MINUTES OF THE MEETING
TAXATION COMMITTEES
MONTANA STATE SENATE AND
HOUSE OF REPRESENTATIVES

January 19, 1987

The first joint meeting of the Taxation Committees of the House of Representatives and Senate was called to order at 7:15 P.M. on January 19, 1987 by Senator George McCallum in Room 325 of the State Capitol.

ROLL CALL: See attached roll call sheets from the Senate Taxation Committee and the House Taxation Committee.

Chairman McCallum called the hearing to order and advised that the House of Representatives was still in session and the Representatives would join the hearing as soon as possible. He reviewed some of the tax measures before the legislature and advised that this is the reason we wanted some public input on the taxation question in the state. He opened the hearing for comments from the public.

Dr. Maxine Johnson, Director, Bureau of Business and Economic Research, University of Montana, presented the committee with her comments concerning Montana's tax system. Her written statement is attached as Exhibit 1.

Terry Anderson, Professor of Economics, Montana State University, presented comments to the committee and a pamphlet entitled "Montana Economy: Reality and Perceptions". His written statement and pamphlet are attached as Exhibit 2.

Bruce R. Beattie gave information to the committee concerning tax reform. His written statement is attached as Exhibit 3.

Marilyn Wessel, President's Office, Montana State University, representing the steering committee from the Montana State University and University of Montana people who put together the conference "Taxation and the Montana Economy", wanted the committee to be aware of information that came out of the conference that was available to members of this committee. She listed the following information that would be available to the legislators or their constituents: pamphlets entitled "Trends in Montana Economy and Taxation", "Taxation and Revenue

Systems in Montana" and "Taxation and the Montana Economy"; and video tapes of the entire conference, of the "Impact of Taxation on the Business Climate in Montana" and a presentation that was done with public and private sector panelists who struggled to design a new tax system for a mythical state.

The Representatives from the House Taxation Committee arrived at the hearing.

Tom Markle, representing the Montana Forward Coalition, appeared to introduce the Coalition's findings and recommendations of a research study conducted by them. He said we began first by identifying serious disincentives of business development in Montana and then selected the most serious disincentives for problem solving debate. We overwhelmingly concluded that Montana's tax system was not: balanced, broadly based, equitable, and simple. What it really does do is provide some revenue. In early 1986, the Coalition commissioned Miller and Associates of Olympia, Washington, to pursue an examination of Montana's economy, our tax system and governmental expenditures. Wally Miller of that firm, the former Budget Director of the state of Washington, will present a consensus of that effort. Mr. Miller was commissioned to analyze taxes and expenditures, to compare Montana taxes, to identify problems and to give us our alternatives to offset revenue losses where appropriate and to develop specific recommendations from which to draft legislation. In November, the Montana Forward Coalition adopted, for consideration and debate, a comprehensive tax reform package. This package was presented to the Governor. Our proposals differ significantly from the Governor's proposal in that we have targeted personal property tax relief as a major concern.

Wally Miller, Miller Associates, reviewed the report with the committee. See attached Exhibit 4.

George Anderson, Co-Chairman of MONTREC, CPA, Helena, presented testimony to the committee and a consensus of his testimony is attached as Exhibit 5.

Al Donahue, founding member of MONTREC, gave testimony which is attached as Exhibit 6.

Conrad Stroebe, member of the Billings High School Board, gave testimony which is attached as Exhibit 7.

Jim Murry, Executive Secretary of the Montana State AFL-CIO, gave testimony which is attached as Exhibit 8.

Dennis Burr, representing the Montana Taxpayers Assn., gave testimony to the committee. The property taxes are too high and the distribution of property taxes paid is inequitable. In 1985, if Montana had the average tax system of the 50 states, we would have collected $194 million less in property tax than we actually collected in 1985. In 1985, if Montana had the average tax system of the 11 western states, we would have collected $220 million less in property tax dollars than we collected. Our taxes are not only high but the distribution is inequitable. Over the last ten years, we have shifted the burden of property tax away from real estate and onto the personal property. The personal property in this state generally represents production taxes. At the present time our taxes on personal property are three or four times as high as they are in real estate and improvements. Ten years ago they were approximately the same. In the same period, because we have taken the increase, as a result of reappraisal, out of the tax base, we have caused the mill levies which are levied by local governments to increase dramatically. The average mill levies in the largest counties ten years ago was 288 mills; this past year, 1985, the average was 405 mills. He does not think a sales tax is really the answer. He said for Mountain Bell the average property tax per $1,000 of investment in plants in Montana is $32.15. The average for the 7 states that company operates in is $15.44. Our property tax on that particular company, which is in a classification similar to personal property at 12%, is double the average of the seven states that company operates in. Total taxes per $1,000 of plant investment, this includes sales tax in states that have it, brings Montana's tax up to $41.89 and brings the seven state average up to $22.97. So, by including all other taxes, besides property taxes, and including sales taxes, we increase the average of the seven states by $7 and increase the taxes in Montana by $9. Our recommendation to this legislature is that you decrease personal property taxes to the level of 4%. There have been recommendations that personal property taxes be eliminated completely but the Taxpayers Association does not feel that is necessary. In the property tax area there are a couple of serious problems that will have to be faced. One is that we are losing a good percentage of the tax base in the next year. In 1985 the gross value per barrel of oil was $25.00 and the deductions amounted to $9.43 per barrel. In 1986, the price per barrel averaged between $13 and $14 per barrel and he would assume the deductions would remain about the same. So we are looking at probably 60 or 70 percent of the net proceeds base will be gone and that represents around 10% of the total property tax base that will be gone next year. We are facing a declining property tax base at a time when we have to consider property tax relief. In relation to I-105, what makes sense to them is the proposals that suggest exempting a certain amount of the appraised value of property from taxation and extending that consideration to all class four property. The Taxpayers Association is in support of the elimination of the unitary method of taxation for corporations. One of the proposals that have been discussed is to simply put into law what the Department of Revenue currently does and that would take away the disincentive of foreign companies to operate in Montana. He thinks the legislature should go one step further and treat domestic corporations in the same favorable light as they would treat foreign corporations. Montana is pricing itself out of the market in production of natural resources. A recent study in California on oil taxes shows that Montana had the highest oil taxes of the nine states studied. In fact, the taxes in Montana were 200% higher than the taxes in California on oil. We know that the coal tax is double that of Wyoming and the hard rock mining taxes are also high in Montana. In relation to replacing tax revenue, he said he did not think you gain very much if you replace a tax with another tax, particularly if the burden is born by the same person. If everything has been done to cut the budget and there is still a deficit, then the logical answer is a sales tax. The Taxpayers Association would support a sales tax if you would first look at balancing the Montana tax structure, look at reducing expenditures where you can and then if you need additional revenue, as well as revenue for tax relief, then they would support this legislature in that decision.

Robert N. Helding, representing the Make Montana Competitive Committee, gave testimony which is attached as Exhibit 9.

Joe Brand, State Director, United Transportation Union, and also on behalf of the Brotherhood of Weigh Employees, Brotherhood of Railway and Airline Clerks, and the Brotherhood of Locomotive Engineers, gave testimony to the committee. He said the only thing discussed at their meetings was the sales tax and his remarks will be directed to a sales tax. They are opposed to a general sales tax as they say it is regressive. When other states have imposed a sales tax eventually it increases. Corporations and others are given exemption and the counties and cities are allowed to implement an additional sales tax. There is no end to it.

Gary Carlson, Montana Society of Certified Public Accountants, offered a resolution to the Committee on Exhibit 10.

Forrest "Buck" Boles, President, Montana Chamber of Commerce, said production in the state has been taxed too much, for too long, and that the Committee would have the support of the Montana Chamber of Commerce in its tax reform efforts.

Ken Peres, Economist, Montana Alliance of Progressive Policy, advised that the 1983 Legislature stressed economic development. He said new industry credit was obtained by Sunshine Mine, and that Burlington Northern experienced a $39 million tax reduction as a result of its suit with DOR.

Mr. Peres stated that only 13% of firms, responding to an Alliance survey, said low taxes were a favorable point of consideration and, therefore, he assumed that Montana Inventory Tax Credit had no effect either way. Mr. Peres explained that state and local taxes comprise about 2-4% of taxes paid overall. He commented that, in his opinion, business tax incentives don't work and can be detrimental to long-term econonic growth.

Gary Zurry, Columbia Falls Aluminum Company, read from a prepared statement, Exhibit 11, in support of the bill. He said CFAC received a $2.4 million tax bill in 1986, as a result of a $198 million appraisal, although Company was purchased for $1 from ARCO. He said CFAC pays 2.5 times more per year in taxes than do aluminum-producing plants in Washington state, which are not subject to corporation taxes. Mr. Zurry went on to explain that he believes such a fixed tax is wrong for Montana, and said the state is ignorant of the aluminum business.

Mr. Zurry advised he sees problems with the unitary tax, used only by Montana and three other states; that corporation taxes are too high; and that incentives for new business are restrictive. He suggested that the Legislature reduce spending, live within its budget, and become competitive with neighboring states.

Mr. Zurry said CFAC is operating at only 64% of its capacity, right now, and that employees took a 15% wage cut to keep the plant in operation.

Eric Feaver, President, Montana Education Association, said the state is too dependent upon property and resource development taxes. He advised he would support a comprehensive tax system, which is universal, balanced, and revenue-producing, adding that he believes corporate tax rates should be reduced and the unitary tax, replaced. Mr. Feaver said the oil severance tax should be adjusted and the tax on new oil and coal production, reduced to 20%.

He commented that MEA does not support a referendum as late as 1988, but does support a sales tax out of the best interests for education, along with property tax relief and broadening of the tax base. Mr. Feaver summarized that MEA would support necessary and progressive taxation for education and public service.

Janelle Fallan, Executive Director, Montana Petroleum Association, submitted written testimony in support of a sales tax, Exhibit 12. She added that new proposals would be brought before both the House and Senate Taxation Committees. Ms. Fallan said that in 1985, almost all legislators regarded coal legislation favorably, and thanked those present for their support.

Richard Barrett, Professor of Economics, University of Montana, and member of the Governor's Economic Development Council, stated there is much mixed evidence on capital formation, allowing loopholes to eventually sneak into tax law. He said that has much to do with economic development in the state, which he believes is developing rapidly. Mr. Barrett said new kinds of economic activity are creating new jobs, which need a tax system that treats all taxpayers equally.

Ed Sheehy, Association of Retired Federal Employees, explained that service jobs are growing rapidly across the nation, and that Montana needs to capitalize on this source of outside income (retirees), who come to the state because there is no sales tax.

Barbara Archer, Women's Lobbyist Fund, told committee members she represented 39 organizations and over 6,500 women in the state. She advised the Committee that one of five children is poor, and one of two female heads-of-household are poor. Ms. Archer explained that one of three women are the sole income earner in their household, earning 53 cents to every dollar earned by men. She added that the median income for women in Montana is $4,931 annually.

Ms. Archer requested that guidelines be considered in developing a new tax structure, and said that one-fourth of Montana taxpayers earning more than $120,000 annually, pay no income tax in the state. She stated that taxes need to be sufficient to create revenue to fund state services, and at the same time, need to be fair. Ms. Archer commented that because one-half of the population in the state is female, the need for an enlightened economic policy is increased.

Mike Micone, Executive Director, Montana Environmental Trade Association, read from Exhibit #13 in support of the bill. He stated he believes the state cannot continue to provide all levels of services, currently being provided. Mr. Micone asked if the state really needed 600 elected officials, 6 separate university systems, and 500 school districts.

Sam Ryan, Montana Senior Citizens Association, told the committee he opposed a sales tax, and had voted for I-105. He suggested that the committee close loopholes in the inventory tax, as a positive alternative.

Tom Markle, Billings attorney, said he believes the only way to turn the state around is with the tax reform proposed by the Montana Forward Coalition Reformation Report.

Chet Kinsey, Montana Farmers Union, said farmers will end up being the new tax sources, through the sales tax, and reaffirmed his opposition to implementation of a sales tax.

Earl Riley, Montana Senior Citizens, stated his opposition to a sales tax, because of its effect on retired persons with fixed incomes.

Rep. Tom Asay, read Exhibit #14, from the Crow Tribal Council, explaining tribal views of tax reform.

The conference sponsored by Montana Council on Economic Education and Center for Political Economy and Natural Resources, University of Montana, furnished the committee with a pamphlet entitled "Rethinking Montana's Tax System", attached as Exhibit #15.

ADJOURNMENT: There being no further business before the Committee, the meeting adjourned at 10:50 P.M.

George McCallum

SENATOR GEORGE McCALLUM, Chairman

ROLL CALL

TAXATION (SENATE) COMMITTEE

50th LEGISLATIVE SESSION -- 1987 Date 1-19-87

NAME	PRESENT	ABSENT	EXCUSED
SENATOR CRIPPEN	✓		
SENATOR NEUMAN	✓		
SENATOR SEVERSON	✓		
SENATOR LYBECK	✓		
SENATOR HAGER			✓
SENATOR MAZUREK	✓		
SENATOR ECK	✓		
SENATOR BROWN	✓		
SENATOR HIRSCH	✓		
SENATOR BISHOP	✓		
SENATOR HALLIGAN, VICE CHAIRMAN	✓		
SENATOR McCALLUM, CHAIRMAN	✓		

Each day attach to minutes.

DAILY ROLL CALL

HOUSE TAXATION COMMITTEE

50th LEGISLATIVE SESSION -- 1987

Date Jan 19, 1987

NAME	PRESENT	ABSENT	EXCUSED
REP. RAMIREZ	✓		
REP. ASAY	✓		
REP. ELLISON	✓		
REP. GILBERT	✓		
REP. HANSON	✓		
REP. HARP		✓	
REP. HARRINGTON		✓	✓
REP. HOFFMAN	✓		
REP. KEENAN	✓		
REP. KOEHNKE	✓		
REP. PATTERSON	✓		
REP. RANEY	✓		
REP. REAM	✓		
REP. SANDS	✓		
REP. SCHYE	✓		
REP. WILLIAMS		✓	

CS-30

DATE 1-19-87

COMMITTEE ON Taxation

VISITORS' REGISTER

NAME	REPRESENTING	BILL #	Check One: Support	Check One: Oppose
Ben Stuhlman	Helena MT			
Larry F. Johnson X	Jordahl + Sliter			
Mike Hillard	Mt Soc of CPAs			
Jane Campbell	" " " "			
Janelle Fallan X	Mont Petroleum Assoc			
Alve Thomas	Retired Teachers			
Jim Mockler	MT. Coal Council			
Carol Mosher	Mt. Cattle Women			
Eric Feaver X	Mont Educ Assoc			
Larry Dahlmeier	Save Our State, Inc.			
Thomas B. Boyd X	Poke-A-Pack			
Barbara Archer	Women's Lobbyist Fund			
Roger Mlyn	Helena			✓
Wendy Fulbright	" "			✓
Ted J. Doney	ASARCO; MT. Dairymen's Assn.			
Gary Sumney X	Columbia Falls Aluminum Co.			
Lorna Frank	Mt. Farm Bureau			
Richard Barrett X	—			
Lloyd D. Anderson	Montrec			
Al Donohue X	Montrec			
KEN PERES X	Montana Alliance			
Judith H. Carlson	Mt Ch NASW			
Earl Reilly	M.S.C.A.			
Pat Haugland	MT Society of CPAs			
Steve Hedges	Columbia Falls Aluminum Co.			
Alan Nicholson	Helena - MONTREK			

(Please leave prepared statement with S...

DATE 1-19-87

COMMITTEE ON TAXATION

VISITORS' REGISTER

NAME	REPRESENTING	BILL #	Check One: Support	Check One: Oppose
Dennis BURR	MONTANA TAXPAYERS ASSOCIATION			
~~[illegible]~~	~~Self~~			
TOM MARKLE out	Montana Forward Coalition			
GORDON MORRIS X	Mont. Assoc. Counties			
BOB HELDING	Mont. Competitive Comm			
X MAXINE JOHNSON	UM Bureau of Bus Research			
X Terry L. Anderson	Montana St. U.			
F.H. BUCK BOLES X	MONTANA CHAMBER			
Myles J. Watts	Mont State U			
Bruce R. Beattie	Mont. State Univ (Ag Econ & Econ)			
Terry Minow out	Montana Fed Teachers			
GARY B. CARLSON X	MT Society of CPA'S			
Ed Sheehy X	RETIRED FEDERAL EMPLOYEES			
Don Ryan X	M.S.C.A.			
~~Thomas Schneider~~	~~MPEA~~			
~~Alec Hansen~~	~~League of Cities~~			
Joe Brand X	United Transportation Union			
Bill [illegible]	[illegible]			
[illegible] X	Helena, MT Policemakers			✓
[illegible]	Helena Mont Policemen			✓
Pershing Carter	MSCA			
DeLoris Carter	MSCA			
Wally Miller	Miller & Assoc. Inc.			
Mary L. Craig	Equity In Taxation			
John Ortwein	MT Catholic Conference			
Bill [illegible]	HELENA MONT			✓

(Please leave prepared statement with ...

DATE 1-19-87

COMMITTEE ON Taxation

VISITORS' REGISTER

NAME	REPRESENTING	BILL #	Check One Support	Oppose
[illegible]	Mont. Assoc. of Churches	— no	testimony	
Sue Fifield	Montana Low Income Coal.			
Mike [illegible]	WETA			
Doug Campbell	Montana Senior Citizens Assn.			
Cort Harrington	Montana County Treasurers Ass.			
Mons Teigen	Mt. ~~Stock~~growers Assn			
[illegible]	MLIC			
Terry Murphy	Mt. Farmers Union			
Jim Murry	Mt. State AFL-CIO			
Claudia Clifford	United Food & Commercial Workers			
[illegible]	Mt. Chamber of Commerce			

(Please leave prepared statement with Secretary)

Maxine C. Johnson, Director
Bureau of Business and Economic Research
University of Montana

January 19, 1987

Mr. Chairman, I have some general comments on Montana's tax system. In particular, I would like to make three points:

1. Montana's tax structure is out of balance and overly dependent upon production taxes, especially on natural resource industries.

2. On the average, taxes paid by Montana individuals and households are not high compared to those paid by residents of other states.

3. Resource industries make up an important part of Montana's economic base. The heavy tax burden they carry may put them at a competitive disadvantage in world and national markets.

First, Montana's tax structure: Our state derives a larger proportion of total tax revenue from business and industry than most other states. The Montana Economic Development Project report, prepared with the assistance of McKinsey & Co., classified 35 percent of total state tax collections in Montana in 1980 as taxes on production. That compared to proportions ranging from 6 to 29 percent in six neighboring states (North and South Dakota, Colorado, Wyoming, Utah, and Idaho). Taxes included were corporate income taxes, severance and producer taxes, utility and insurance company taxes.

SENATE TAXATION / House Taxation
EXHIBIT NO. 1
DATE 1-19-87
~~BILL NO.~~ Joint Hearing

When severance taxes were excluded, Montana still ranked number one, with 17 percent of total tax collections classified as production taxes, compared to 2 to 13 percent in the other states.

The second point I would make is that, as a consequence of the heavy dependence on resource taxes, Montana individuals and families do not pay high taxes compared to residents of other states.

When all state and local tax collections were combined, Montana ranked 23rd in tax revenue per capita and 9th in tax revenue as a percentage of personal income in 1984. But when severance taxes were subtracted from the figures for all states, Montana ranked 32nd in tax revenue per capita and 26th in tax revenue as a percentage of income.

These two comparisons make an important point. Severance taxes are mostly exported; they are paid by consumers in other states. Many other business taxes (but not all) may be passed on by Montana businesses to Montana consumers. But, even if Montana businesses succeeded in passing all their taxes except severance taxes on to Montana consumers, per capita taxes on individuals would not be out of line with other states. The comparison would likely be even more favorable if data were available to exclude proceeds taxes, also generally conceded to be exported to out-of-state consumers.

Let me also speak to property taxes. Property taxes are higher in Montana. In 1984, we ranked 9th in property tax revenue per capita and 2nd in property tax revenue as a percentage of personal income. But most property taxes are paid by business (including agriculture) or by the mining industry in the form of proceeds taxes. In 1984, the effective property tax rate on single family homes with an

~~SENATE~~ House ~~[redacted]~~ TAXATION

EXHIBIT NO. 1

DATE 1-19-87

FHA mortgage in Montana was 1.14 percent. The U.S. average was 1.23 percent, ranking us 20th among the 44 states included in the report.

A recent study by the government of the District of Columbia compared total tax burdens of income, property, sales and use, automobile, and gasoline taxes on representative families in the largest city of each state. The results show the state and local tax burden for a Billings family ranging from 5.8 percent at the lowest income level ($15,000) to 7.8 at the top ($75,000). Among the states, Montana ranked from 41st at the lower income level to 34th at the highest.

While none of these studies is the definitive word on Montana's tax structure, I think the evidence is clear that our system places very heavy dependence on production or business taxes, especially on resource industries, and that consumers are not overtaxed. I'd like to speak to the impact of this imbalance on the state economy.

One consequence is abundantly clear: ad valorem tax collections based on mineral production and price are subject to large fluctuations. But of greater importance is the fact that Montana's resource industries make up a large part of its economic base. As basic industries selling their product out-of-state, they are largely responsible for the overall performance of the Montana economy. We are going to be dependent upon them for the foreseeable future. They have a lot of problems, many not unique to Montana. But other problems are unique--among them distance from markets and, in some instances, higher extraction costs due to the nature of the resource. If our tax policies make it even more difficult for our basic industries to compete in world and national markets or to maintain their production in Montana, then that should concern us all.

In the short-run, taxes on resource industries may be exported but over the long-run these taxes may affect the survival of these industries and the economic welfare of all Montanans.

Changes in State and Local Tax Collections
Per Capita, Montana, Fiscal Years 1969-1984
(In 1985 Dollars)

	1969	1984	Change Amount	Change Percent
All taxes	$955	$1,313	$358	38
Property	529	607	78	15
Gross & net proceeds	26[a]	116	90	346
Other property taxes	503	491	-12	-2
Income	154	257	103	67
Severance	16	181	165	1,031
Other	256	269	13	5
Total, less severance and proceeds taxes	913	1,016	103	11

Sources: U.S. Bureau of the Census, Governmental Finances, 1968-69 and 1983-84, and Montana Department of Revenue.

[a]Fiscal 1970 figure.

State and Local Tax Revenue Per Capita
and as a Percentage of Income, Fiscal Year 1984

	Tax Revenues per Capita		Tax Revenue as a Percentage of Personal Income	
	Amount	Rank[a]	Percent	Rank[a]
U.S. Average	$1,356	---	11.7	--
Idaho	953	47	10.1	43
Montana	1,275	23	12.9	9
North Dakota	1,334	20	11.5	24
Wyoming	2,504	2	20.9	2
Less severance taxes:				
Montana	1,099	32	11.1	26

Source: Advisory Commission on Intergovernmental Relations, Significant Features of Fiscal Federalism, 1985-86 Edition.

[a]Among 50 states and the District of Columbia.

State and Local Tax Burdens, Representative
Billings Families, 1984

Gross Income	Taxes as a Percentage of Income
$15,000	5.8
25,000	6.3
35,000	7.0
50,000	7.6
75,000	7.8

Source: Government of the District of Columbia, Tax Rates and Tax Burdens in the District of Columbia: A Nationwide Comparison, June 1985. Taken from Montana Cooperative Extension Service, Trends in the Montana Economy and Taxation, Bulletin 1343, September 1986.

THE MONTANA ECONOMY: REALITY AND PERCEPTIONS

by

Michael Reilly
James W. Robinson
and
John C. Rogers

Foreword
by
Terry L. Anderson

SENATE TAXATION / House
EXHIBIT NO. 2
DATE 1-19-87
BILL NO. Joint Hearing

MONTANA'S TAX SYSTEM:
PERCEPTIONS AND REALITIES*

by

Terry L. Anderson**

When President Reagan took office in 1980, he popularized the notion of supply-side economics. Backed by people like David Stockman, Jack Kemp, Paul Craig Roberts, and Arthur Laffer, the administration pursued the policy of reducing taxes in the interest of stimulating productivity. There were two key components of the supply-side theory. First, it was argued that reducing tax rates would actually increase tax revenues because the overall size of the economic pie would be larger. This, in turn, it was argued, would help balance the budget. Secondly, it was argued that incentives matter and that incentives are largely determined by the tax structure.

Though the supply siders were far too optimistic in their prediction about how tax cuts would help raise revenues to balance the budget in a short time, their emphasis on incentives has changed the way we think about taxes. In a sense, this emphasis was nothing more than traditional economic analysis which focused on taxes rather than prices, wages, or production costs. Picking up on this emphasis, economists have begun to provide the empirical tests of the supply-side theory.

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*Prepared at the request of the House and Senate Taxation Committee. These comments do not necessarily represent the views of Montana State University or its Department of Agricultural Economics & Economics.

**Professor of Economics, Montana State University, and Executive Director of the Montana Council on Economic Education.

House/SENATE TAXATION
EXHIBIT NO. 2
DATE 1-19-87
~~BILL NO.~~ Joint Hearing

In 1986 the Montana Council on Economic Education sponsored two programs dealing with Montana's economy and its tax system. One of these resulted in a paper entitled "The Montana Economy: Reality and Perceptions," by Michael Reilly, James W. Robinson, and John C. Rogers. The other program entitled "Rethinking Montana's Tax System: Possibilities for Reform," was a conference which brought together a group of economists on May 2, 1986, to focus on the potential impact of tax reform on incentives. In addition to these programs, the University of Montana and Montana State University co-sponsored a seminar entitled "Taxation and the Montana Economy," on September 5-6, 1986. Output from these three programs should provide the legislature with considerable guidance in considering tax reform.

Perceptions of Business People

The study by Reilly, Robinson, and Rogers obtained perceptions of business people regarding the importance of various factors on location and expansion by using a survey prepared by the Federal Reserve Bank of Kansas City. Reilly, et al. surveyed 475 firms in the states of Idaho, Montana, North Dakota, South Dakota, Wyoming, Colorado, and Utah. Of the 180 responses, 106 came from Montana and 74 from out-of-state. Some of the results of their survey follow:

(1) When asked to rank the importance of factors in the business climate influencing a firm's decision to locate, non-Montana respondents ranked labor force availability, labor costs, state regulatory policies, state and local property taxes, and union strength as the top five in descending order. For Montana residents, labor costs, state and local property taxes, union

House / SENATE TAXATION
EXHIBIT NO. 2
DATE 1-19-87

strength, state regulatory policies, and transportation costs were the top five factors.

(2) Unfortunately, the attitudes of out-of-state respondents regarding these locational factors show that Montana is not perceived as an attractive business location. Of all respondents, 48% said that state and local property taxes were a barrier to business; 45% said transportation costs; 43% said union strength; 41% said state regulatory policies; and 29% said state corporate income taxes. It is important to note that of the five factors ranked as most important for location decisions, three are found in the top five factors ranked as barriers to business in Montana.

(3) When asked to rank the seven states on a scale of 1 to 7 (1 being highest) with respect to its potential attractiveness for relocation or expansion, Montana's ranking was 3.67. Only two states, South Dakota and North Dakota, received lower scores.

(4) Reilly et al. asked several open-ended questions.

(a) When asked, "What can state government do to make a given state more attractive to businesses like yours?" 43% said minimize taxes or offer tax incentives.

(b) When asked, "As it is currently managed, what is the single most attractive aspect of the State of Montana as a location for your business?" quality of life, natural resources, and labor costs ranked the highest. More telling, however, is the fact that 60% of the out-of-state respondents were unable to think of a single attractive aspect of Montana!

House/SENATE TAXATION
EXHIBIT NO. 2
DATE 1-19-87
BILL NO. Joint Hearing

(c) When asked, "What is the single most negative aspect of Montana as a location for your business?" tax burden and anti-business climate received the top votes.

What is evident from these open-ended questions is that Montana is attractive on dimensions that are not particularly important to business location decisions and unattractive on those factors which are important. When asked, "What change in legislative/regulatory policy would increase the attractiveness of Montana as a location for your business?" 26% responded with reduce taxes or offer incentives. Less regulation, pro-business climate, and implementation of a sales tax in place of other taxes each received 8% of the responses. In short, if we wish to make Montana an attractive place for business location expansion, legislature must consider tax reform which will change business perceptions about our state.

Rethinking Montana's Tax System

The conference sponsored by the Montana Council on Economic Education on May 2, 1986, included papers by several economists from around the country. Paper topics included income taxes, general business taxes, severance taxes, unitary taxation, and sales tax regressivity. Since the papers did not deal specifically with Montana, they do not provide exact policy implications for tax reform.

The papers investigated the influence of various taxes, but of course, no author suggested that only taxes matter. Economic analysis tells us that if everything else remained constant and the price of the commodity increased, less of that commodity would be consumed. When

House / SENATE TAXATION
EXHIBIT NO. 2
DATE 1-19-87

other things are allowed to vary, the impact of a price change may be dwarfed by these other variables. Similar results can be expected from tax changes. If a severance tax on coal is reduced, economic analysis would predict a greater extraction of coal. However, if at the same time the price of oil falls, the impact of the severance tax change may be dwarfed. Therefore, it is important in studying taxes to consider other variables which may also be influencing economic incentives and activity.

Following is a brief summary of the papers presented at the tax conference sponsored by the Montana Council on Economic Education:

(1) One obvious area of taxation, where incentives matter, is the area of income taxes. As Richard Stroup and James Gwartney point out, workers are influenced by their rate of take-home pay. As taxes rise, this rate of take-home pay declines. For a person already paying a high tax rate, this means that a one-percent change in the tax rate "reduces the take-home pay from a dollar of income by a larger percentage than it does for a person in a lower tax bracket" (Stroup and Gwartney, p. 6).

Such reasoning has prompted economists to consider the Laffer curve described by Stroup and Gwartney. This curve suggests that reducing very high tax rates will actually increase tax revenues, and increasing low tax rates will do the same. Stroup and Gwartney present evidence for the 1920s and 1960s consistent with this theory. Similar evidence for the recent tax cuts is now available. The 1981 tax cut was described as a windfall for the rich because it cut the top rate by 28%. But, the result was that the share of

House/ SENATE TAXATION
EXHIBIT NO. 2
DATE 1-19-87
BILL NO. Joint Hearing

taxes from the top bracket actually increased (see Wall Street Journal, Tuesday, May 6, 1986). Compared to predictions, which ignored the incentive effects of tax rates, reported income from the top taxpayers was actually 20% more than it would have been with no tax cut. As a result of the tax cut, $600 million more in taxes was paid by people in this top bracket. Lawrence Lindsey reported in the Wall Street Journal that "the results suggest that for every 10% increase in the share of his income he is allowed to keep, the taxpayer reported 7.5% more income." Since the across-the-board cuts gave the top rate payers a bigger percentage increase in take-home pay from an additional dollar earned, it is not surprising that their tax payments and their share of taxes increased. It should be emphasized, however, that many other variables also were changing and could have affected reported income. Unfortunately, the necessary statistical work to sort these out has not been done.

(2) The paper by Ronald Johnson (based on a study with former MSU professor, Bruce Benson) suggests that taxes also make a difference for capital investment. First, he asks why many surveys of business conclude that taxes do not matter. The main reason is that, across states, tax competition occurred, evening the overall burden of taxes. By way of analogy, if all grocery stores charged the same price for food and consumers were asked whether food prices determined where they shop, they would most likely say "no." If businesses face the same general tax rate across states, taxes will not be an important variable to them. However, tax rates do

SENATE TAXATION
EXHIBIT NO. 2
DATE 1-19-87

vary from time to time and Johnson was able to measure relative tax changes between states. He found that if a state's tax rate increased by 1% relative to other states, capital investment by business would decrease by 1.02%. However, not surprisingly, he found that there is a lag between the time when taxes change and when the influence on capital investment is felt. "The major portion of the long-run effect of relative tax changes occurs within 4 to 5 years of the change" (Johnson, p. 10).

(3) Robert Deacon presented findings that severance taxes do influence the rate of crude oil and natural gas exploitation. He also found that there is a lagged impact of changes in severance taxes. Examining California, where there is a 6% severance tax on oil and gas, Deacon found that a 1% change in the tax would reduce the number of wells drilled by 1.17%. For Montana, the effect of our severance tax is much higher because a net proceeds tax of 15-20% and a corporate income tax of 6.75% must be added to the severance tax on oil of 5.5%. "When combined, the total levy is large in comparison to that found in any other state, even including Alaska" (Deacon, p. 2).

At the conference on "Taxation and the Montana Economy" co-sponsored by the University of Montana and Montana State University, Rodney Smith examined the state taxation of oil and gas. He found that "Montana levies severe taxation on its oil and gas industry. The high rate of taxation results from the <u>combination</u> of taxes, rather than the level of any specific tax -- Montana virtually stands alone in the severity of its taxation"

House/SENATE TAXATION
EXHIBIT NO. 2
DATE 1-19-87
BILL NO.

(p. 20). According to Professor Smith, this high level of taxation cannot be justified by the claim that resource taxes can be exported to out-of-state consumers or by the necessity for impact payments for public services. Underlying his analysis is the fact that the demand for Montana's energy resources has become more price sensitive with time. When our 30% severance tax was imposed in the 1970s, consumers and producers had not yet adjusted to high energy prices. Now, however, both demand and supply have become more price responsive. As a result, the possibility of "exporting" our severance tax has diminished.

(4) The question of the impact of unitary taxation on business was addressed by Charles E. McLure, Jr., former Deputy Assistant Secretary of the Treasury. In his presentation, Professor McLure emphasized that, with unitary taxation, the effective tax rate on corporations is a function of the statutory corporate tax rate and the profit rate of a corporation in locations outside the state. McLure pointed out that, in the absence of unitary taxation, corporations might be able to avoid corporate income taxes. But, he emphasized that a "water's edge" system of unitary taxation is preferable to worldwide unitary taxation. Professor McLure concludes that the most important implication of his analysis "is that the corporation income tax is an unsatisfactory source of revenue for state governments and should be replaced by other forms of state or federal taxation."

(5) The paper by Douglas Young and Bruce Beattie examined the desirability of a sales tax in terms of its burden on low versus high income groups. Young and Beattie argued that a sales tax need not be regressive. There are two reasons for this conclusion. First, when viewed over the life cycle of an individual, the tax tends to be proportional. During the early years, a person who is relatively poor tends to consume more than his or her current income and, therefore, faces a relatively high burden from the sales tax. As the person grows older, however, income rises relative to consumption, reducing the burden of tax. The second reason that the sales tax tends not to be regressive is that many items can be exempted from taxation. Young and Beattie conclude that if food consumed at home, shelter, fuels, utilities, public services, health care, education, and personal insurance and pensions were exempted, the "sales tax would be slightly progressive" (Young and Beattie, p. 11).

Though Young and Beattie did not address the impact of a sales tax on economic growth, Professor Vedder did consider the correlation (not the causation) between economic growth and sales taxes. He found that the fastest growing states derived 27% of their income from from the sales tax, while the slow growing states got over 21% of their revenues from the same source. "The low growth states raised almost 20% more money from income taxes than from sales taxes, while the high growth states raised over twice as much money from sales as opposed to income taxes" (Vedder, p. 8).

House/SENATE TAXATION
EXHIBIT NO. 2
DATE 1-19-87

The common thread in these papers is that taxes do matter, but that the degree to which they matter depends on what is happening to other economic variables. Taxes cannot be considered in a vacuum. Furthermore, not all taxes have the same impact on economic activity. When considering tax reform, careful attention must be paid to whether our taxes increase or decrease the size of the economic pie. If we cannot get the pie growing, state government and Montana's citizens will continue to have to fight over the slicing of smaller and smaller pieces.

COMMENTS ON MONTANA TAX REFORM *

Myles J. Watts and Bruce R. Beattie **

The term tax reform has a variety of meanings depending upon the context and who is using it. Tax reform has often meant simplification. Clearly, that is not the center of concern in the Montana debate. In the current Montana tax reform discussion, it appears that reform encompasses not so much tax simplification but is concerned with overall levels of taxation and the composition of taxes (by composition, we mean the proportion of revenue generated from each source, i.e., by economic sector -- agriculture, mining, wage earners, etc. -- and by type of tax -- property tax, income tax, severance tax or sales tax). The debate also encompasses concern over the level of business activity in Montana and the relation of taxes thereto.

We will discuss the following three items:

1) Criteria for evaluating a tax system

2) Taxes and business activity

3) Specific considerations for tax reform

Criteria for Evaluating A Tax System

Four possible criteria for evaluating a tax system are:

1) Equity/fairness

2) Impact on economic growth

3) Stability of revenue

4) Economy of administration

* Prepared at the request of the Montana Joint House and Senate Taxation Committee; testimony presented to the Committee on January 19, 1987. These comments are solely the views of the authors and in no way should be construed as representing Montana State University or its Department of Agricultural Economics and Economics.

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House/ SENATE TAXATION
EXHIBIT NO. 3
DATE 1-19-87
~~BILL NO.~~ Joint Hearing

Equity/Fairness. Equity means treating people in the same economic circumstances (wealth, income, and/or expenditure) in a similar manner. Judgements about fairness or equity are generally based on either the principle of ability to pay or benefits received or both. Forging workable measures of these principles is fraught with difficulties and inconsistencies, not the least of which is agreeing on what is the best (least bad) operational measure of ability to pay, i.e., current income, current "taxable" income (according to the federal or state income tax code), permanent income, wealth, or consumption. Obviously, views of fairness and equity depend largely on personal values and perspective. Not surprisingly, a consensus on the fairness and equity of individual taxes and the tax system has not and likely will not emerge.

Impact on Economic Growth. This criterion has to do with designing a tax system that minimizes in so far as possible adverse effects on resource allocation and investment, incentives for business activity, and growth of the "economic pie". Taxes make a difference as to the attractiveness of alternative business locations and on long-term economic growth as does the level and quality of government services, e.g., highways and education.

Two particularly troublesome problems exist in correctly assessing the impact of taxation on business activity. First, taxes often redirect resources in unintended ways. For instance, federal tax policy, primarily capital gains taxation, encouraged the conversion of rangeland to cropland during the late 1970s and early 1980s. Second, the ultimate incidence of a tax (i.e. who pays in the final analysis) is often not the entity (individual, firm or item) upon which the tax is levied. For purposes of analysis it would be convenient if taxes were not "shiftable", so that those intended to

House/ SENATE TAXATION
EXHIBIT NO. 3
DATE 1-19-87

bear the burden actually did so. Tax shifting should be taken into account in assessing tax incidence, impact on economic growth, and policy.

Stability of Revenue. There are at least three opposing views of what is desirable with respect to stability of revenue and thus government spending. One view is that government services should continue at about the same level through good and bad economic times and that a desirable tax system should produce a relatively stable stream of revenue. Obviously, this stability argument is inconsistent with the competing idea (view) that tax collections should vary with the ability to pay of the individual taxpayers, i.e., collections should rise and fall with the economic times. There is yet a third view that government expenditures should move counter-cyclical to the economic health of an economy--the idea being to provide impetus to the economy when the private sector falls on hard times and to provide a safety net for those hardest hit by an economic downturn. Irrespective of which view is held, it seems desirable to design a tax system that produces a less volatile revenue stream than the present Montana tax system on both the up side as well as the downswing.

Economy of Administration. This criterion refers to a tax that can be administered efficiently and cost effectively. Compliance and collection costs imposed on the private sector as well as the government deserves consideration. If the combined cost of taxpayer compliance and government collection and enforcement for a particular tax exceeds the revenue forthcoming, such a tax has dubious merit as a revenue source. (For additional discussion of criteria for evaluating taxes, see House and Wolfe.)

Taxes and Business Activity

Before discussing the relationship between taxes and business activity, some other points need to be raised. Much of the recent debate has been predicated on the assumption that Montana wishes to increase the level of business activity. Such an assumption deserves careful consideration in a broad context. The level of business activity depends upon a wide variety of government policies and nongovernmental characteristics of the economy. Nongovernmental characteristics include, for example, geography and climate, distance to market, labor supply and quality, and the resource base. Governmental policies include environmental regulations, labor laws, and taxes. While taxes and governmental policy make a difference, other factors are likely to be of relatively greater importance in determining the future health of the Montana economy, as in the past. Whether we like it or not most of what happens to Montana's economy is beyond the control of Montanans--especially beyond the control of state government.

Turning now to the main issue: What do we currently know about taxation and business activity? The literature does not provide very much solid information about business activity and taxation. Clearly, high total taxes (tax collection from all sources -- income, severance, property, sales taxes, etc.) result over a period of time in reduced business activity (Benson and Johnson). However, claims that substantial decreases in taxes will result in huge increases in business activity and asset values are just as ridiculous as claims that taxes have no influence. "Reasonable" taxation levels (in line with competing states) have a moderate to small effect on the location of business activity. While tax effects on business activity should not be ignored, tax effects should not be exaggerated such that sight is lost of other important influences -- influences that are more than likely of greater relative importance, especially in Montana.

The final incidence of taxes is an important consideration in ascertaining the impact of taxes on business climate as well as tax policy generally. However, not much is known about tax incidence. In the end people pay taxes, but it is not easy to identify which people. For example, in the case of a corporate income tax levied on sawmills, do the stockholders (in terms of reduced dividends and asset values), the loggers (who bring timber to the sawmill), the owners of the timber (in terms of reduced stumpage), and/or the sawmill workers (in the form of reduced wages or hours worked) pay the tax in the end?

Most economists believe intuitively that the composition of taxes influences the kind or level of business activity. In particular, it is commonly thought (a belief that we share) that a tax on consumption such as the retail sales tax has less negative effect on business activity than personal income tax, corporate income tax, or other business-targeted taxes; but again we must emphasize there is little applied research aside from opinion polls to support this view.

Specific Considerations for Tax Reform

If Montana wishes to encourage business activity, then it must compete with other states. Therefore, it is appropriate to consider those areas of taxation where Montana differs from other states in a way that is perceived by the business community to be disadvantageous.

Unitary Method of Taxation. Apparently the worldwide unitary method of corporate income taxation is a "red flag" to some businesses even though Montana's tax is not as worldwide as perceived. However, moving to a "water's edge" criterion might be a signal of welcome to these businesses. Also, if little tax revenue would be given up by such a move, then changing or eliminating the unitary taxation method could have a positive impact on

Montana's perceived business climate at little or no cost to the state treasury.

Personal Income Tax. Montana's top marginal personal-income-tax rate is high relative to most other states. Executives who may consider Montana as a business location are likely to be sensitive to high state personal income taxes. At the recent joint UM/MSU sponsored conference on "Taxation and the Montana Economy," James Brady of Fantus Company was an invited speaker. (Fantus Company specializes in assisting businesses in finding attractive and profitable locations for their operations.) With regard to the 11 percent top Montana income tax bracket, Brady suggested that "... it tends to create instant lockjaw among most higher-level managers who will often shudder at the prospect of having to pay this much money. ... With a top rate of 11 percent, you instantaneously turn off a lot of decision-makers potentially looking at Montana ..." (p. 7).

Two general alternatives might be considered to deal with the problem of high top-end marginal income tax rates. The first would be to merely reduce the higher rates. The net effect of higher rate reduction would be to reduce income tax revenues at least in the short run. However, in the longer run if a lower top-end personal income tax rate had the desired effect in terms of business attractiveness, then the negative impact on revenue might be reversed. An example of the second alternative might be to reduce the overall rate schedule (especially the top end) and terminate deductibility of federal income taxes so that effective income tax collections remain approximately constant, i.e., make two adjustments to the income tax code that are roughly offsetting so that the net effect is revenue neutral in the short run. There are no doubt other adjustments that would be more attractive than eliminating federal income tax deductibility. It was used only for illustrative purposes.

SENATE TAXATION
EXHIBIT NO. 3
DATE 1-19-87

Worker's Compensation Insurance. At this point, Worker's Compensation Insurance premium rates in Montana are high compared to other states in the region. Again, Brady points out that

> ... despite the fact that maximum weekly benefits in Montana fall within an average range, and income benefits for scheduled injuries in Montana are not unreasonable, the rates charged by private insurance carriers to Montana businesses are very high. Clearly, something is going on to make these rates so high, such as the size of recent awards, possible liberal interpretation and administration of the act, reflected perhaps by the fact that 55 percent of the workers' compensation cases in Montana are judged to be permanent partial disability, which is at the high end of the range among states ... (p. 8).

Montana's Worker's Compensation program should be evaluated to determine why it is out-of-line with other states and corrective action taken. Brady's statement suggests a fruitful direction for investigation.

Property Taxes on Livestock. The revenue generated by property taxes on livestock is relatively small--less than .2% of state and local tax revenues. It is our hypothesis that collection costs for both the government and the private sector are relatively high for such a small amount of revenue generated. Bordering states of North and South Dakota, Wyoming and Idaho do not tax livestock. Montana should likewise discontinue the property tax on livestock.

Coal Severance Tax. Montana's coal severance tax is high, which certainly has to affect business activity in the energy and mining sectors. Terry Anderson discusses this issue. A 50% reduction of our 30% severance tax rate would not be unreasonable and is needed to bring us in line with Wyoming and North Dakota.

SENATE TAXATION
EXHIBIT NO. 3
DATE 1-19-87
BILL NO. 7 ...

Retail Sales Tax. Several pros and cons of a sales tax are worthy of note. First, while the empirical evidence is unclear, there seems to be a broadly-held belief that a retail sales tax has less adverse effect on business activity than other kinds of taxes. On the con side, the recent termination of the deductibility of sales tax in computing federal income taxes makes the sales tax less desirable than heretofore. On the pro side, it is our hypothesis that a sales tax would reduce the volatile nature on Montana's tax revenue stream.

Finally, the regressivity argument so often mustered against sales taxes is, to a large extent, falacious (Young and Beattie). A sales tax can be designed to be regressive, proportional or even progressive by exempting certain items from the base. More fundamentally, of course, the progressivity or regressivity of any tax, including the sales tax, depends on the measure of ability to pay -- current income, federal or state taxable income, permanent income, wealth or consumption -- and whether the matter is viewed from a current year or a life-cycle perspective. The commonly held belief that retail sales taxes are regressive is no doubt based on the premise that current year federal or state taxable income is an acceptable or even good measure of ability to pay. In our view nothing could be further from the truth, recent changes in the federal tax code notwithstanding.

In addition to these pros and cons, two matters are likely crucial to the efficacy and political viability of a sales tax. If a sales tax is proposed, serious consideration should be given to including certain retail services as well as "hard" goods. Retail services is one of the fastest growing segments of the U.S. economy. Finally, if a sales tax were to be considered, tying it to property, income, and severance tax relief and/or a constitutional or statutory limit on state government tax-supported spending would not be unreasonable. (The limit on state government tax collections could be indexed to growth in the state's economy.)

Neal Peirce, a national syndicated columnist specializing in state and local government, was the wrap-up speaker at the aforementioned conference on "Taxation and the Montana Economy". Peirce stated,

> I should think, and I hope, that Montanans at large will make note of what counsel was offered here on the sales tax question. That the visiting firemen and firewomen, conservative and liberal and middle-of-the-road alike, all pretty much told you, the time for the sales tax is at hand. ... to outsiders, it makes precious little sense for Montanans to maintain blanket opposition to the sales tax (p. 34).

Summary of Specific Considerations and Conclusion

In review, we believe that seven ideas are worthy of serious consideration in restructuring Montana's tax system:

1. Move to a "water's edge" unitary tax method in place of the present "worldwide" unitary tax method for corporate income tax purposes.
2. Reduce the top Montana personal income tax rate(s).
3. Investigate Worker's Compensation Insurance policy and procedures and take appropriate corrective actions to bring premiums in line with other states.
4. Eliminate property taxes on livestock.
5. Substantially reduce coal severance tax rates.
6. Enact a sales tax to offset lost revenues due to anticipated reduction in severance and income tax collections and the elimination of property taxes on livestock.

SENATE TAXATION
EXHIBIT NO. 3
DATE 1-19-87
BILL NO. Joint

7. Enact a constitutional or statutory limit on growth in tax revenue collections in support of state government, indexed to the state's economy.

While the list is not comprehensive, these suggested changes in Montana's tax system are offered for consideration as areas where Montana differs significantly from other competing states in its tax structure. There are good reasons to believe that these existing tax structure differences are deleterious to Montana's prospects for economic recovery and future economic growth and development. Being different is sometimes virtuous and a source of individual and state pride. However, such is definitely not the case when it comes to designing an optional state tax system.

In the final analysis, Montana must decide what levels of various government services are desired relative to their costs. The cost and benefits should be an important consideration in program choice. While each and every government service should be evaluated relative to its benefits and costs, it is particularly important to be aware of the overall level of services and taxation in considering each program in order to develop a package of government services desired by the citizens and affordable to the taxpayers of Montana. Thus, as you grapple with reforming Montana's tax system, it is important to be concerned both about taxes and the services those taxes are supporting.

SENATE TAXATION
EXHIBIT NO. 3
DATE 1-19-87

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SENATE TAXATION
EXHIBIT NO. 3
DATE 1-19-87
BILL NO. [illegible]

MONTANA

COMPREHENSIVE ANNUAL FINANCIAL REPORT

JUNE 30, 1986

House SENATE TAXATION
EXHIBIT NO. 4
DATE 1-19-87
BILL NO. Joint Hearing

Wally Miller Report

Legislature given guidelines

Guest columnist

Gary Buchanan

The Montana Tax Reform Education Committee was formed over a year ago to promote debate and reform of Montana's tax and revenue system. MONTREC was formed in part because of legislative inaction on the tough issues of taxes and government expenditures.

When we started, tax reform was not at the top of the political agenda. It now is, thanks to our own I-105 and the near passage of CI-27. It is also at the top of the agenda because of the widespread realization that the status quo does not work and major changes are in order.

Some people are asking what's the message behind I-105? As the sponsors, we thought we would restate our fundamental theme and objectives:

I. Reduction of government expenditures
II. Substantive property tax relief
III. Alternative revenue sources to replace property taxes
IV. The development of a balanced tax system

I. REDUCE GOVERNMENT EXPENDITURES

Montana has an overbuilt, overly administered governmental system. Our declining population of 826,000 people is about the same size as an intermediate sized American city, but look at what we attempt to support — 56 counties, 127 cities, 19 judicial districts, six separate universities and a community college system (with declining enrollments). Just at the county level, we pay for more than 600 elected officials. We've built a service structure too large for our revenue base and it's time to fix it. The Legislature must deal with government consolidation at the state, county, city and university levels. Controlling expenditures must remain the highest priority.

II. PROPERTY TAX RELIEF

The Legislature clearly must deal with the property tax rebellion. CI-27 and I-105 were just two symptoms of a tax system that is flawed and not working. The reappraisal system is a debacle and aggravated the current situation further. A revised I-27 will pass the next time around if the Legislature does not act. Legislative proposals to duck issues and send them back to the initiative or referendum process are an abdication of responsibility and merely "political ping pong." We elect and pay legislators to act, and now is the time to solve these severe problems during the 1987 session. I-105 will freeze taxes in certain classes only if the Legislature does not act to lower them. A cosmetic response will only backfire. MONTREC will, in fact, support expansion of this concept by the Legislature to additional classes.

ALTERNATIVE REVENUE SOURCES

We think the legislative history in support of local governments is dismal. As the League of Cities and Towns said in 1985, "There is a basic structural problem in Montana's method of financing local government and education. Heavy spending requirements are loaded on a narrow property tax base and the entire system is out of balance and riddled with inequities."

The 1987 Legislature must reverse and discontinue its practice of balancing the budget crisis on the backs of local government. Local government must be given meaningful, not cosmetic, revenue alternatives to the property tax.

IV. DEVELOP BALANCED TAX SYSTEM

The lack of balance of Montana's tax system was made clear by the Advisory Council's Intergovernmental Relations Sept. 1985 study. Montana was ranked 46th in the study's "final report card," 43rd in business climate and 47th or nearly last in "balance" of our tax system. We are concerned with this lack of balance and our overreliance on residential and business property taxes to fund public services. We applaud the Montana Forward study and agree with their concern regarding "personal property taxes." We also support the Governor's Transition Task Force recommendation on tax reform from an economic development standpoint.

In conclusion, study after study points to the problem. Our tax system is not only out of balance and often negative for business and economic development, but in 1986 does not raise the necessary revenue for fundamental public services. Fundamental tax reform is essential — not bandages, tourniquets and compresses like the actions of the last special session. The 1987 Legislature must act on its own because that's why we elect Senate and House members. Legislative actions to duck the issue and simply refer solutions back to the initiative process are unacceptable. That's what I-105 is about. It is a purposely general yet firm and constructive message to prompt the Legislature towards leadership.

Gary Buchanan is an investment broker in Billings. He is also co-chairman of the Montana Tax Reform Education Committee, sponsors of Initiative 105.

House / SENATE TAXATION
EXHIBIT NO. 5
DATE 1-19-87
~~BILL NO.~~ Joint Hearing

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Montana Tax Reform Education Committee, supporters of Property Tax Reform Initiative 105 voted in a majority Friday to take a position on the sales tax as the most acceptable alternative revenue source for the Legislature to consider in this session.

At a joint House and Senate Taxation Committee hearing Monday night MONTREC officials will also recommend that, if the Legislature feels that a new tax would go to the people anyway, that it should be in a Special Election before July, 1987. In addition, the sales tax should be matched up with an income tax surcharge.

Montana property owners cannot wait until 1988 or 1989 for relief. Montana's schools and local government cannot wait until 1988 or 1989 for tax reform and alternative revenues.

Initiative 105 clearly told the Legislature and the Governor to solve it now and not to delay the solution by what appears to be a combination of political ping pong and dodge ball. Initiative 105 advises the Legislature that, along with property tax relief, there must be alternative revenues for local governments and schools.

House/ SENATE TAXATION
EXHIBIT NO. 5
DATE 1-19-87
~~BILL~~ NO. Joint Hearing

If the Legislature and Governor will not accept this responsibility to act, then the people should be given an option of a sales tax or the only other viable option -- a dramatic income tax increase to raise the same monies as a sales tax. Action on the $73,000,000 windfall from the Federal Tax Reform Law should also be deferred until there is a sales tax/income tax Special Election.

The $73,000,000 windfall should be included in a genuine income tax increase, which it is.

Seventy-three million dollars is a defecto income tax increase, which should be recognized as such.

If the Legislature and Governor are going to insist on not providing leadership on these issues and merely kick it back to the people, then lets get going as soon as possible. The matter should be resolved before July 1 of this year, when Initiative 105 triggers a freeze on property tax, unless there is tax reform.

MONTREC feels that a sales tax or the surcharge on income tax should be for substantial property tax relief.

The MONTREC organization has pledged to take the lead in promoting a sales tax to the Legislature and also if it comes to a Special Election.

House SENATE TAXATION
EXHIBIT NO. 5
DATE 1-19-87
BILL NO. Joint Hea

Many organizations interested in property tax reform have contacted MONTREC in the past two weeks to be more than just a monitor of tax reform in the Legislature. Various members of the House and Senate also suggested that MONTREC take a stand.

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House/SENATE TAXATION
EXHIBIT NO. 5
DATE 1-19-87
BILL NO. Joint Hearing

Al Donahue, ~~Great Falls~~ Montrec

I approach you this evening as a founding member of MONTREC..a Democrat...and a life long one at that..who was defeated in the June primary. ~~by less than 1/2 of 1% of the vote~~, while running for the State Senate, from Great Falls. I lost, BUT BARELY because I advocated a sales tax for property tax relief.. ~~At one time, while working in the Legislature, I was adamantly opposed to a General Sales Tax~~. I rather imagine that I'm the only one in this room, who was defeated, because he felt that a sales tax, for property tax relief, was needed in our state. For some time, standing alone as a sales tax Democrat, I felt somewhat ostracized, but now, I know longer stand alone, for thinking people of both parties realize only too fully, that we must give consideration to joining the 98% of the people of the US who pay it.

[illegible] 1/2 of 1% (41 votes) [illegible] would have been [illegible]. The ST is ~~no longer~~ slowly diminishing as a political albatrose.

For...I've discovered, it was the Democrats in the earlier days, that proposed the sales tax, so as to fund social programs, and further, of the 45 states that have the sales tax, 35 states signed it into law, over the signature of a Democratic Gov. That is, better than 80% of the sales tax states, saw it come into being, under a Democratic Governor. Now, 97.5% of the people of these united States, pay a general sales tax. Not a signle state has ever seen it voted it in by the people, but conversely, not a single state has ever permanently thrown out the sales tax. Why...because it works.

House/ SENATE TAXATION
EXHIBIT NO. 6
DATE 1-19-87
~~BILL~~ NO. Joint Hearing

A WELL [illegible]

poor by exempting the necessities of life, is a fairer tax to them, than escalating property taxes. Property taxes are the regressive taxes, for they have nothing to do with ones ability to pay. A WELL ~~properly~~ designed sales tax, with a cap on it that could only be changed by a vote of the people could be considered. Low income people pay a higher percentage of their income for the necessites of life, and under the proper sales tax proposal, those necessities would probably be exempt. And the possibility exists that rebates could be given to low income people, to offset their sales tax charges. So, who winds up paying most of the sales tax... the middle and high income people..as well, it should be.

I have great difficulty in understanding CERTAIN SEGMENTS OF ORG ~~LABOR~~ labor when they say....we have always been opposed to a sales tax, and always shall be. That is not the case in other states, where organized labor has supported the concept, & some major Mont. labor organizations are now for labor in those states know, that low property taxes mean jobs. Harry Truman advocated the sales tax.

SENATE TAXATION
EXHIBIT NO. 6
DATE 1-19-87
BILL NO. Joint Hearing

I recall listening on tv the other night to the former Gov. of Alabama, George Wallace, who said at one time, that he would NEVER support segragation. During that same program it showed him accepting, in a wheel chair, an honorary degree from a ~~colored~~ black university, and he said that it was a highlite of his life and that he was wrong in his fight for segration. To say that you will NEVER support a sales tax is kin to saying that apartheid will never be defeated in

South Africa..or that integration would NEVER come to the South.

Everyone pays a sales tax, including the tax dodgers and evaders. The Federal Gov. estimates that the underground cash society is worth about one billion dollars a year. That many dollars rolls around without any tax being paid on it. At least, when those folks buy something, we've got 'em. This state is looking more and more to tourism as an industry to bring dollars into Montana. Now the tourists pay NO sales tax, and enjoy the benefits of our state, cities and towns.

In our tax situation, What worked back then...is not working now. The big boys have left and are leaving Montana. The property tax burden continues to fall on those of us that are left, whether we are average working citizens or small businesses. We can't handle it any longer. We need a balanced tax system and the sales tax, for property tax relief, should be part of it. But DO IT NOW! We can't last another two years.

Al Donohue

House - SENATE TAXATION
EXHIBIT NO. 6
DATE 1-19-87
BILL NO. [illegible]

Conrad & Brown

512 NORTH 29TH STREET
BILLINGS, MONTANA 59101

406-245-6102

CONRAD F. STROEBE, CPA
JAMES M. BROWN, CPA

To: Senator George McCallum
Representative Jack Ramirez
Senate and House Committees on Taxation
of the 50th Montana Legislature

Please accept the attached address and the accompanying narrative in response to your call for public testimony on Montana's overall tax system.

Thank you for listening.

Sincerely,

Conrad Stroebe

James Brown

House/
SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87
~~BILL NO.~~ Joint Hearing

JANUARY 19, 1987

MR. CHAIRMEN, LADIES AND GENTLEMEN OF THE HOUSE AND SENATE COMMITTEES ON TAXATION:

IN NOVEMBER, 1986, THE PEOPLE OF MONTANA PASSED INITIATIVE 105 AND ALMOST PASSED CONSTITUTIONAL INITIATIVE 27. I-105 CALLED FOR PROPERTY TAX RELIEF. CI-27 PROPOSED THAT PROPERTY TAXES BE ELIMINATED.

WE READ NOW IN THE PAPERS THAT SOME LEGISLATORS WOULD LIKE THE PEOPLE TO CHOOSE IN THE NEXT FEW MONTHS BETWEEN A SALES TAX AND AN INCOME TAX SURCHARGE TO HELP BALANCE THE BUDGET. WE DO NOT BELIEVE THAT THESE LEGISLATORS HAVE HEARD THE MESSAGE OF EITHER I-105 OR CI-27. THE PEOPLE OF MONTANA DO NOT WANT AN ADDITIONAL TAX.

OUR ECONOMY IS STRUGGLING. OUR TAXING SYSTEM PLACES AN ENORMOUS BURDEN ON OUR BUSINESSES, ONE THAT MAKES IT VERY DIFFICULT TO COMPETE IN OUR TRADE AREA. WE NEED TO GIVE OUR BUSINESSES TAX RELIEF IN ORDER TO STIMULATE OUR DEPRESSED ECONOMY.

AT THE SAME TIME THAT THE PEOPLE AND BUSINESSES ARE ASKING FOR RELIEF, THE STATE FACES A SUBSTANTIAL BUDGET DEFICIT. THE QUESTION IS HOW TO PROVIDE BOTH RELIEF AND ENOUGH REVENUE FOR THE STATE TO OPERATE.

SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87
~~BILL~~ NO. Joint Hearing

WE OFFER THE PEOPLE'S PLAN FOR TAX REFORM AS A SOLUTION TO THIS DILEMMA. THIS PLAN PROPOSES THE FOLLOWING:

1) ELIMINATE ALL RESIDENTIAL REAL PROPERTY TAXES. THIS RESPONDS TO BOTH I-105 AND CI-27.

2) ELIMINATE ALL PERSONAL PROPERTY TAXES ON BUSINESS AND AGRICULTURAL EQUIPMENT. THIS PROVIDES TAX RELIEF TO BUSINESS.

3) REDUCE BY 33% AND FREEZE, PROPERTY TAXES ON AGRICULTURAL, MINERAL, UTILITY AND COMMERCIAL PROPERTIES. THIS PROVIDES ACROSS THE BOARD RELIEF TO BUSINESSES.

IN PLACE OF THE ABOVE TAXES, THE FOLLOWING WOULD BE ENACTED:

1) IMPOSE A 5% SELECTIVE SALES TAX ON ALL RETAIL SALES AND SERVICES. GROCERIES, PRESCRIPTION DRUGS, HEALTH CARE AND UTILITIES WOULD BE EXEMPT FROM TAXATION. BUSINESS AND AGRICULTURAL PURCHASES FROM WHOLESALERS WOULD ALSO BE EXEMPT. THE AVERAGE PROPERTY OWNER WOULD PAY SUBSTANTIALLY LESS IN SALES TAX THAN IN PROPERTY TAX EVEN CONSIDERING THAT A DEDUCTION FOR PROPERTY TAXES WOULD NO LONGER BE ALLOWED ON FEDERAL AND STATE INCOME TAX RETURNS.

2) IMPOSE A 2% TRANSFER TAX ON REAL PROPERTY SALES. RESIDENTIAL PROPERTY SUPPOSEDLY SELLS EVERY SEVEN YEARS. PROPERTY TAXES CURRENTLY AVERAGE ABOUT 1.3% OF VALUE EACH YEAR, OR 9.1% OVER 7 YEARS. THIS TAX RECOGNIZES THAT PROPERTY OWNERS ARE THE USERS OF ESSENTIAL SERVICES BUT IT TAXES THEM AT A FAR LESS RATE THAN THE CURRENT RATE. THE IMPOSITION OF THIS TAX RESULTS IN VERY LITTLE CHANGE IN THE NET PROCEEDS RECEIVED ON SALE THAN HAPPENS CURRENTLY.

SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87

3) IF THE SALES AND TRANSFER TAX ARE NOT SUFFICIENT TO COVER REVENUE LOST BY ELIMINATING AND REDUCING PROPERTY TAXES, IMPOSE A PAYROLL TAX NOT TO EXCEED 1% TO COVER THE SHORTFALL. THIS TAX WOULD BE PAID 50% BY BUSINESS AND 50% BY THE EMPLOYEE. PRELIMINARY REVENUE ESTIMATES INDICATE THAT SUCH A TAX MAY NOT BE NEEDED AT ALL OR WOULD BE SUBSTANTIALLY LESS THAN 1%.

THE ADVANTAGES OF THE ABOVE TAXES ARE THAT THEY ARE A REPLACEMENT OF PROPERTY TAXES AND RESULT IN LESS TAXES BEING PAID BY THE PROPERTY OWNER. ADDITIONALLY, THEY ARE ELASTIC--YOU PAY TAX ONLY WHEN YOU CHOOSE TO PURCHASE. THIS IS NOT THE CASE WITH PROPERTY TAXES. FINALLY, THE TAX BASE IS BROADENED. TOURISTS, NON PROPERTY OWNERS AND OUT OF STATE PURCHASERS OF RETAIL PRODUCTS PAY THEIR FAIR SHARE.

THE ABOVE PROPOSAL IS INTENDED TO BE REVENUE NEUTRAL. TAX RELIEF IS ESTIMATED AT $350 MILLION. THE SALES TAX AND TRANSFER TAX SHOULD BRING IN $303 MILLION. INTEREST EARNED ON SALES TAX REVENUE SHOULD APPROXIMATE $7 MILLION. ADDITIONAL STATE INCOME TAXES FROM NONDEDUCTION OF PROPERTY TAX COULD APPROXIMATE $10 MILLION. THERE WILL ALSO BE AN INCREASE IN FEDERAL TAX REVENUE FROM NONDEDUCTION OF PROPERTY TAXES. THE STATE SHOULD PETITION ITS FEDERAL LEGISLATORS FOR A REBATE OF THESE TAXES FOR A FEW YEARS IN EXCHANGE FOR PAYING THEM IN THE FUTURE. THE COMBINATION OF THESE REVENUE SOURCES COULD ELIMINATE THE REQUIREMENT FOR ANY EMPLOYEE PAYROLL TAX.

SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87
BILL NO. [illegible]

AS WAS INDICATED EARLIER, THE PEOPLE'S PLAN ALSO OFFERS THE POSSIBILITY OF RELIEF FOR THE BUDGET DEFICIT--BUT ONLY IN THIS BIENNIUM. SEVERAL REPORTS INDICATE THAT MONTANA'S LEVEL OF GOVERNMENTAL SPENDING IS TOO HIGH. OBVIOUSLY THIS CAN NOT BE CURED OVERNIGHT. THE PEOPLE'S PLAN HELPS GIVE THE LEGISLATURE TWO YEARS TO DEAL WITH THIS PROBLEM.

WE PROPOSE THAT PROPERTY OWNERS PAY PROPERTY TAXES AT THE CURRENT LEVELS FOR THE FIRST FOUR MONTHS OF 1987. THESE TAXES WOULD BE COLLECTED IN NOVEMBER, 1987. THE SALES TAX WOULD BE IMPOSED TO BE EFFECTIVE ON JULY 1, 1987. THROUGH THIS COMBINATION OF TIMING, APPROXIMATELY $83 MILLION OF REVENUE COULD BE RAISED TO HELP WITH THE DEFICIT PROBLEM.

WE BELIEVE THAT THE PEOPLE'S PLAN IS A GOOD PLAN -- ONE THAT IS RESPONSIVE TO PEOPLE AND TO BUSINESS. WITHOUT EXCEPTION, OTHER TAX REFORM PROPOSALS THAT HAVE BEEN MADE PUBLIC, WILL RESULT IN TAX INCREASES FOR OUR PEOPLE. THAT IS NOT WHAT THEY ASKED FOR FROM YOU.

IF MONTANA WANTS A SALES TAX, THEN MONTANAN'S DESERVE SOMETHING BETTER THAN MORE TAXES OR MORE GOVERNMENT.

CONRAD & BROWN
512 North 29th Street
Billings, Montana 59101
Ph: (406) 245-6102

SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87
BILL NO. Joint Hearing

Conrad & Brown
512 NORTH 29TH STREET
BILLINGS, MONTANA 59101

406-245-6102

CONRAD F. STROEBE, CPA
JAMES M. BROWN, CPA

January, 1987

Dear Fellow Montanan:

No doubt you've been keeping up on the tax and budget issues which confront our legislature. Recent articles in the Billings Gazette indicate that our legislators are confused and that ultimately, we, the people, may have to choose between a surcharge on state income taxes or a statewide sales tax to balance the budget. Governor Schwinden favors a vote of the people in November, 1988 to decide the options. We don't feel that we can wait that long.

An article that recently appeared in the Billings Gazette, "Consider following tax plan", is enclosed. This article proposes $220 million of tax relief to businesses and $150 million of property tax relief to individuals. A 5% sales tax basically replaces the lost tax revenue.

We feel that this plan will stimulate the economy and expand the tax base so that a fair amount of tax is paid by all. Additionally, this plan could go a long way toward providing needed revenue to balance the budget--if it is properly implemented--without stealing from trust funds.

We intend to provide a full and comprehensive plan to the legislature. However, much needs to be done and we need your help to do it. We need funds to properly prepare the plan, advertise it and sell it to the legislature. We intend to persuade the legislature to make a decision now. We have reviewed other plans for tax reform and have seen several good points raised. Most incorporate a sales tax with property tax reduction. We do not believe that a sales tax will pass as an additional tax--even if property tax relief is promised. We believe that Montanans will accept a sales tax only as a replacement for property taxes. That premise is the foundation of our plan.

I am enclosing a brief explanation of the rationale behind The People's Plan as well as estimates of costs and savings. (These numbers differ slightly from those in the article as they are more current and more precise.) Please estimate your business and personal tax relief under the proposed plan and send 1% to The People's Plan For Tax Reform to help fund this effort. You will be the principal beneficiary if it is successful. I would be happy to discuss this proposal, as well as our future course of action, at your convenience.

Sincerely,

C. Stroebe

SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87

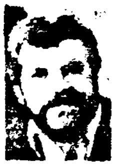
The Billings Gazette is dedicated to the continued growth of Billings and Montana while recognizing that our unique quality of life must be maintained and preserved.

Wayne E. Schile: Publisher
Richard J. Wesnick: Editor
Carl E. Rexroad: Managing Editor
Gary Svee: Opinion Editor

DEC. 24, 1986

Consider following tax plan

Guest columnist



Conrad Stroebe

In November, Montana's voters expressed their concern about property taxes by their votes on CI-27 and I-105. Throughout 1986, many businesses have questioned the fairness of various forms of taxation. Everyone wants relief — but not at the expense of essential services, particularly education.

The governor, several legislators and various political action committees are busy formulating plans for relief. But none of the plans that have been released publicly are really responsive to CI-27 and I-105.

We need to implement a balanced tax program to give relief to individuals and businesses. We need a program that takes advantage of the purchasing power of our tourist trade. Additionally, it must be flexible in that if the consumer does not have the money to spend, he does not pay the tax. This is certainly not the case with property taxes. The Montana economy is severely depressed, property values are plummeting and property taxes are escalating. Anyone who has recently attempted to refinance his home can attest to that.

But we do not need a new tax in addition to property taxes. We need a consumption tax in place of our property tax. A reduction in property taxes coupled with imposition of a sales tax is not the answer. Look at our neighboring states who got relief until the legislators needed to balance ever expanding budgets. Now they have a sales tax and their property taxes are back to where they were before "relief."

Before you look at the tax reform plan assembled here, please know that it is the result of a lot of work by a lot of people. First, it comes directly from the voters of Montana through CI-27 and I-105. Second, it takes into account research and recommendatios from local business people along with such groups as the Advisory Commission on Intergovernmental Relations (Washington, D.C.).

In summary, we propose the following:

1. Abolish residential real property taxes.

2. Abolish personal property taxes on business and agricultural equipment and mobile homes.

3. Reduce and freeze taxes on agricultural and commercial real properties, mineral properties and utility properties by 33 percent.

These proposals will reduce tax income by about $370 million. To replace that income, we offer the following:

1. Impose a 5 percent selective sales tax on retail sales and services. Groceries, prescriptions and health care are excluded. A value added tax could produce the same revenue.

2. Impose a 2 percent transfer tax on sales of real estate.

3. Consider a 1 percent payroll tax paid by the employee and/or the employer to cover any short fall that the selective (or value added) sales and 2 percent transfer taxes do not cover. This payroll tax must sunset within five years.

As you review and argue this proposal, please take time to apply it to your own personal situation. Then send a copy of those results to us. We need to let the 50th Legislature know if this plan is really workable on an individual basis. Regardless of the outcome, the results will get to our state leaders.

In November, Montanans across this state spoke very clearly through two initiatives. Both of those initiatives, taken together, said very simply "Give us something in return."

If you want a sales tax, you deserve something better than more government.

Conrad Stroebe is a Certified Public Accountant with Conrad and Brown. He is the rural district representative from Lockwood on the Billings High School District No. 2 Board of Trustees. He is treasurer of the Yellowstone County Democratic Party and the Montana Tax Reform Education Committee.

PEOPLE'S INITIATIVE — 1987
MONTANA TAX REFORM WORKSHEET

THESE PROGRAMS WOULD PROVIDE NEW TAX REVENUES

PROGRAM	AMOUNT	REASONS
• 5 percent selective sales tax on all retail sales and services (except groceries and prescriptions) statewide or statewide/local option	$250 million	— Less regressive than property tax — Provides elastic base, responsive to economic times — Easier to administer and enforce, less costly
• 2 percent transfer tax on real estate sales (2-year phase in)	$20 million	— One-time tax on recorded sales price is fairer to administer, not subject to questionable appraisals
• 1 percent payroll tax with 5-year sunset	$100 million	— Maintains voter "pocketbook" involvement — Responsive to economic employment conditions
TOTAL	$370 million	

THESE PROPERTY TAXES WOULD BE ELIMINATED OR REDUCED

ELIMINATE PROPERTY TAX LEVIES ON:		
• Homes (residential real) including equivalent rent credit	$150 million	— Responds directly to CI-27 and I-105 votes — Key trade items to win voter approval — Property taxes cost voter more than sales taxes
• Personal property (all, including agriculture and business)	$100 million	— Not as fair as one-time sales tax — Serious administrative flaws in present system; significant undercollections and overappraisals
33 PERCENT REDUCTION IN PROPERTY TAX LEVIES ON:		
• Agriculture real properties	$20 million	— Provides basic industry incentives
• Mineral Properties	$40 million	— Provides "pro-business" signals
• Utility Properties	$35 million	— Provides business relief across-the-board
• Commercial Real Properties	$25 million	
Total	$370 million	

Source: Rural and Co. High School District No. 2 taxpayers in conjunction with Conrad & Brown, Yellowstone County [illegible]

SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87
BILL NO. Joint

SUMMARY OF THE PEOPLE'S PLAN FOR TAX REFORM

The Legislature is now in session and the focal point is taxation. Several plans have been proposed that promise tax relief--most incorporate a sales tax with property tax relief. The people of Montana do not want an additional tax, even if they get some temporary relief from another form of taxation. Our neighboring states have adopted this course of action and now have lost the relief but still have the other tax. But Montanans do want property tax relief and they want to stimulate this sluggish economy. The People's Plan satisfies these goals.

The following are some characteristics of the Montana tax system. Rankings are provided by the Advisory Commission on Intergovernmental Relations.

1) Property taxes provide almost 50% of the State's tax revenue, a characteristic that helps rank Montana as the State with the 4th most unbalanced tax structure in the nation.

2) Montana's real property taxes are almost 20% higher than the national average.

3) Montana's personal property taxes are almost three times higher than those of the next highest state in our eight state trade region.

4) Montana ranks fourth in the nation in the number of government employees per capita.

5) Montana's per capita income level ranks 40th in the nation.

Obviously, a redistribution of the tax burden and a reduction in spending are required for Montana to get going again.

Property taxes, both real and personal, have been abused as a source of revenue in Montana. In many cases, the valuations are arbitrary and capricious. And certainly these taxes are totally inelastic--many Montanans find the going tough right now, with our severely depressed economy, yet they still must pay these taxes and generally at a higher rate than before the depression began. Finally, the tax burden is not spread among all the people.

House SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87
BILL NO. Joint Hearing

A selective sales tax has the following characteristics:

1) It is elastic. When times are tough and an individual chooses not to purchase, no tax is paid.

2) It is relatively painless in that you pay as you go.

3) Necessities such as food, prescriptions, health care, and utilities are not subject to tax.

4) The tax base is broadened--tourists, non property owners, and out of state purchasers of retail products would pay their share of the tax.

Ideally, a sales tax should be used in concert with a property tax, but we do not believe that Montanans will accept an additional tax. We believe that Montanans will accept a sales tax if property taxes are eliminated. Therefore, in order to obtain relief for property owners and business and in an effort to stimulate the economy, we propose that a selective sales tax be used to replace property taxes. A real estate transfer tax is also proposed and would help to maintain some balance.

If the plan is implemented on the proper timetable, a major portion of the budget deficit currently facing the legislature can be eliminated. This would be a one time occurrence. The legislature must still find a way to trim spending.

The major problem with any tax reform package is how to make the Legislature act. Many legislators and the Governor favor a vote of the people in November, 1988. We feel that that approach is a cop out. We need something done now! But if the legislature wants a referendum in 1988 to reaffirm their action, then so be it.

We intend to persuade the legislators to act now. Our approach will be as follows:

1) We will develop a comprehensive plan along the guidelines stated in this package. This plan will be presented to the legislature.

2) We will develop a statewide advertising plan that will include a mailer from the constituents to the legislators.

3) A statewide poll will be conducted and the results will be given to the legislature.

4) An intense lobbying effort will be conducted at the legislature.

Bob Henckel of Sage Advertising will be coordinating the campaign. The following narrative details the rationale and some estimates of costs and revenues of The People's Plan.

SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87
BILL NO. Taint

THE PEOPLE'S PLAN FOR TAX REFORM

On December 24, 1986, People's Initiative--1987 (The People's Plan) appeared on the opinion page of the Billings Gazette. This tax reform plan called for the following:

1) Abolish all residential real estate taxes.

2) Abolish all personal property taxes.

3) Reduce by 33% and freeze property tax levies on agricultural, mineral, utility and commercial real properties.

4) Impose a 5% sales tax to replace lost revenue.

5) Impose a 2% real estate transfer tax.

6) If the sales tax and transfer tax do not produce enough revenue to offset the lost property tax revenue, impose a payroll tax, not to exceed 1%, to make up the difference. The payroll tax could be in effect no longer than 5 years.

The People's Plan is intended to be revenue neutral. Residential property owners and businesses will receive tax relief because additional income sources--tourists, non-property owners, and out of state purchasers--will be created by this proposal. In effect, the tax base will be broadened.

The following details the rationale behind this Plan.

<u>ABOLISH ALL RESIDENTIAL PROPERTY TAXES-</u>

In November, 1986, the voters of Montana passed Initiative 105 which freezes property taxes at the current levels. Constitutional Initiative 27, which would have abolished all residential property tax, received a 44% favorable vote. An intense lobbying effort, primarily by the schools, probably caused the defeat of CI-27. It very likely would have passed if an alternative source for the lost revenue had been proposed. Be that as it may, the message from the voters was clear--no additional property taxes and consider eliminating property taxes altogether.

The vote of the people in November could very well have been a reaction to the receipt of their property tax bills shortly before the election. Properties were taxed based on 1982 values on these statements and yet, because of the depression which Montana is experiencing, 1986 values are substantially below 1982 levels. The result is that when people are least able to pay, the taxes are the highest.

The People's Plan responds to the vote of the people on I-105 and CI-27. For the reason noted in the section on the sales tax, we propose that the residential property taxes be completely eliminated rather than reduced.

SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87
BILL NO. a.

ABOLISH ALL PERSONAL PROPERTY TAXES-

According to "A Recommended Montana Economic and Tax Reform Program for 1987" prepared by Miller & Assoc., Inc. for The Montana Forward Coalition, Inc., "Montana's taxes on personal property are almost three times that of the next highest state" in Montana's immediate trade area. Obviously, this puts our businesses and agricultural industry at a competitive disadvantage. Business and Agriculture need a boost and the elimination of this tax will help provide such a lift.

REDUCE BY 33% AND FREEZE TAXES ON BUSINESS AND AGRICULTURAL REAL PROPERTY-

Much has been made of the complaint that Montana is anti-business. This proposed tax reduction, coupled with the personal property tax elimination, provides a clear pro business signal. Additionally, this relief will help to stimulate the depressed economy. Regulated utilities will be required to pass their relief on to the consumer through reduced rates.

IMPOSE A 5% SELECTIVE SALES TAX-

Montana's tax structure is considered the fourth most unbalanced in the Nation by the Advisory Commission on Intergovernmental Relations. This is principally due to our strong reliance on property taxes as a source of revenue (46% of total tax revenue comes from property taxes).

While we continue to overburden our property owners with taxes, we lose several important sources of revenue--many of whom use the services paid for by property taxes. Tourists, non-property owners, and out of state purchasers of retail products should pay their fair share of taxes. This can be accomplished through imposition of a selective sales tax.

Groceries, utilities, prescriptions and health care would be excluded from taxation. All other retail sales and services would be taxed at 5%.

A sales tax is a fair tax in that individuals pay it on items which they choose to purchase. It is elastic--when an individual does not purchase merchandise because times are tough, he does not pay any tax. The same can not be said about property taxes.

Ideally, a sales tax should be imposed in concert with property taxes. But property taxes as a source of revenue have been so badly abused that the Montana voter will not accept a sales tax unless it replaces property taxes. The trend in surrounding states has been to impose a sales tax as property tax relief only to eventually raise property taxes at a later date to balance budgets. Montana voters do not want this to happen. Therefore, we propose that property taxes be completely eliminated in favor of the sales tax.

IMPOSE 2% TRANSFER TAX ON REAL ESTATE SALES-

Real estate is a product and essential services are provided in connection with this product. A 2% tax recognizes that some of the burden for providing these services should be borne by the property owner. Real estate turns over every seven years on the average. Property taxes nationwide average approximately 1% per

SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87

year of the property's value. Obviously, this tax is substantially less than a property tax but does contribute to overall tax balance.

IMPOSE A PAYROLL TAX WITH A FIVE YEAR SUNSET-
If the revenue generated by the sales and transfer tax is insufficient to replace the revenue lost by abolition of various property taxes, we propose that a tax on payroll be imposed to cure the deficiency. This tax should be a last resort and could never exceed 1% of gross payroll. The tax would be abolished in five years regardless of any deficiency that might be present then. Preliminary estimates of revenue indicate that this tax will very likely not be necessary.

House- SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87

ESTIMATED COSTS AND SAVINGS OF THE PLAN

The next page of this proposal details the estimated tax relief and the revenues that would be raised by implementing The People's Plan. This information is derived from the following sources:

1) Property tax statistics provided by Research Bureau, Montana Department of Revenue.

2) Sales tax data provided by "Sales Tax Data Base" presented to the Revenue Oversight Committee, Montana State Legislature by Paul Polzin, Bureau of Business and Economic Research, University of Montana.

3) Impacts of the 2% real estate transfer tax and the 1% payroll tax were estimated by Conrad & Brown, CPA.

Two important conclusions come from this data.

1) Revenue raised exceeds relief by $53 million. The 1% tax on payroll can be cut substantially. Regulated utilities would be required to pass savings on to customers. The utilities' relief cited includes both regulated and non-regulated utilities. We are attempting to find out how much relief would be passed on. If the utilities opted not to pass the relief on, they would continue to pay tax and the 1% tax on payroll would be further reduced.

2) Agriculuture and businesses would pay no tax on wholesale purchases. The sales tax is imposed only on retail sales and services. In addition to the exemptions listed, individuals and businesses will pay no tax on utilities or insurance.

House SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87
BILL NO. Taint

THE PEOPLE'S PLAN FOR TAX REFORM

PROPOSED TAX RELIEF (IN MILLIONS)

ABOLISH ALL RESIDENTIAL PROPERTY TAXES	138.996
ABOLISH ALL PERSONAL PROPERTY TAXES	102.388
REDUCE BY 33% AND THEN FREEZE THE FOLLOWING PROPERTY TAXES:	
AGRICULTURAL REAL PROPERTY	17.366
MINERAL PROPERTIES	36.619
UTILITY PROPERTIES (NOTE 1)	31.334
COMMERCIAL REAL PROPERTIES	23.784
TOTAL TAX RELIEF	350.487

NEW TAX REVENUES (IN MILLIONS)

5% SELECTIVE SALES TAX (NOTE 2)	283.525
2% TRANSFER TAX ON REAL ESTATE SALES	20.000
1% PAYROLL TAX (NOTE 3)	100.000
TOTAL NEW TAX REVENUE	403.525

NOTES-

1) REGULATED UTILITIES WOULD RECEIVE RELIEF ONLY IF THEY AGREE TO PASS RELIEF TO THE PEOPLE THROUGH LOWER RATES.

2) THE SALES TAX REVENUE IS COMPUTED AS FOLLOWS:

TAX AT 1% ON ALL SALES AND SERVICES (1987 ESTIMATE)	70.422
EXEMPT THE FOLLOWING:	
GROCERIES	-9.427
PRESCRIPTION DRUGS	-0.494
HEALTH CARE	-3.796
REVENUE PER 1% TAX	56.705

3) THE 1% PAYROLL TAX WOULD ONLY BE USED TO MAKE UP FOR ANY REVENUE SHORTFALLS IN IMPLEMENTING THIS PLAN. THE RATE CAN NEVER BE HIGHER THAN 1% BUT WOULD BE REDUCED DEPENDING ON THE SIZE OF THE SHORTFALL. THIS TAX WOULD BE COMPLETELY ELIMINATED IN 5 YEARS REGARDLESS OF SHORTFALLS AT THAT TIME.

SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87

The next page compares the estimated property tax burden by income level with the proposed estimated sales tax burden. The property tax burdens were estimated using the following approach:

1) In qualifying an individual for a mortgage, financial institutions typically require that no more than 25% of before tax income be used for payment of principal, interest, taxes and insurance. Using this rule of thumb with 10% downpayment, 9.5% interest and a 30 year repayment, maximum purchase prices of house by income level were determined.

2) This maximum house value was multiplied by 1.3% to arrive at the property tax burden. The Miller & Assoc. study states that statewide the rate is 1.32% but that for the 10 largest cities in Montana, the rate is closer to 1.5%.

It should be noted that many people with lower income levels may not own homes. However, if they rent, their rent is determined based on the economic requirements of the landlord and these requirements include property taxes. Therefore, they are indirectly paying property taxes. Many elderly people exist on social security but live in homes which they paid for over the years. These individuals directly pay the property tax.

As Montana does not currently have a sales tax, statistics related to burden are not available. We have therefore presented three estimates for comparison:

1) Using information from the Sales Tax Data Base Study prepared for the Revenue Oversight Committee, together with estimates of certain expenditures by Conrad & Brown, a table was constructed that estimates sales tax burden after exemptions by income level.

2) The State of Colorado, which had a 3.5% sales tax in 1982 published a study of tax burden by income level for the year 1982. These statistics, adjusted for the proposed 5% tax, are also presented.

3) The Federal Government publishes a table of sales tax allowances to be used with Form 1040. These allowances do not include sales tax on major purchases such as cars. We selected seven states that currently have a 5% tax, with exemptions for food, utilities, and prescription drugs, and averaged the allowances for selected income levels. These are also presented.

Under Federal tax reform, sales tax will no longer be deductible on the Federal or Montana income tax returns. Property taxes continue to be deductible. The "tax benefit" of deducting property taxes is minimal for those with income levels below $17,500. From $17,500 to $40,000 of gross income, the "benefit" approaches 20% to 23% of the property taxes paid. Above that income level, the "benefit" approaches 33% to 35% of the property tax bill.

SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87
BILL NO.

The obvious conclusion from reviewing the data presented is that the taxpayer in Montana will pay more in property taxes, even considering income tax benefits, than he will pay with a 5% sales tax.

COMPARISON OF PROPERTY TAX BURDEN WITH SALES TAX BURDEN AT SELECTED INCOME LEVELS

GROSS INCOME	12500	17500	25000	35000	50000
ESTIMATED PROPERTY TAXES	347	493	709	1009	1455
ESTIMATED SALES TAX BURDEN	224	338	406	543	618
SALES TAX BURDEN INDICATED BY COLORADO STUDY OF THEIR 1982 TAXES (ADJUSTED TO 5%)	263	355	400	560	550
SALES TAX ALLOWANCE PER FEDERAL GOVT., 1986 FORM 1040	191	243	336	420	552

IN THE ABOVE ANALYSIS, THE VALUE OF A HOME HAS BEEN ESTIMATED BASED ON THE INCOME LEVEL STATED. FINANCIAL INSTITUTIONS WILL LEND BASED ON A PAYMENT ABILITY FOR PRINCIPAL, INTEREST, TAXES AND INSURANCE OF 25% OF GROSS INCOME. DOWNPAYMENT AT 10% AND FINANCING OVER 30 YEARS AT 9.5% WERE ASSUMED.

PROPERTY TAXES WERE ESTIMATED AT 1.3% OF HOME VALUE. THE MILLER & ASSOC. STUDY FOR MONTANA FORWARD, STATED THAT THE OVERALL AVERAGE IN MONTANA IS 1.32% AND THAT FOR THE TEN LARGEST MONTANA CITIES, IT IS 1.5% FOR 1985-86.

ESTIMATED SALES TAX BURDEN IS COMPUTED USING THE SALES TAX DATA BASE STUDY PREPARED BY PAUL POLZIN.

THE COLORADO INFORMATION COMES FROM THE COLORADO TAX PROFILE STUDY FOR 1982.

SALES TAX ALLOWANCES FOR 1986 FORM 1040 ARE ALSO PRESENTED. THESE ARE THE AVERAGES FOR SEVERAL STATES WITH A 5% RATE. SALES TAX FOR MAJOR PURCHASES SUCH AS CARS WOULD BE ADDED TO THESE AMOUNTS.

NOTE: THE FEDERAL TAX REVISIONS THAT TAKE EFFECT IN 1987 COMPLETELY DISALLOW A DEDUCTION FOR SALES TAX ON ITEMIZED RETURNS. PROPERTY TAXES ARE STILL ALLOWED AS A DEDUCTION. THEREFORE, IN THE ABOVE COMPARISON, ONE SHOULD REDUCE THE OVERALL PROPERTY TAX BURDEN BY THE TAX BENEFIT RECEIVED FROM DEDUCTING THE TAX. INDIVIDUALS IN THE $7,500 AND $12,500 CATEGORIES WOULD RECEIVE NO SUBSTANTIAL TAX BENEFIT. THOSE IN THE $17,500, $25,000 AND $35,000 CATEGORIES WOULD RECEIVE APPROXIMATELY 20% TO 23% BENEFIT. THOSE IN THE $50,000 CATEGORY WOULD RECEIVE 36% BENEFIT. NONE OF THE ABOVE WOULD PAY MORE IN SALES TAX THAN PROPERTY TAX, EVEN CONSIDERING THE INCOME TAX EFFECT.

SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87
BILL NO. Joint

CONCLUSION

From the preceding it is obvious that the property owner is better off with a sales tax than with a property tax. Obviously, businesses and agriculture are better off with no personal property tax and a one third reduction of real taxes. So if this proposal is revenue neutral, who provides the relief? The relief comes because the tax base is broadened. Non property owners, tourists and out of state purchasers of products would pay their fair share of the tax. Businesses which purchase retail products would also pay the tax. It is very difficult to estimate who, specifically, will pay the tax, but the following is a rough estimate:

	(Millions)
Resident individuals	$143
Businesses	92
Tourists & Out of state purchasers	48
Sellers of real property	20
Total	$303

Some people argue that all taxes paid by business are simply passed on to the consumer anyway. This may be, but this proposal eliminates $210 million of business related taxes and replaces them with $92 million. It would seem that the consumer comes out ahead and so does business.

TIMING AND HELP WITH BUDGET DEFICIT

The timing of the implementation of this proposal is critical. We propose that the sales tax be imposed effective July 1, 1987. Property owners receiving relief under this Plan would be required to pay their full property taxes for the first four months of 1987, only. This would be done in November, 1987. This, together with the additional income tax revenue from the loss of the property tax deduction on State returns, should contribute almost $90 million to help take care of the current budget deficit. Additionally, the payroll tax would probably not need to be imposed.

House – SENATE TAXATION
EXHIBIT NO. 7
DATE 1-19-87
BILL NO. Joint

MONTANA STATE AFL-CIO
AFL CIO
APRIL 29 1956

Box 1176, Helena, Montana

JAMES W. MURRY
EXECUTIVE SECRETARY

ZIP CODE 59624
406/442-1708

TESTIMONY OF JIM MURRY BEFORE THE SENATE-HOUSE JOINT COMMITTEE ON TAXATION, JANUARY 19, 1987.

THE FIRST QUESTION RAISED BY THIS COMMITTEE ASKS WHETHER OR NOT MONTANA'S TAX SYSTEM IS BALANCED. LET ME BEGIN BY SAYING THAT MONTANA HAS A THREE-LEGGED TAX STRUCTURE. THE FIRST LEG INCLUDES PERSONAL AND BUSINESS PROPERTY TAXES. THE SECOND LEG INCLUDES INDIVIDUAL AND CORPORATE INCOME TAXES. AND THE THIRD LEG INCLUDES OUR MINERAL AND RESOURCE TAXES.

MONTANA'S PROPERTY TAXES ARE NOT EXHORBITANTLY HIGH. IN FACT, A RECENT DEPARTMENT OF REVENUE STUDY CONCLUDES THAT MONTANA'S TAXES ON INDIVIDUALS--INCLUDING INCOME AND PROPERTY TAXES--WERE 34 PERCENT LOWER THAN THE NATIONAL AVERAGE. IN A 1984 U.S. DEPARTMENT OF HOUSING ANALYSIS, MONTANA RANKED 20TH AMONG 46 STATES SURVEYED FOR PROPERTY TAX RATES ON SINGLE FAMILY HOMES. MONTANA"S PROGRESSIVE TAX SYSTEM SUBSTANTIALLY REDUCES PROPERTY TAXES FOR LOW-INCOME GROUPS AND THE ELDERLY. CLEARLY, MONTANA IS NOT A HIGH PROPERTY TAX STATE.

LET US EXPLORE OUR ALLEGEDLY HIGH STATE INCOME TAXES. IN 1984, REVENUES FROM MONTANA'S INDIVIDUAL INCOME TAXES WERE 2.1% OF PERSONAL INCOME, WHICH GAVE US A RANKING OF 29 AMONG THE 48 STATES. IN ADDITION, FOR INCOMES UP TO $30,000 THE STATE'S INCOME TAX IS FAIRLY PROGRESSIVE. IT IS ONLY IN THE HIGHEST INCOME BRACKETS WHERE TAX RATES REMAIN FAIRLY FLAT. WE WOULD AGREE THAT THIS IS AN AREA WHERE WE COULD USE SOME TAX REFORM, SINCE THERE ARE MANY WEALTHY INDIVIDUALS WHO PAY NO INCOME TAX AT ALL. BUT, IN THE FINAL ANALYSIS, IT IS FALLACIOUS TO CONTEND THAT MONTANA'S INCOME TAXES ARE ABOVE WHAT IS CONSIDERED A "NORMAL" BURDEN.

SENATE TAXATION/House Taxation
EXHIBIT NO. 8
DATE 1-19-87
~~BILL NO.~~ Joint Hearing

THE THIRD MAJOR LEG OF OUR STATE'S TAX SYSTEM IS OUR MINERAL RESOURCES TAX. THESE ACCOUNT FOR 22.4 PERCENT OF OUR TOTAL TAX REVENUES. MUCH OF THIS BURDEN IS EXPORTED, SINCE THOSE PAYING THE TAXES ARE FOR THE MOST PART OUT OF STATE CUSTOMERS. IT SHOULD ALSO BE NOTED THAT OUR MINERAL TAX PROCEEDS APPROXIMATE THE PERCENTAGE CONTRIBUTION OF SALES TAX REVENUES IN OTHER STATES.

IN OTHER WORDS, MR. CHAIRMAN, OUR CONTENTION THAT MONTANA'S TAX SYSTEM IS A FAIRLY WELL BALANCED ONE IS ACCURATE.

THE SECOND QUESTION POSED BY THIS COMMITTEE ASKS WHAT THE IMPACTS OF ALTERNATIVE TAX POLICIES IN MONTANA WOULD BE? TO ANSWER THIS, I BELIEVE THAT WE SHOULD EXAMINE MONTANA'S PAST EXPERIENCE IN THIS AREA.

THREE MEASURES COMMONLY USED FOR GAUGING ECONOMIC GROWTH ARE GROWTH IN EMPLOYMENT, GROWTH IN PERSONAL INCOME AND GROWTH IN PER CAPITA INCOME. STARTING IN 1969, MONTANA INCREASED ITS INDIVIDUAL INCOME TAX RATES AND ADDED ON A 10 PERCENT SURTAX. IN 1971, THE SURTAX WAS INCREASED TO 40 PERCENT. IN 1973, WE LOWERED THE SURTAX TO 10 PERCENT BUT INCREASED OUR CORPORATE INCOME TAX RATES. FROM 1971 to 1975, OUR STATE'S ANNUAL GROWTH IN EMPLOYMENT WAS 2.75%, GROWTH IN PERSONAL INCOME IN REAL DOLLARS WAS 6% AND GROWTH IN PER CAPITA INCOME WAS 4.5% IN REAL DOLLARS.

WHAT WE ARE SAYING IS THAT EVEN DURING THIS PERIOD OF INCREASED LEVELS OF STATE TAXATION, MONTANA EXPERIENCED REASONABLY ROBUST RATES OF ECONOMIC GROWTH.

BEGINNING IN 1979, MONTANA BEGAN TO TAKE STEPS THAT REDUCED SEVERAL TAX RATES. DURING THAT YEAR, MONTANA EXEMPTED BANK STOCK AND SURPLUS CAPITAL FROM PROPERTY TAXATION. IN 1981, WE INCREASED INVESTMENT TAX CREDITS FROM 20 PERCENT OF FEDERAL LEVELS TO 30 PERCENT OF FEDERAL LEVELS, AND ADOPTED

FEDERAL ACRS PROVISIONS. IN ADDITION, OUR LEGISLATURE EXEMPTED BUSINESS INVENTORIES FROM THE TAX BASE AND REPEALED OUR STATE INCOME TAX SURTAX.

LET US RETURN TO OUR MEASURES OF ECONOMIC GROWTH. FROM 1981 TO 1985 OUR ANNUAL GROWTH IN EMPLOYMENT WAS 1.25 PERCENT, GROWTH IN PERSONAL INCOME WAS 1.175 PERCENT AND PERCAPITA INCOME GREW AT A MINISCULE .25 PERCENT. IN OTHER WORDS, THERE WAS A VERY SLOW, ALMOST STAGNATE PERIOD OF GROWTH BETWEEN 1981 and 1985. JUST THE OPPOSITE OF WHAT OCCURRED IN THE EARLY 1970's.

MR. CHAIRMAN, WE ARE NOT CONTENDING THAT INCREASING TAXES STIMULATES ECONOMIC GROWTH. BUT WE DO BELIEVE THAT THE CONVERSE IS ALSO NOT NECESSARILY TRUE: THAT LOWERING TAX RATES DOES NOT NECESSARILY LEAD TO ECONOMIC DEVELOPMENT. THE RELATIONSHIP BETWEEN ECONOMIC DEVELOPMENT AND TAXATION IS MUCH MORE COMPLEX THAN CERTAIN BUSINESS LOBBYING GROUPS WOULD HAVE US BELIEVE.

THE FINAL QUESTION POSED BY THIS COMMITTEE IS WHETHER OR NOT MONTANA NEEDS TO CHANGE ITS OVERALL TAX SYSTEM? THERE IS NO QUESTION THAT MONTANA'S ECONOMY IS IN TOUGH SHAPE, BUT SOMEHOW THE DEBATE HAS BEEN STRUCTURED SO THAT WE THINK THAT WE ARE UNIQUE IN OUR ECONOMIC DILEMNA.

IN FACT, MR. CHAIRMAN, MONTANA IS ONLY ONE OF THIRTY-ONE STATES, HOLDING HALF THE POPULATION OF THIS COUNTRY, THAT ARE ON THE BRINK OF ECONOMIC COLLAPSE. THESE STATES HAVE A MYRIAD OF DIFFERING TAX SYSTEMS, FROM HIGH LEVELS OF SALES TAXES TO ALL SORTS OF EXTENSIVE BUSINESS TAX INCENTIVES.

THE REASONS FOR THEIR PROBLEMS ARE NOT THE RESULTS OF THEIR METHODS OF STATE TAXATION, BUT ARE THE RESULTS OF THE FAILED NATIONAL ECONOMIC AND TRADE POLICIES.

TWENTY-ONE STATES HAVE CUT OR HAVE ANNOUNCED PLANS TO CUT THEIR BUDGETS FOR FISCAL 1987. ACCORDING TO GERALD R. MILLER, EXECUTIVE DIRECTOR OF THE NATIONAL ASSOCIATION OF STATE BUDGETS, "THE (NATIONAL) ECONOMY IS BATTERING

SENATE TAXATION
EXHIBIT NO. 8
DATE 1-19-87
BILL NO.

STATE'S BUDGETS WITH HURRICANE FORCE." IN THE FOURTH QUARTER OF THIS YEAR, ONE-THIRD OUR STATES ACTUALLY SAW A DECLINE IN PERSONAL INCOME. (MONTANA'S PERSONAL INCOME RATE FELL BY 4.6 PERCENT)

IT IS EASY TO PLACE THE BLAME ON WASHINGTON, BUT THE REALITY OF THE SITUATION IS THAT YOU AS LEGISLATORS WILL HAVE TO COME TO GRIPS WITH OUR REVENUE SHORTFALLS. WHEN GRAPPLING WITH THESE URGENT PROBLEMS, WE URGE YOU TO ARRIVE AT PROGRESSIVE RATHER THAN REGRESSIVE SOLUTIONS.

A SALES TAX HAS BEEN PROPOSED BY MANY AS A SOLUTION TO OUR PROBLEMS. BUT THE FACT IS THAT SALES TAXES ARE BY THEIR VERY NATURE REGRESSIVE, PLACING THE GREATEST BURDEN ON THOSE AT THE BOTTOM RUNGS OF THE ECONOMIC LADDER. FAMILY FARMERS, MAINSTREET BUSINESSES, WORKING MEN AND WOMEN, THE POOR, SENIOR CITIZENS AND OTHERS ON FIXED INCOMES ARE LOCKED IN A DESPERATE STRUGGLE FOR SURVIVAL. A SALES TAX IS A BURDEN THAT FEW CAN AFFORD TO BEAR.

A SALES TAX HAS ALSO BEEN BANDIED ABOUT AS A MEANS OF PROPERTY TAX RELIEF. BUT IF ONE EXAMINES THE FACTS, EVEN WITH SUBSTANTIAL REDUCTIONS IN PROPERTY TAX RATES, A SALES TAX WOULD PLACE AN ADDITIONAL BURDEN ON A MAJORITY OF MONTANA'S CITIZENS.

TO GIVE YOU AN EXAMPLE: AN AVERAGE MISSOULA HOMEOWNER WITH A $50,000 HOME AND A FAMILY OF FOUR PAID $475 DOLLARS IN PROPERTY TAXES IN 1985. BY REDUCING HIS PROPERTY TAXES 30%, THE HOMEOWNER WILL SAVE $143. BUT WITH A 5% SALES TAX, THE HOMEOWNER WILL PAY APPROXIMATELY $696 PER YEAR IN SALES TAXES. THIS WOULD RESULT IN AN OVERALL TAX INCREASE FOR THE HOMEOWNER FOR $533 PER YEAR. A SALES TAX WOULD NOT RELIEVE THE TAX BURDEN FOR A MAJORITY OF MONTANANS.

MONTANA'S BUDGET DEFICITS ARE CRYING OUT FOR TAX REFORM, BUT REGRESSIVE TAXES ARE NOT THE ANSWER. OUR LABOR FEDERATION URGES YOU TO CONSIDER PROGRESSIVE TAX CHANGES THAT ARE BASED UPON A PERSON'S ABILITY TO PAY.

SENATE TAXATION
EXHIBIT NO. 8
DATE 1-19-87

TO QUOTE DAN ROSTENKOWSKI, CHAIRMAN OF THE U.S. HOUSE TAXATION COMMITTEE, "THIS COUNTRY IS NOT UNWILLING TO PAY HIGHER TAXES--AS LONG AS THEY ARE FAIR. IF WE NEED MORE MONEY FOR GOVERNMENT, THEN LET'S GO THROUGH THE FRONT DOOR AND COLLECT IT FROM THOSE WHO CAN PAY--NOT THROUGH THE BACK FROM THOSE WHO CAN'T."

SENATE TAXATION
EXHIBIT NO. 8
DATE 1-19-87
BILL NO.

POSITION PAPER OF THE MAKE MONTANA COMPETITIVE COMMITTEE

Montana Coal Council
Montana Wood Products Association
Montana Automobile Dealers Association
Montana Taxpayers Association
Montana Chamber of Commerce
Montana Stockgrowers Association
Montana Bankers Association
Montana Motor Carriers Association
Western Environmental Trade Association
Montana Mining Association
Montana Association of Realtors
Montana Cattlewomen Association
Montana Petroleum Association
Montana Wool Growers Association

January 16, 1987

House/ SENATE TAXATION
EXHIBIT NO. 9
DATE 1-19-87
~~BILL NO.~~ Joint Hearing

The foundation of Montana's economy is its natural resources. All of Montana's wealth--coal, hardrock minerals, oil and gas, timber, grain and red meat--comes from Mother Earth.

In the decade of the 1980's, several studies have confirmed this. Recommendations have been made to provide incentives for the development of Montana's natural resources. However, no significant incentives have been taken to make Montana's natural resources competitive with those in other states and, thus, the worldwide marketplace. The result has been economic stagnation.

As the Montana Legislature celebrates its Golden Anniversary in 1987, the time has come to renew this state's commitment to provide jobs for its citizens through the careful development of its natural resources without detracting from its natural beauty.

Every major study that has been completed in recent years has pointed out that Montana's economy lags behind those in neighboring states. They cite several reasons for this:

1) Taxes on natural resource production and the property necessary to stimulate production in Montana are among the highest, if not the highest, in the nation. This has resulted in a paradoxical situation: Because of the reliance of state and local government on natural resource taxes, production has lagged partly because of the inequitable tax burden natural resource industries in Montana are expected to carry.

2) Montana has an anti-business image primarily because its environmental laws and regulations are among the most stringent in the nation. In the areas of environmental and tax policy, executive agencies have used the Administrative Procedures Act to expand authority given them by the Legislature. This has resulted, whether real or perceived, in Montana's anti-business image.

3) Because of "boom" periods in the collection of natural resource taxes, state and local governments have splurged in spending for social programs and education. In addition, too little money has been spent on improvements of Montana's communication and transportation infrastructure. Montana ranks 40th in the nation in per capita income, yet stands 4th in the nation in its spending for education and social programs. According to a study prepared in 1986 for Montana Forward, state and local spending would have to be reduced by $200 million a year to bring Montana's spending in line with its income.

SENATE TAXATION
EXHIBIT NO. 9
DATE 1-19-87
BILL NO.

As far back as 1982, the McKinsey Report--commissioned by the Montana International Trade Commission--made several recommendations aimed at spurring production and correcting Montana's anti-business perception. Among its suggestions were five year moratoriums on increases in severance taxes and environmental regulations. In addition, the report advised that administrative agencies, when promulgating regulations, should prepare economic impact statements on how those regulations would affect the economy in general. Another of its recommendations was passage of an Equal Access to Justice Statute, which would allow parties injured by inappropriate administrative rules to seek damages.

Although these recommendations never were adopted, one proposal--creation of a Governor's Council on the Economy--was accomplished. Born in 1983 and consisting of diverse segments of Montana's population, the Governor's Council on Economic Development, proposed many ways to enhance economic activity in Montana. Among its suggestions was initiation of a 5-year development strategy for Montana's natural resources, including a probe of the negative affects of severance taxes and environmental regulation on natural resource industries. None of the Council's major recommendations, thus far, have been implemented.

The latest recommendations were made in 1986 by the Economic Transition Task Force, a group appointed by Gov. Ted Schwinden; and the Montana Forward Coalition, a group of eastern Montana businessmen, who commissioned a study completed by Miller and Associates of Olympia, Washington. Also in 1986, a "white paper"--The Montana Economy: Reality and Perception--was prepared for the Montana Joint Council on Economic Education. All three documents cited many of the same problems that had been acknowledged in previous studies: An over-reliance on severance and personal property taxes; a lack of tax incentives to attract new business or encourage expansion; high workers compensation rates; and an anti-business perception in taxation and environmental policy.

Two elements that have been missing in these studies are a lack of dynamic action and the absence of a unified approach to correct the problems. Recognizing this, the Make Montana Competitive Committee was formed in late December to provide a united effort.

The Committee has made the following recommendations for action by the 50th session of the Montana Legislature:

SENATE TAXATION
EXHIBIT NO. 9
DATE 1-19-87

1) Equalization of Montana's discriminatory taxes on personal property. Personal property now is taxed at various rates, ranging from 16 to 11 percent of valuation, which are among the highest rates on property tax schedules. Besides being arbitrarily administered, the rates penalize dynamic, capital intensive industries and tend to discourage development of Montana's natural resources and the creation of jobs. To bring personal property in line with other property in Montana the rates should be consistently reduced to 4 percent.

2) Adjustments should be made in Montana's severance taxes on coal, nonfuel minerals and oil and gas. The Montana Legislature has stagnated production in its zeal to receive compensation for the loss of its natural resources. In fact, the 30 percent coal severance tax was passed specifically to discourage development. In the latter case, the severance tax policy of the 1970's has accomplished its intended purpose. However, because social and environmental fears of extractive development have never been realized, the time has come to place severance taxes in line with those in other states. Specific recommendations have been made to accomplish this purpose by the trade associations representing these industries.

3) Livestock and grain inventories should be treated as business inventories. In 1981, the tax on business inventories was eliminated, but Montana continues to tax livestock and grain inventories. Livestock, is not taxed in any of Montana's surrounding states. This slows the development of a strong commercial cattle feeding industry because of the competitive advantage held by neighboring states. Montana, with its availability of quality feeder cattle and grain, could expand its feeding potential, thereby making full use of two commodities in large supply if this competitive disadvantage were eliminated.

4) Passage of a tax incentive that will encourage the birth of new dynamic industry and the expansion of existing development. Although Montana has several tax incentives on the books, they lack the teeth to inspire new capital investment or expansion in Montana's basic industries. In 1985, House Bill 122 was introduced. Under the legislation, new or expanding developments that met certain conditions would have been taxed at 50 percent of their valuation for the first five years with the valuation increasing 10 percent each year thereafter until full appraisal would be obtained after the 10th year. The measure won widespread, bipartisan support in the House, but was tabled in the Senate Taxation Committee. Similar legislation should be introduced in and passed by the

SENATE TAXATION
EXHIBIT NO. 9
DATE 1-19-87
BILL NO.

1987 Legislature. The incentive should be at local option in the event that a local government may consider it discriminatory to existing business. It also should make clear that existing revenue will not be affected.

5) <u>The Administrative Procedures Act should be changed so that the Legislature has more control over rules promulgated by administrative agencies.</u> In theory, the Legislature passes the general framework for public policy while the finishing touches are applied by administrators in agencies charged with their enforcement. In reality, rules have expanded the authority of bureaucratic agencies leading to many differences of opinion over legislative intent. This has contributed to Montana's anti-business perception and an inconsistent public policy. As a result, outside investors are reluctant to come to Montana because the rules of the game either are unclear or discouraging. The Legislature should be given more authority to require administrative agencies to follow legislative intent.

6) <u>Liability insurance should be more available.</u> The rash of lawsuits and liberal awards have made liability insurance for business either extremely expensive or unattainable. passage of Initiative 30 by voters in 1986 will make it possible for the legislature to reform Montana's tort system so that persons who are harmed can be compensated adequately. At the same time, damages should be limited to reflect the actual harm experienced by the injured party. This can be accomplished by limiting punitive damages; bad faith claims; wrongful discharge suits, and enacting other major tort reform.

7) <u>Workers Compensation rates must be reduced.</u> In recent years, lump-sum settlements and generous awards arrived at through litigation have resulted in multi-million dollar deficits in Montana's Worker Compensation Fund. Rates for businesses have skyrocketed. Montana's rates are seventy times higher than in other states. Stricter requirements must be placed on awards so that rates are more affordable. Lump-sum settlements should be modified. Benefits must be made more dependable so that litigation will be reduced, and a limit should be placed on the length of time benefits are received by the claimants. The deficit must be eliminated without placing an additional burden on employers.

8) <u>Montana's unitary tax must be amended to "waters edge."</u> Montana is one of three states that currently imposes this worldwide combination method to tax corporations. This discourages investment in Montana. This method of taxation in Montana should be repealed.

House/ SENATE TAXATION
EXHIBIT NO. 9
DATE 1-19-87
BILL NO.

9) Spending by state and local governments must more accurately reflect income. Montana's spending is not in line with its income. Spending for education and social programs are not in balance with its ability to pay. Spending for education and social programs must be reduced until the equation is reached between expenditures and income and some of the money should be channeled into improving Montana's infrastructure to enhance commerce.

Conclusion: Montana is dependent on its traditional industries and will continue to rely on them to maintain or improve its standard of living. Disincentives, rather than incentives, have been built into Montana's tax system. This has contributed to the cost of conducting business. Montana's "anti-business" perception has been caused by the promulgation of regulations that have expanded the intent of legislation primarily in environmental and taxation policy. Finally, Montana does not live within its income.

It is imperative that these problems be addressed by the 50th Legislative Assembly. Unless Montana's basic industries are allowed to grow and prosper, the economy will continue to stagnate and its citizens will not enjoy the standard of living that traditional industries have provided in the past.

Exh #10

Jody - Taxation
Committee House
will furnish

Senate Finance and Claims Committee Action:

1. General Fund for District State Veterinarians Work on Rabies

The general fund appropriation for the rabies control program is increased $34,481 per year to pay salaries, mileage and per diem for district state veterinarians. These costs had previously been absorbed from livestock mill levies. This provides for the equivalent of 1.2 FTE costing $49,995 and $4,486 for mileage and per diem while working on rabies problems.

COLUMBIA FALLS ALUMINUM COMPANY

POSITION PAPER - MONTANA TAX SYSTEM

Presented To The Joint House/Senate Hearing On The State Of Taxes In Montana

January 19, 1987 - 7:00 P.M.

House/ SENATE TAXATION
EXHIBIT NO. 11
DATE 1-19-87
BILL NO. Joint Hearing

INTRODUCTION AND BACKGROUND:

My name is Gary Saurey, CPA, Tax Coordinator for Columbia Falls Aluminum Company. I was recently a partner in a CPA firm in Kalispell and Whitefish, with ten years of experience in tax practice.

Columbia Falls Aluminum Company (CFAC) has been operating the aluminum reduction plant purchased in September, 1985, from Atlantic Richfield Company (ARCO). ARCO avoided a costly shutdown and was able to receive full value for its remaining inventories. Since then, the plant has been able to continue in operation by negotiating a variable power rate structure that provides for rate relief at depressed aluminum prices in exchange for higher rates at robust aluminum prices. In addition, we have negotiated lower transportation rates, substantially reduced wages and benefits, and trimmed the workforce from nearly 1,000 to less than 800 employees. At the same time, we have increased production and operating efficiencies to enable us to remain marginally competitive. Our product recently has been exported to Japan, a positive contribution to the U.S. trade deficit. None of this would have been possible without tremendous support from the community-based "People For Jobs" coalition, the Governor, the Montana

Congressional Delegation, and local politicians. In addition, the employees and the local union have been extremely helpful. Throughout, however, the new owners have continued to be concerned over the high corporate and property taxes in Montana. In fact, the only substantial part of the plan to keep the plant operating that has not been realized to-date is a reduction in our highest fixed cost, property taxes.

Even though the assets of the plant were purchased for $1 from ARCO, the Montana Department of Revenue has appraised them at $148 million, resulting in a 1986 tax bill of $2.4 million. To illustrate the outrageous nature of this appraisal, a plant in Goldendale, Washington with 2/3 of our capacity recently announced shutdown after the final potential buyer refused to pay approximately $19 million for it. There are eight other operating reduction plants in the Northwest who pay an average of $742,000 in annual property and other fixed taxes. When calculated in terms of the amount of aluminum produced each year, CFAC pays 2 1/2 times more in fixed taxes per ton of capacity than the other operating plants. This places CFAC at a distinct competitive disadvantage.

In 1985, ARCO paid less than $20,000 in Montana corporate income tax. If we are able to fully achieve our business plan, CFAC will pay several millions of dollars of Montana corporate income taxes over the next three years. Contrast that with the fact that our competitors in Washington state are not subject to corporate income taxes.

SENATE TAXATION
EXHIBIT NO. 11
DATE 1-19-87
BILL NO. ____

DISCUSSION:

Specific areas we feel are wrong with the Montana property tax system include:

1. It is a fixed tax. It would apply even were we producing at less than full capacity. Although presently we are at 100% of capacity, we have only two customers, utilizing 60% and 40% of our capacity respectively. Losing one of these customers and facing such a large fixed cost would place us in a very difficult situation.

2. Montana's system places the most productive assets, such as those used in mining and manufacturing, in classifications subject to higher rates of tax. New equipment purchased by CFAC is subject to an annual rate of tax of approximately 3% of value. Because of the Department of Revenue's trending and depreciation factors, the annual tax on 15-year-old equipment remains at approximately 1 3/4% of original cost. Contrast this with the approximately 1% annual tax on the value of real property. Other states have capped the property tax rates at from 1% to 1 1/2%. These factors alone exhibit an "anti-business" reality in Montana that is not being currently addressed.

3. Montana's system is complicated and difficult to administer. In 1981, we had 11 classifications of taxable properties. Four years later, there were 19 different classifications. Similarly, the list of exempt property is rapidly expanding.

SENATE TAXATION
EXHIBIT NO. 11
DATE 1-19-87
BILL NO.

4. Montana's Department of Revenue seems to be administratively extending some of the concepts behind the property tax law. In a recent informal meeting with certain Department personnel relating to the appraisal of CFAC's property, we were quite surprised by their apparent desire to determine a tax based upon the value of its use to us. This is in direct conflict with the market value standard of the Montana statute. Furthermore, Department people at the meeting expressed the feeling that our property taxes were a low percentage of our total revenues and if we were even marginally profitable, we should have no problem paying the property tax as assessed. This displays an ignorance of the realities of the high risk and volatile aluminum business or any worldwide commodity business where thin margins are rapidly consumed by fixed costs. It also indicates an extension of the "ability to pay" concept to the property tax area. Taxing business and individuals according to their "ability to pay" is taken care of through the income tax system; this concept should be abandoned with respect to property taxation.

Specific areas we feel are wrong with the Montana corporate income tax system are:

1. The unitary tax. It is complicated and is difficult and expensive to comply with and administer. The "anti-business" perception that results is not worth the amount of tax that is collected. Montana and three other states stand conspicuously alone in persisting with this tax system. Furthermore, although Montana purportedly follows federal law, the Department of Revenue has taken the position that Montana

SENATE TAXATION
EXHIBIT NO. 11
DATE 1-19-87
BILL NO.

will not allow the benefits available to foreign sales corporations designed to encourage exports.

2. Relative to nearby states, our corporate rates are high. South Dakota, Wyoming and Washington do not impose any corporate income taxes. Most of our northwest competitors in the aluminum business are based in Washington and pay no corporate income tax.

3. Montana lacks incentives for new business. Where they do exist, they are very restrictive as to the application to real Montana situations. For example, although we are clearly a new business, we would have had to have shut down for three years in order to realize any property tax reduction.

RECOMMENDATIONS:

Destroy the "anti-business" perception by repealing the unitary tax and reducing all tax rates including property, income, and severance. Do not "back into" tax increases due to the windfall from federal tax reform to balance the budget. Instead, follow the example of businesses such as ours and reduce spending, make substantial cuts and live within a budget. Become competitive with nearby states by reducing the tax burden. Consider tax and other incentives to attract and keep business. However, if tax rates and government spending are lowered, such incentives may be unnecessary.

SENATE TAXATION
EXHIBIT NO. 11
DATE 1-19-87
BILL NO.

SUMMARY:

The employees of CFAC took 15% wage and benefit cuts. Some jobs were sacrificed. Bonneville Power Administration offered a variable rate to the Northwest Aluminum Industry to keep us in business. Burlington Northern offered lower freight rates to avoid losing a major customer. Other vendors were similarly cooperative.

We are asking only that you allow us to continue to do business and contribute to the State's economy by adopting a fair and equitable tax system.

MONTANA PETROLEUM ASSOCIATION
A Division of the
Rocky Mountain Oil and Gas Association

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2030 11th Avenue, Suite 23
Helena, Montana 59601
(406) 442-7582

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The Grand Building, Suite 501
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Janelle K. Fallan
Executive Director

Joint Meeting
House and Senate Taxation Committees
January 19, 1987

Presented by
Janelle Fallan, Executive Director
Montana Petroleum Association

The debate over whether or not Montana is a high tax state can be skipped on the question of oil and gas taxation, because Montana has, on average, the highest petroleum taxes in the nation. Louisiana has a higher severance tax but exempts oil and gas from property taxation (Montana's net proceeds tax is, on average, higher and more burdensome than the severance tax). Colorado levies the same severance tax but offers a generous tax credit on local property taxes. New Mexico, Utah and Wyoming levy lower taxes than Montana across the board. North Dakota and Wyoming are also working on serious tax incentives for oil and gas in their legislative sessions.

As the price of oil and gas have fallen -- crude oil experienced a 50% drop in 1986 -- the impact of being a high tax state will become more evident.

Taxes have a greater impact on development as value declines. Under favorable conditions, the difference in value of a project between high and low tax states can be as much as 30%. Under unfavorable conditions, high taxes will wipe out 100% of potential returns. The rising oil prices of the 1970s and early '80s masked the economic consequences of state taxes to a large degree. As the value of oil rose, the attractiveness of oil investment increased everywhere, regardless of how much of the incremental gain would be taken by states. As a result of 1986 however, the negative impact of high state taxes cannot be ignored.

During this session, we will be before both taxation committees with some tax incentives for new production. We do not believe this is a total solution, as it will not result in a lower overall tax rate for Montana. On the other hand, we hope you will appreciate that we do not see this as the session likely to approve lower tax rates. We do believe that 24-month holidays from the severance and net proceeds taxes would stimulate

House SENATE TAXATION
EXHIBIT NO. 12
DATE 1-19-87
BILL NO. Joint Hearing

investment in the state and will protect the state and local tax base. Passage of such measures would not represent a handout, but rather a recognition of the negative impact of being a high-tax state.

Oil production in Montana is currently at a 30-year low. Employment has fallen severly, in an industry in which the average salary is $26,000. The highest year for production was 1968, when the price of oil was $2.57. That was the year the Powder River Basin came into production, and would seem to indicate that what drives production, and therefore employment, is not so much the price of oil as exploration.

There is no question that unless producers receive a price allowing return on their investment, there will be little exploration. But the price received in Montana will not be that different from the price received in Wyoming and North Dakota. Those who are looking for oil will have been tempered by the industry's worst year ever, in 1986, and will probably take a more careful look than they did in the past as to which states offer better opportunities.

The 1985 Legislature did pass important oil and gas legislation. Some measures you approved last session actually brought new investment into the state. But the severe downturn last year helped to underscore how much more work Montana has ahead.

In September, many of you attended a taxation forum conducted by the University of Montana and Montana State University. I would like to quote briefly from one of the papers presented at that conference: The current and likely future conditions in the oil and gas market will force Montanans to reconsider their tax policy toward the industry. The "oil bust" has reduced the margin between prices and extraction costs, which in turn raises the degree of full taxation on investment in oil and gas. Unless the state re-focuses its attention on nurturing the further development of the industry, Montana may find that it has maintained high tax rates which yield little long term revenue for state and local governments.

SENATE TAXATION
EXHIBIT NO. 12
DATE 1-19-87
BILL NO. ______

MONTANA PETROLEUM FACT SHEET

PRODUCTION

CY	Bbls.	Gross Value	MCF	Gross Value	Total Wells Drilled
1978	30,934,923	$ 277,737,502	44,615,198	37,342,921	778
1979	30,285,631	362,239,259	50,691,868	60,931,625	822
1980	29,927,468	626,154,711	48,928,608	70,261,481	902
1981	30,517,947	1,052,333,907	44,800,000	85,120,000	1289
1982	30,937,514	963,428,800	50,932,000	107,109,990	816
1983	29,320,418	842,681,933	41,203,000	99,010,809	511
1984	30,668,305	845,919,776	48,499,939	120,949,800	819
1985	29,770,000	808,553,200	44,330,000	98,772,380	592
1986	27,045,000	371,436,030	44,016,000	86,799,552	348

	OIL WELLHEAD PRICE: $/BBL	PRODUCING OIL WELLS	NATURAL GAS PRICE: $/MCF	PRODUCING GAS WELLS	EXTRACTION EMPLOYMENT	SEISMIC CREW MONTHS
1973	3.843	3536	.162	1118	1523	62
1974	6.814	3028	.257	1184	1861	155
1975	7.845	3150	.394	1232	1810	40
1976	8.411	3310	.441	1950	2084	85
1977	8.582	3354	.735	1490	2357	57
1978	9.253	3275	.837	1377	2789	155
1979	12.279	3573	1.202	1881	3383	135
1980	22.250	3628	1.436	2150	4636	202
1981	34.317	3968	1.900	2142	6852	388
1982	31.311	4311	2.103	2069	5482	224
1983	28.804	4675	2.403	2043	3760	156
1984	28.066	4201	2.512	2088	4293	125
1985	25.214	4196	2.329	2033	3357	43
1986	13.734	4036 (est.)	1.972	2006 (est.)	na	na

TAXES

Montana imposes four taxes on oil and natural gas:

A. Severance tax is currently 5% of the gross value of oil and 2.65% for natural gas.

The revenue is allocated as follows:

1) One-third of the oil severance tax to Local Government Block Grant account for distribution to all Montana cities and counties.

2) A portion of the collections is returned to cities and counties in the oil-producing areas to help them in dealing with impacts. The portion returned varies according to the new production in each county:

FY	OIL	NATURAL GAS
1981	$ 992,488	na
1982	1,644,112	183,789
1983	4,353,485	206,759
1984	1,422,335	509,260
1985	3,087,474	104,910
1986	475,922	106,915

SENATE TAXATION
EXHIBIT NO. 12
DATE 1-19-87
BILL NO.

3) The remainder to the state general fund.

The tax rate for incremental oil produced through tertiary recovery after July 1, 1985, is 2.5%.

B. Net Proceeds Tax is calculated on gross value of oil, minus all allowable deductions multiplied by the local mill levy. The 1985 Legislature set a 7% maximum on oil and a 12% maximum on gas produced after July 1, 1985, from leases which have not produced during the preceding five years. Therefore, the maximum tax rate on "new" production from a previously non-producing lease will be 12.7% on oil and 15.35% on gas.

C. Resource Indemnity Trust Tax is .5% of gross value of all minerals produced. These taxes are placed in a trust fund to "indemnify the state against damage to the environment from the extraction of non-renewable natural resources." Interest from the trust is appropriated for projects "to improve the total environment and rectify damages thereto."

	SEVERANCE TAX		NET PROCEEDS TAX		RESOURCE INDEMNITY TRUST TAX	
FY	OIL	NATURAL GAS	OIL	NATURAL GAS	OIL	NATURAL GAS
1980	$10,544,555	$1,264,025	$21,011,951	na	$1,828,947	$355,054
1981	19,578,172	2,116,291	28,663,376	na	3,328,426	419,647
1982	51,073,425	2,659,811	40,868,506	na	5,308,525	491,832
1983	45,228,535	2,649,726	66,160,884	na	4,783,438	522,396
1984	49,029,017	2,797,996	65,610,580	$11,976,791	4,279,714	589,348
1985	48,789,984	2,945,778	60,819,000	14,220,000	4,204,763	627,504
1986	34,728,749	2,890,666	67,220,584	14,771,771	3,913,955	583,961

D. Conservation Tax: The Board of Oil and Gas Conservation levies a tax to support its own operations. The tax is .2% of gross value. It yielded $753,000 in FY 1985 and $631,000 in FY 1986.

On the average, local governments spend 60% of these funds for education, 8% for city operations, 23% for county operations, and 6% for fire and other special districts. About 3% is returned to the state to support the university system.

Information compiled January, 1987, from:

Montana Department of Revenue annual reports
Governor's Budget Office reports
Montana Oil and Gas annual reviews
"The Petroleum Industry in Your State," Independent Petroleum Association of America

Compiled by: Montana Petroleum Association
Helena, Montana
442-7582

SENATE TAXATION
EXHIBIT NO. 12
DATE 1-19-87
BILL NO.

MONTANA PETROLEUM TAXES

TAX	RATE	FY1986
To the state:		
(1) severance tax		
oil	5%	$23,152,504
natural gas	2.65%	2,890,666
(2) resource indemnity trust tax	.5%	
oil		3,913,955
natural gas		583,961
(3) oil/gas conservation tax	.2%	629,287
(4) corporate license tax	6.75%	6,553,610*
Lease royalty from state lands		
oil		4,193,476
natural gas		1,248,139
Bonuses and rentals on state lands		4,950,779
To local government:		
(1) net proceeds tax		
oil	(ave. 7%)	67,220,584
natural gas	(ave. 12%)	14,771,771
(2) ad valorem property tax on plant and equipment	11%	not available
(3) one-third of the oil severance tax plus the amount by which any tax collected within a county exceeds collections in the county from the previous year by reason of increased production.		11,576,246
oil		475,922
gas		106,915

Does not include: income from federal leases
income taxes on royalty income:
paid by individuals
and corporations

*FY 1985 figure -- FY 1986 not available

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SENATE TAXATION
EXHIBIT NO. 12
DATE 1-19-87
BILL NO. Joint Hearing

'WESTERN ENVIRONMENTAL/ TRADE ASSN.
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TX

House- SENATE TAXATION
EXHIBIT NO. 13
DATE 1-19-87
BILL NO. Joint Hearing

TESTIMONY BEFORE THE SENATE AND HOUSE TAXATION COMMITTEES

January 19, 1987

Much has been written and said over the past few years regarding Montana's taxes and tax reform in our State. The terms have a variety of meanings, depending on who is using them. This debate has a number of issues that include among others, whether Montana is a high tax State or not; whether our tax system is fair and equitable; and whether the level of spending in Montana is in line with the level of revenues collected.

Two issues should quickly be set aside. One is perfectly clear. The people of Montana have expressed very strongly the need for a reduction in property taxes.

Second, there is no useful purpose served in debating the issue of Montana being a high tax State. The perception of individuals and business outside and within our State is that we are a high tax State. Whether Montana is a high tax state or not is irrelevant as people perceive it as such. Recognizing and accepting these two statements, we then should direct our collective attention to the other important issues.

Montana has been unable or unwilling to adjust its spending patterns in keeping with the revenues received. At a time when Montana enjoyed high revenues, particularly from natural resource taxes, a number of spending programs were authorized to meet the wishes of individuals and groups. But declined revenues have resulted in only minimal cuts occurring in programs.

It is unwise to continually enact across the board cuts in state budgets as essential services soon become jeopardized. Montana must establish priorities in all services, including education, and fund those services at levels that will make Montana competitive. The difficult, but necessary action, is to permanently curtail those programs not determined as a having a high essential and necessary priority.

Over the years, Montana has acquired an overbuilt government system. We can no longer view ourselves in this large geographic area attempting to provide a wide variety of services to a small population. It is time that we view ourselves as a city with a population of 800,000 people. Then we should ask the questions "Do we really want or need 183 separate governmental jurisdictions with over 600 elected officials," or do we need over 500 separate school districts; and do we need 6 separate units of the university system within our city. These are difficult issues to resolve but must necessarily be addressed.

EXHIBIT
DATE 1-19-87
HB

The Montana tax system must be reviewed to insure that it not only is fair and equitable, but broad based. We all know the fairest tax is one that someone else pays. But if Montana is to be competitive in attracting jobs to our State, then the tax system must also reflect a competitive spirit.

The people believe there has been too much reliance on the property tax. Studies indicate that Montana has been overly dependent on natural resource taxes.

In addressing these issues, the Montana Legislature will be faced with some difficult decisions to fund essential services. Whatever the decision, be it consideration of adjustments in the income tax or a sales tax, the decisions should be made and action taken at this time rather than postponing any decision until 1988. I would prefer this elected body to make such a decision, but if it is the direction of the Legislature to call for a vote by the people, then such a vote should be immediately upon the conclusion of this Legislature.

Montana's citizens recognize that you have some difficult choices to make this year. If you make those choices rather than delaying your actions, Montana will accept them as necessary to meet our present needs and provide for our economic future.

CROW TRIBAL COUNCIL

P.O. Box 159
Crow Agency, MT 59022

RICHARD REAL BIRD, Chairman
JEROME HUGS, Vice Chairman
TRUMAN C. JEFFERSON, Secretary
CARLTON NOMEE, SR., Vice Secretary
Crow Country

Crow Country

Montana State Legislature
Capitol Building
Helena, Montana 59601

Attn: Joint Senate and House
Committee on Taxation

Dear Members:

The Montana State Severence Tax is of major concern to the Crow Tribe.

In view of the soft market that we are experiencing, the Montana Severence Tax makes the feasibility of marketing Coal from the Absaloka Mine on Sarpy Creek much more difficult. This drastically effects the economical condition of the tribe as disruptive to our revenue flow.

On behalf of the Crow Tribe, I am encouraging you to give consideration to lowering the Montana Severence Tax equal to or lower than that of Wyoming's.

Sincerely,

Richard Real Bird
Crow Tribal Chairman
Crow Tribal Council

RRB/bms

cc: file

House / SENATE TAXATION
EXHIBIT NO. 14
DATE 1-19-87
BILL NO. Joint Hearing

RETHINKING MONTANA'S TAX SYSTEM

POSSIBILITIES FOR REFORM

A CONFERENCE SPONSORED BY

MONTANA COUNCIL ON ECONOMIC EDUCATION

AND

CENTER FOR POLITICAL ECONOMY AND NATURAL RESOURCES

MONTANA STATE UNIVERSITY

House
SENATE TAXATION
EXHIBIT NO. 15
DATE 1-19-87
BILL NO. Joint Hearing