ag Economics from MSU.

Bruce Beattie, MSU, Department of Ag Economics, (277) said that in 1986 there would be some weakening in the realized price of wheat and some of the deficiency payment would not be realized until 1987.

Chairman Harp asked if coal production was going to be pretty stagnant through 1986-87 but she said there was some small increase in coal production predicted by the industry but also a possibility of some losses. The new air standards in Minnesota may have an effect on the coal production in Montana.

Inflation Rate (323)

Terry Johnson said the indices they used to estimate the revenues were forecast by Wharton Econometrics and the main one of the CPI (Consumer Price Index) is the one that the income tax rate is adjusted for terms of tax indexing so that is the more critical one. They forecast for 1986 that the growth in the CPI would be 1.5% and 2.7% in CY87. Those were supplied by Wharton in April and since that time the May forecast is a little bit higher. He also said they use the national CPI rate for income tax indexing.

Chairman Harp asked if the change in the May forecast was because of oil prices. Mr. Johnson said that was so and that Wharton had an inflation rate as low as 1% a couple months ago but since that time they have increased the forecast and energy is definitely an important part of the CPI.

Judy Waldron said the LFA used the CPI for forecasting the individual income tax collections. For June 1986 they had an increase over June 1985 of 1.1% and 2.9% increase of 1987 over 1986.

Interest Rates (437)

She explained that the interest rates they were using for short term rates for FY86 was 7.7% and 7.1% for FY87. They have 9 months of actual data for the 1986 rates so they only had to forecast for the remaining 3-4 months of the year. She said they had the same rates for FY87. She said another place where interest rates fit in is the coal trust fund and the interest rate earned on that is mostly deposited in the general fund. That would be long-term interest rates and corporate bonds are added to that account. For those long-term rates they used 10.7% for 1986 and 9.25% for 1987.

Mr. Johnson said their rates were 7.8% in 1986 and 7% in 1987. Again, for long term rates, they approached it the same way; used the forecast supplied by Wharton, take about five different long-term rates that they forecast and computed an average on those. They approached the long-term forecasts on a calendar year basis so the numbers were not quite comparable. In CY86 they forecast 9.68% and 9.72% for CY87 and that would be the interest rates on the new investments that would be made so any investments that are currently tied up would be at something different than that.

Rep. Sands asked if they could extrapolate from fiscal year to calendar year for a comparison figure. Ms. Waldron said they were forecasting interest rates on a fiscal year basis. Mr. Johnson calculated that his calendar year rates would be 10.48% for FY86 and 9.7% in FY87. His short-term rates were figured on a fiscal year basis.

Jim Howeth, Board of Investments (551) said that forecasting interest rates is nothing more than a guessing game. He said that the reason the interest rates have declined so dramatically is because inflation is low and right now interest rates are basically tied to the rate of inflation. He said it is also apparent that the inflation rate has been tied to the price of oil. He said if the price of oil was known the inflation rate may be determined and then it would be known where interest rates were going to go. He said that interest rates should remain pretty stable over the next year and guessed that short-term rates would fluctuate between 6-7% and long-term rates 9-10%. He said that interest rates are still historically high but the way the system is built the rates would probably remain at historical levels. He didn't anticipate that inflation was going to go away and that higher interest rates would return someday. He said that if oil prices could go down they could also go back up. OPEC still controls 70% of the world's known oil reserves so it's only a matter of time.

Chairman Harp stated that it appears the inflation rate is going to start going up in the next 5-6 months and possibly a slight increase in oil prices; wouldn't that also reflect in the interest rates? Mr. Howeth felt that the reason for the lag in interest rates would be probably due to the poor economic conditions of the nation and worldwide.

Tape 2:A:000

Personal Income (010)

Terry Johnson said that the OBPP was forecasting \$9.2 billion in 1986 and \$10 billion in 1987 and those forecasts were adopted by the REAC. Their forecast for CY87 was actually slightly less than that. They were comfortable with the 1986 numbers but they felt it would grow at a more normal rate in 1987. Their forecast from 1985 to 1986 is about 3.8% and from 1986 to 1987 8.6% growth.

Ms. Waldron said they used Montana non-farm labor income rather than total personal income and felt it was a better predictor of the adjusted gross income. Their growth rate for CY86 was 1.9% and 3.7% for 1997.

Rep. Sands stated that Mr. Johnson was talking about a 8.6% growth from 1986 to 1987 and an inflation rate of 2.7% or a real growth of almost 6% and asked if that wasn't totally contrary to the 15 year trend in Montana. Mr. Johnson said it was definitely not contrary to the trend as there had been as high as 18% growth during good agricultural years.

Phil Brooks, State Economist, Department of Commerce (110) said that the Federal Reserve uses the method of what he called historical statistical procedure. They don't apply any state's economy to any national variables. They just look at the history of a particular income variable and do it in a very sophisticated way but the future is not always a replication of the past. One of the strengths of their methodology is because they work with historical data, then they can come out with an idea of the air-bound on their forecast which is a very important thing and in terms of the most recent copy of the forecast from the Federal Reserve, the variable non-farm labor income, they forecast a 1% real growth adjusted for inflation for 1986 and the air-bound -- they talked about a range of as high as 7% plus or 8% negative. It is difficult to forecast for Montana because it is relatively small and relatively unstable. He said if he had to pick numbers he would recommend the numbers that the Council has recommended for 1986.

Mr. Brooks said that 1974-1979 was a period of strong growth and 1979-1984 was just the opposite. 1980, 1981 and 1982 were periods of recession and income went down. 1983 and 1984 were recovery years, 1985 - not all the data is available but it appears there was a slight recession in 1985.

Business Income (250)

Judy Waldron said that in forecasting corporation taxes they look at what is happening to U.S. corporate profits. For FY86 those taxes are pretty much in - they expect essentially no change in profits between the CY85 level and what is projected for CY86 - that profits will remain essentially flat and corporate tax projections vary between 1986 and 1987 for other factors and that is the one time payment from Montana Power and secondly, the audit revenue that is coming into the department. They expect the revenue from audits will decline from \$9 million to \$5 million. These two items are what is driving the corporate income tax projections down.

Terry Johnson said they approached the corporation taxes in a similar way. They anticipated about a 5.7% decline from FY85 to FY86 and about a 3.5% decline from 1986 to 1987. Also included in the FY86 forecast is \$7.6 million due to the Colstrip IV sale and the audit collections of \$9.7 million and then dropping to \$6.1 million in 1987. The \$9.7 is a number they felt fairly comfortable with and for 1987 the Department also felt comfortable with the \$6.1 million.

Rep. Sands asked why corporation taxes decline substantially at the same time that personal income taxes rise substantially. Mr. Johnson said that with lower oil prices and lower interest rates that does have a stimulus effect on the economy and that will generate more personal income at some point in time. The unemployed will come back into the work force because of the stimulus of lower interest rates and lower oil prices. One group that might be affected by that would be the trucking industry as far as lower fuel prices which would be a positive flow for corporation tax.

Rep. Switzer asked Mr. Johnson for more information on the sale of Colstrip IV. Mr. Johnson told the Committee that the Colstrip IV sale took place on December 31, 1985 so because that was the end of CY85, the corporation reports on a calendar year basis, but that had an impact on FY86 revenues - that was a one time revenue gain that was received in FY86 and that will never show up again. This was fully paid at the time and there were no payments. The sale amounted to \$292 million.

Chairman Harp said that Montana Power is operating the plant for the purchaser and sometime down the road they may be able to purchase the plant but that was the only way for the Power Company to alleviate themselves from that cost because they knew they would never come under the PSC rate base.

Rep. Sands stated that the net effect is the difference between the LFA and the OBPP figures in terms of dollars. Ms. Waldron said that it shows the corporation license tax for 1987 biennium a difference of about \$3.5 million - the LFA is lower. There is also a difference of \$27 million this year and lower by \$735,000 in 1987. She said their revenue forecast for this year is based on 11 months of actual tax collections.

Mr. Johnson said that after a conversation with the department of revenue as of June 12, 1986 it indicates that there may be \$1.5-\$2 million that may be received by June 30, 1986. Even if they get the \$1.5 by the end of this year their forecast for FY86 is probably too high. He said they would be something higher than the LFA but lower than the \$36 million.

Kathy Shenkle, Research Bureau, Department of Labor and Industry (Tape III:B:004) said that in Montana certain employers have to pay unemployment insurance on their employees which is called covered employment. She said that they have one program that collects data for these covered employers in the state of Montana. Because that data is not readily available on a current basis, they have a sample that estimates employment until that data does become available. They survey businesses to find out what their employment levels are, what their average weekly hours and average weekly wages are. In addition to that there is a national program called Current Population Survey that goes around and does a household survey in all states. When they forecast employment in the state of Montana they base it on total non-agricultural employment. From 1984 to 1990 they are projecting an employment increase of 1.1% per year. The Federal Reserve was projecting a 4% estimate a year ago. She said that 1.1% in Montana is not a good growth rate.

Rep. Harrington said that Montana Resources will be employing 350 people by August 1, 1986 and asked if that fell into her projected increase. She replied that they have tried to allow for some of those things happening. She said there has been no large increase in employment, only a slight decrease in unemployment.

Rep. Williams asked about the people that have fallen through the

cracks and are not on the unemployment rolls. She said that those people are tracked through the household surveys. There are also people that have quit looking for work and they cannot be counted. She said the procedure is based on a formula mandated by law to be used in all states.

The population estimate from the Bureau of Census shows Montana still growing, however, the 1985 figures that came out said that the national migration figures for the state of Montana is now zero. Mr. Brooks said the population for 1985 was 826,000 and in 1984 it was 823,000.

Mr. Johnson said he did not have the percentage increase but did have the raw numbers in terms of non-ag employment: 1980, 280.4; 1981, 281.8; 1982, 273.7; 1983, 276; 1984, 281.1 and 1985, 278.4. Those figures exclude all non-ag plus self-employed plus military.

Bruce Beattie, Montana State University, (240) said they expect the price of wheat to be the same as it has been with a target price of \$4.38 per bushel. The farmers won't get the full deficiency payment in 1986; some of it will come in 1987. The new farm bill is two phase. They projected a realized price in 1986 of \$3.93. He also said that 93% is under the program in Montana. There is a much more favorable barley program in the new farm bill and projected the barley price in 1986 and 1987 at \$2.30 and \$2.60 respectively compared to \$2.39 in 1984 and \$2.15 in 1985. Feeder calves should average \$60-62 for steers and heifers and at one time he felt there might be a slight increase but was not sure of that at this time. He said that the difference between the price paid and the futures market is staying farther apart than before. He thought the price might be \$62-63 but it could be a little higher and in 1987 it may be \$65. The number of cattle has been decreased and it is the bottom of the cattle cycle. He felt that lambs and hogs would continue about where they are.

Rep. Schye questioned if the wheat prices were considering the Gramm-Rudman cuts but Mr. Beattie said that most of the program is exempt from the Gramm-Rudman act. He said he was very nervous about what might happen in the future because they are projecting market price to drop from about \$3.40 per bushel down to about \$2.55 for 1986 and 1987 which means the government will be picking up a bigger share of the \$4.38 and that means there will be a higher cost to the farm program in 1986 and 1987 than what was anticipated.

Rep. Williams asked if they had taken into consideration the production levels. The Crop and Livestock Reporting Service is predicting some good crops. The average yield per acre through 1985 is: 1980, 23.5; 1981, 29.17; 1982, 33.6; 1983, 31; 1984, 22.6 and 1985, 12.7 average.

The Committee recessed at 10:35 a.m.

The hearing resumed at 10:55 a.m.

Tape 2:B:000

The Committee reviewed the previously heard estimates and then went on to the other items on the agenda as follows.

EXECUTIVE ACTION (015)

Inflation Rate: The OBPP was at 1.5 for 1986 and 2.7 for 1987; the LFA was at 1.1 for 1986 and 2.9 for 1987.

Rep. Sands moved to accept the figures of the LFA as noted above. Further discussion was held. The question was called and the MOTION PASSED, with Rep. Pavlovich not present to vote.

Interest Rates: Chairman Harp stated to the Committee that he did not think they could ignore the figures of the board of investments. The board predicted 6-7% for short-term for FY86 and also FY87; the long-term rates are 9-10% for 1986 and 1987. The average from July through April (actual figures) was at 7.9% and that has dropped down to about 7.1%. That is from the board of investments' report. Mr. Johnson of OBPP said they were forecasting 7% for 1987.

Rep. Schye moved to accept the figures of the OBPP for interest rates for short-term and long-term. Discussion was held on the motion. Rep. Switzer said he would like to go with Mr. Howeth's figures which are a known number. Rep. Schye stated that the OBPP for long-term is between 9-10% and that is right in the middle of all the figures uplied to the Committee. Chairman Harp shared the view with Rep. Switzer for long-term money at 10.4% or a little under 10. He suggested that the motion be separated into the two separate rates. Rep. Schye withdrew his original motion.

Rep. Williams moved to accept the OBPP figures of 7.86 for FY86 for short-term. The motion PASSED with Reps. Switzer and Sands voting "no".

Rep. Williams moved to accept the OBPP figures of 7% for short-term rates for FY87. Rep. Harrington said he thought if the price of oil escalates this figure would be low but Mr. Johnson said it would be some time before interest rates would respond to an increased oil price. Rep. Sands also pointed out to the Committee that the motion was at the very high range of the board of investments' recommendation for 1987 and accepted that they were substantially higher for 1986. Chairman Harp agreed with that statement but said that in 1986 they had 9 months of data on which to base the decision so he felt very comfortable with that figure. The motion PASSED unanimously.

The Committee then considered the long-term rates. The LFA was 10.7 for 1986 and 9.25 for 1987. The OBPP was 10.48 and 9.7.

Rep. Sands moved to accept for 1986 long-term rates the figure of 10%. The motion PASSED unanimously.

Rep. Williams moved that the Committee accept 10% for 1987 for long-term rates. The motion FAILED with Reps. Switzer, Sands and Harp voting "no".

Rep. Schye moved to accept 9.8% for 1987 for long-term rates. The motion PASSED with Reps. Switzer and Sands voting "no".

Personal Income: The OBPP had an increase of 3.8 and the LFA of 1.9 for 1986. One is figured on non-farm income and the other is figured on total personal income so it is hard to compare those and that is the reason for the disparity.

Mr. Johnson said the OBPP figures for growth rate are 3.8 and 8.6 which are Montana numbers but are derived from national statistics. Chairman Harp stated that with the figure of 8.6 for 1987 they were contemplating that the agricultural community was bouncing back and that money was being filtered through non-farm income and that was the reason for the 8.6 growth in personal income. Mr. Johnson pointed out that the 1987 income has a very small effect on FY87 receipts - the key year is CY96 personal income as CY85 generated revenue for FY86, etc. From CY85 to CY86 there was a 1.5% growth in total personal income. The 3.8% they are projecting is actually lower than historical levels.

Phil Brooks (376) said that one is forecasting a recession in 1986 and the other is predicting slow growth.

Rep. Schye moved to accept the increase of 1.9% of the LFA for CY86. The motion PASSED unanimously.

Rep. Sands moved to accept the LFA figure of 3.7% for 1987. The chairman brought out the disparity which is the non-farm labor income and total personal income. The LFA said they have a 5.5% growth and the OBPP has 6.2% so the difference in the growth rate isn't that big. Rep. Sands said it was \$2 million big.

Further discussion was held on the personal income tax. Judy Waldron explained how they came up with the non-farm labor income figure of 3.7%. Chairman Harp stated that when they accepted that figure that is what they agreed on.

Business Income: Chairman Harp stated that both the LFA and the OBPP were looking at declines and asked if there was some current information for 1986. Judy Waldron said that as of June 11, 1986 the general fund portion of the corporation license tax was \$33.2 million and there may be some more audit collections coming in. She referred the Committee to Table V of the handout attached to the minutes and said that these figures are going to change and they will have to be looked at again.

Mr. Johnson said their total involved in the audits was \$9.7 million - \$6.1 in 1987. Judy Waldron said they looked at actual collections through the end of May but didn't have the breakdown of how much of that came from the audits and how much from somewhere else but their number would probably be a little lower than 9.7. The figures at the present are not dollar figures but assumptions and the assumption was that the OBPP had a decline of 5.7 in 1986 and 3.5 in 1987. Ms. Waldron said this was a case where they did not use the same variables.

Rep. Williams moved to accept the figures of the OBPP but following more detailed discussion with Mr. Johnson Rep. Williams withdrew his motion. Chairman Harp stated that they would take up the dollar amounts and assumptions following the lunch recess.

REVENUE SOURCES: (086) Janelle Fallan, Montana Petroleum Association had talked to people from Shell Oil since they produce one-quarter of the oil in the state. (See Exhibit #2) The safest figure is \$15 per barrel through CY87. Currently, world excess is about 3 million barrels per day and the current price for west Texas crude is about \$12.55. The Montana posted price runs \$1-1.50 lower than that. The July futures price for west Texas crude is \$12.57.

Chairman Harp asked Miss Fallan if they had seen another drop in oil recently. She replied that it had been as low as \$9.50 per barrel in March. The west Texas price was \$15 two weeks ago but it had dropped off again. They see a greater decline in production and in 1987 a substantial decline. She said that even if the price of oil came back it would be a couple years before the state would recover from this. She also said that there are wells that are being shut down rather than being repaired. Leases on state, federal and private lands were discussed. Rep. Switzer asked if they anticipated 1988 production to have as significant a drop as 1986-87. Miss Fallan said that at \$15 per barrel production could drop further.

Jerome Anderson, Shell Oil Company (138) said that the only increase for coming years would be an inflationary increase. Fifteen dollar oil is not attractive as far as exploration is concerned. This has to be back in the \$20 range. Fifteen dollars was suggested as the projected barrel price for 1986 and 1987.

Chairman Harp stated that based on the Governor's REAC the forecast for production is 28.4 million barrels in CY86 and 26.7 million in CY87. Terry Johnson said the figure presented to the REAC was 28.1 and the Council adopted 28.4 million barrels.

Miss Fallan then moved on to natural gas and said their estimate was 2.10/mcf which is lower than the LFA.

Rep. Sands asked Judy Waldron what their reason was for projecting \$25 for oil for 1986. She stated that was for FY86 and the severance tax is based on fiscal years. Chairman Harp mentioned that those figures are deceiving.

Chairman Harp told the Committee that the fiscal year and calendar year figures will have to be discussed. When talking about ending fund balances it gets to be very confusing. Mr. Johnson said that in terms of forecasting oil severance tax they need a fiscal year average price and production but they felt that in terms of industry people, in most cases, they speak in calendar years so they opted to present their numbers in that way so they would be comparable to industry and converted the calendar year numbers to fiscal numbers.

COAL SEVERANCE TAX: 3:B:000 Jim Mockler, Montana Coal Council said that the figures for production are for calendar years. For 1986 the production estimates are: Decker Coal, 12.6 million tons; Spring Creek Coal, 3.2; Westmoreland, 217; Western Energy, 10.6; Peabody Coal, 3.1 and Knife River, .2. He also stated that Westmoreland's is being paid under protest because of the lawsuit of the Crow Indian Tribe. The total tonnage is 29.7 without Westmoreland. 27 1/2 million ton of that is taxed at 30% and 2.2 million at 20%. This projection is 2.3 million tons less than the Governor's office less than 30 days ago. Mr. Mockler said he did not expect much improvement - probably look for 1 1/2 million ton increase if we get the market back that he was predicting as early as May 19th. That figure should be 36 million tons. At a minimum it should go back to last year's which was a total of 34.685. The total projection should be 34.7 million, including Westmoreland.

Chairman Harp asked Mr. Mockler why the decline since May and he said that some of the coal does not meet the new air standards in Minnesota so they are buying Wyoming coal, there has been a tremendous influx of Canadian and BPA hydropower. He said they also lost 1 1/2 million tons to oil and California would rather fire up their oil generators than buy our coal. Mr. Mockler felt that the LFA's figure of 8.46 was probably pretty close. Decker coal is a little higher priced and felt it would be relatively stable after this. Mr. Mockler said that the projected total for 1986 is 32.4 with Westmoreland and without Westmoreland it is 29.7.

Rep. Sands said that the Council assumed that the coal would be taxed through 1987, however, Mr. Mockler pointed out that the Crow Indian suit is in the 9th Circuit Court of Appeals. So, the figures that should be used from Mr. Mockler are 29.7 and 31.7.

Mr. Johnson explained that the entire amount was taken out for Westmoreland, however, there is about 30% that they are paying taxes on - 30% that is not in dispute and this depends if it is produced on private land or state or federal land.

Mr. Johnson said that for 1985 the protested portion of Westmoreland's production was 1.97 million tons and non-protested portion was 1.1 million tons. He also said there was some underlying decrease that they were unaware of. Mr. Mockler felt that Westmoreland's production estimate was high. Mr. Mockler will provide the secretary with written testimony. (Exhibit #5)

Metal Mines Tax: (188) Gary Langley, Executive Director of Montana Mining Association, handed out a copy of his letter to the Governor's Council on Revenue Estimating, Exhibit #3 attached, and went through the major points of the letter.

Mr. Langley said that Montana Resources was not having trouble getting financing but had other major hurdles to overcome, however, they do hope to open this year. They have not decided on their smelter location and have looked at Japan, some European countries as well as U.S. cities.

The Committee recessed for lunch at 12:30 p.m. and will resume the meeting at 1:45 p.m.

(LUNCH RECESS)

The Committee reconvened at 1:45 p.m.

Ms. Waldron informed Chairman Harp that she and Mr. Johnson had not had the opportunity to give their figures on the oil tax.

Ms. Waldron said from calendar year 1985 they have actual data on what production was and what the average price was so they forecast for just the last quarter of that year. They showed a production decline of 3% and an average price of a little over \$24. That's because for the first three quarters they had the actual price. The production decline was based on the three quarters of data that they had. Next year they expect production to fall more, there may be some shutdowns of wells, cut back in exploration and development and they will use the \$15 price per barrel.

Mr. Johnson said that over the years the general trend has been a 1.1% decline in oil production. Rep. Williams asked Mr. Johnson if the \$16.50 would be a relatively secure number for 1987. He said that he had forecast \$14.97 in 1987 but the Governor's Council opted for a higher number.

Oil Production: Rep. Williams moved to accept the oil production figures of the OBPP of 28.4 for 1986 and 26.7 for 1987. MOTION CARRIED UNANIMOUSLY.

Rep. Switzer moved to set the oil price at \$15 per barrel for both 1986 and 1987. MOTION CARRIED UNANIMOUSLY.

Natural Gas: Chairman Harp said that the natural gas is such a small item and asked for the wishes of the Committee.

Rep. Schye moved to accept the OBPP figures for price and production of natural gas. MOTION CARRIED UNANIMOUSLY.

Coal Severance Tax: Chairman Harp stated that some additional information was received from industry at the meeting that the OBPP and LFA did not have and that was that there was a reduction of some 2 million tons of coal being processed in the state. He felt that there was no choice but to take industry at their word. The figure for 1986 was 29.7 not including Westmoreland.

Rep. Sands moved that the Committee accept the figures of 30.5 million tons. That includes the 30% of Westmoreland that is not protested. MOTION CARRIED UNANIMOUSLY.

Rep. Schye moved to accept the price of \$8.46 per ton for coal for FY87. MOTION CARRIED UNANIMOUSLY.

Metal Mines Tax: Rep. Sands moved to accept the LFA figures for 1986 and 1987 but following further discussion the motion was withdrawn.

Rep. Williams said that the figures for FY86 are known numbers but moved to accept the figure of 9.69 of the OBPP for FY87. MOTION CARRIED UNANIMOUSLY.

Interest on Investments: (535) Chairman Harp stated that some of the interest rates that have been assumed should not have to be discussed again at this time. The availability of cash for investment purposes will vary on what the deficit will be or on what the ending balance will be. There is a policy decision where we will increase the \$50 million anticipation notes up to \$75-100 million as far as the transfers go. That is another policy decision that has to be made. Those are a couple of assumptions that have been separated from the Governor's Council.

Mr. Johnson said that in terms of the treasury cash account - the pool of all state funds - some accounts such as the highway gas tax account, that are designated to receive their own investment earnings, these are not included in the treasury cash account. Presently, that money stays in that earmarked account. That is another policy decision that has to be made to allow that money to go into the general fund. Mr. Johnson said that for FY86 - this is current law - the projection is that the average daily balance will be \$166.5 million. FY87 the Governor's Council felt comfortable with making the assumption that the deficit and the problems that are present now would not be acted upon by the Legislature so the average daily cash balance would drop to \$100 million for FY87 and in addition to that we are assuming that \$46 million in tax anticipation notes would be sold in FY86 - that's

a known figure. For 1987 they assumed they'd sell \$50 million under current law.

Ms. Waldron said that for FY86 they showed \$163.4 million and that was based on 9 months of actual data. In FY87 they assumed there would be some action to balance the budget but even so the cash balance available for investment would fall somewhat but not as much as what the Governor's Council determined. The LFA had an average fund balance, without tax anticipation notes, of \$152.4 million.

Chairman Harp said that the Committee should discuss the responsibility of balancing the budget and that they have to assume, in this scenario, that they would have to use the \$150 million figure because that is the issue to be addressed.

The executive forecast is \$1 million. The LFA forecasts \$5 million. Chairman Harp wondered if the OBPP and LFA shouldn't agree on that figure. Mr. Johnson said the Council looked at the average daily balance and based on what the Legislature does, the average daily balance would be \$150-160 million. They chose to assume what would happen if the Legislature did not act. Rep. Williams thought the Committee should accept the \$100 million and then that could be changed later, if necessary.

Chairman Harp mentioned the Governor's resolution on revenue which was not admitted because it was considered as being outside the call, however, he said this would have to go to the rules committee to get the resolution introduced. Mr. Johnson said that all of the policy issues are at the end. Chairman Harp said maybe that would be the way to proceed - put the lower figure in there might be the way to go.

Rep. Schye moved to accept the OBPP's figures for availability for interest on investments and that reflects current policy.
MOTION CARRIED UNANIMOUSLY.

Mr. Johnson asked if the Committee wanted to adopt the assumption on the tax anticipation notes at the \$50 million. Chairman Harp said that he did and that he was not ready to say that they wanted to expand that to \$75 million because that is a major policy issue.

Rep. Williams asked if there must be a motion on that but the chairman said they had assumed they were not going to anticipate that additional dollars when they reflected the \$100 million in 1987.

Rep. Sands asked Mr. Johnson to explain tax and revenue anticipation notes. Mr. Johnson said that under federal regulations state governments are allowed to go out and borrow money on short-term basis to meet cash flow needs. If the state can actually justify a negative cash balance during any point during the year then they can go out and issue these tax and revenue anticipation notes and

and the rule is they can issue up to the deficit for any given month plus the next month's expenditures. They actually do a cash flow on the general fund to determine when the deficit is going to be, which is usually in March.

Coal Trust Interest: Madalyn Quinlan, Legislative Fiscal Analyst, said that an additional factor is that some bonds are being called back since interest rates have dropped. Mr. Johnson agreed that one item that has an impact is the bond calls and so far in 1986 those are much higher than anticipated. They had no idea how long this trend was going to go on but if interest rates go back up there won't be as many. Potentially, there is a lot of bonds that could be called. Mr. Johnson said that with the assumption for lower interest rates they could assume that bond calls may continue for awhile.

The LFA projected 6.37 million in bond calls for FY87. She used a figure of 3.2 for 1986 but they are already 1.5 million above that. There is a 30 day notice requirement for bond calls so there shouldn't be any more before the end of June. The OBPP estimated 1.5 million for 1986. Rep. Sands asked for the best figure for 1986. Mr. Johnson said it would almost be easier to make an estimate of the total interest earnings from the trust account. Rep. Sands asked if it was the only thing they had to do for 1987 - estimate the bond calls. The OBPP figure for 1987 for bond calls is 5.6 for the general fund portion. 85% of the interest earnings from the permanent trust goes to the general fund so the total estimate for bond calls is 6.6 million for 1987 (OBPP).

Rep. Switzer asked when they would run into the lower priced bonds. Mr. Johnson said they still have bonds that are earning 15-16%. The board of investments indicated they think this situation will go on for quite some time but the impact will be in 1988-89.

Rep. Sands moved to adopt the 5.4 figure of the LFA for coal tax interest. MOTION CARRIED UNANIMOUSLY.

Individual Income Tax: (455) Mr. Johnson stated that they work with total personal income. They take that and relate it to the Montana adjusted gross income. Once they arrive at a tax liability number for the calendar year then they have to make adjustments and from there it is converted to a fiscal year number.

The LFA went with actual figures for 11 months for 1986 for audits and tax credits. 1987 was a forecast. The two projections, LFA and OBPP, are not comparable because of the non-farm labor income and total personal income. Ms. Waldron added 2.8 million for the audits for 1987. Mr. Johnson said they used 1.2 million. Again, it is hard to be comparable. It is hard to distinguish between audit collections or regular tax receipts as they come in.

Corporate Income Tax: Mr. Johnson said they derive the figure by taking the forecast of national profits, oil prices and interest rates supplied by Wharton and derive a Montana corporate taxable

income. Based on those variables that's how they came up with 5.7% decline in the corporate taxable income. The corporate tax division believed there would be between 1.5 and 2 million coming in between now and the end of June but that still doesn't bring the receipts up to the level that he forecast.

Chairman Harp stated that they were forecasting \$36 million and said that it may be below that by 1.5-2 million so that would be \$1 million above the LFA. Chairman Harp asked what effect the \$2 million would have. Mr. Johnson said the 5.7% is a projected decline in taxable income, not actual tax dollars. He said his guess would be 6 1/2 to 7%.

Chairman Harp said there is a \$1 million difference approximately but Mr. Johnson said it was not unusual to receive between 1 1/2 and 2 million during the month of June. Chairman Harp said it could be changed if the figures changed dramatically.

The OBPP shows a figure of between 6 and 6 1/2% for a decline of the corporate taxes and a further decline of 3 1/2% for 1987 and a dollar figure of \$34.5 million for 1986 but for 1987 the figures would have to be reduced. Chairman Harp said if there is a \$2 million or \$1.5 million decline in actual dollars being collected he said it would have to be reflected in the assumptions.

Rep. Sands moved to accept the estimate of corporate license tax for 1986 of \$34 million. MOTION CARRIED.

Rep. Williams moved to accept the estimate of \$28 million for corporate license tax for 1987. MOTION CARRIED with Rep. Sands voting "no".

(220) Chairman Harp called on Tucker Hill, Montana Wood Products, before going on to Long Range Bond Excess.

Mr. Hill said that with falling interest rates the housing starts have reached historic highs and Montana producers have benefited from that. The forest receipts off public land was about \$5.9 million for FY86 and that went to about 34 counties but he did not know what the breakdown was as to what went to the foundation program. The one thing to affect that in the future would be the recommended harvest levels on forest lands. The average for Montana was about 584 million board feet from 1974-1983. This has dropped about 47 million board feet. He said they also see a loss in job security because of this in western Montana and for every million board feet there is about seven direct jobs lost in the industry. With 47 million board feet they see about 320-330 jobs being lost in western Montana. Something else that affects the Montana industry which is beyond control is the level of Canadian exports coming into the U.S. This year that has been in excess of 1/3 of the market which is a dramatic increase. He did not see any great growth but some stabilization. Six mills have gone out of business, four of them because of supply problems,

since 1978.

Recess at 3:40 p.m.

Committee resumed at 3:50 p.m.

Tape IV:2:000

Long Range Bond Excess: Ms. Waldron said that the money that goes into the debt service account is 11% of personal and corporate taxes, 79.7% of the cigarette tax and all the tobacco products tax which is all available for transfer to the general fund because the debt service is paid from the general fund appropriation. The cigarette tax is a flat rate per pack and there has been a 2 1/2% decline in each of 1986 and 1987.

Mr. Johnson said they assumed 82.6 million packs for 1986 and 79.7 million for 1987.

Jerome Anderson, Tobacco Institute, said their forecast was a little different than the OBPP and the LFA. His figures for 1985-86 through March was a 5.01 decline. The LFA figures are through April. He said that 80% goes to fund the long range building program. As the taxes increase the sales have decreased which will eventually affect the long range building program. He said the Governor's Council took the figure of 3.6 which was kind of middle ground.

Mr. Anderson said they were talking about 83 million packs this year and 81 million next year. He said that the model used by the Tobacco Institute did project that the economy would be better than it is and the population growth would be better. That does affect the sales. The LFA estimated 81.4 for 1987 and 83.5 for 1986. The OBPP had 83.1 for FY87 but no 1986 figures.

Rep. Sands moved to accept the figures of the OBPP. MOTION CARRIED.

The tobacco products assumption will be the same.

Telephone Tax: Tom McCree, Mountain Bell, said that the revenue will pretty much remain the same. He said he did not see any real growth. Rep. Williams moved to accept the figures of 3.241 for 1986 and 3.419 for 1987. MOTION CARRIED.

Electrical Energy Tax: Following discussion Rep. Williams moved to adopt the figures of the OBPP of 2,547,000 for 1987. MOTION CARRIED.

Freight Tax: Mr. Johnson said they had an actual number for 1986 but there would be a 4.5% increase above the 1986 level. Chairman Harp brought out that there was quite a difference between the OBPP

and the LFA. The reason for the drop in revenue between 1985 and 1986 was because of the problems in agriculture.

Rep. Schye moved to accept the figures of the LFA of 1,448,000 for 1987. There are no 1986 figures. MOTION CARRIED.

Drivers License Revenue: Mr. Johnson will prepare a spread sheet for the Committee to make it easier to see what has been done during the day.

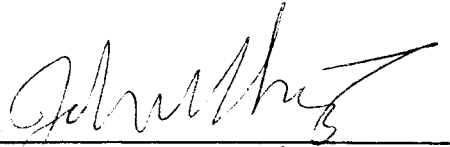
Ms. Waldron said that this includes new license fees, motorcycle endorsements, lost license fee, etc., and they looked at year to date revenues and said the revenue this year would hold about constant with revenues last year so for four years in a row it is about \$800,000.

Mr. Johnson said that even though it is a small source, the data that goes into it is difficult to get a handle on. He said they relied quite heavily on what they have seen so far this year and as of June 12, 1986, they had \$707,000 in the general fund and that compared to their estimate of about \$768,000 so he didn't feel very confident that they were going to get much above that. These figures relate to the population growth and the net migration that is taking place in Montana.

Rep. Sands moved to accept the OBPP figures for 1986 and 1987 for the driver's license revenue. MOTION CARRIED.

Chairman Harp scheduled the meeting for 7:00 a.m., June 13, 1986, and the school foundation program will be first on the agenda.

The meeting was adjourned at 4:30 p.m.



REP. JOHN HARP, Chairman