

MINUTES OF THE MEETING
TAXATION COMMITTEE
MONTANA STATE SENATE

February 24, 1987

The thirty-first meeting of the Senate Taxation Committee was called to order at 8:00 A.M. on February 24, 1987 by Chairman George McCallum in Room 325 of the Capitol Building.

ROLL CALL: All committee members were present.

FURTHER CONSIDERATION OF SB 307: Senator McCallum opened the hearing for Gary Carlson, from the Montana Society of CPA's, to furnish information from their data base.

Gary Carlson, Montana Society of CPA's, furnished additional information to the committee from their data base. The summary of his comments and packet of information are attached as Exhibit 1. Patrick Hanley, Montana Society of CPA's, assisted Mr. Carlson in his presentation. Also enclosed as Exhibit 1, is additional information furnished from the CPA's and a summary of their concerns with SB 307.

QUESTIONS FROM THE COMMITTEE: Senator Mazurek referred to the graph which showed the percentage increase in 1988 federal taxes compared to 1985 taxes paid and it shows a dramatic increase in the two lower brackets. He asked Mr. Carlson if that was because of the loss of shelter write-offs.

Gary Carlson said be sure you use the percentage graph in relation to the average dollar graph. You can see the effect on the average dollar is \$283. That is the increase in tax. The percentage increases are very dramatic and that has got to be because of the attributes of the returns that we have in our data base, which we caution you does not represent the average low income person in the state of Montana. Capital gains, loss of passive losses, limitations on itemized deductions, would cause that percentage to move dramatically.

Senator Mazurek said the taxpayers that you have selected, the reason they are in the 0-10 and now will have an increase, is because they have had deductions that have reduced their preferential treatment. He wonders why they are down in that category.

Gary Carlson said it is the real possibility of capital gains, deduction exclusion, passive losses, limitations on itemized deductions, offset by increases in exemptions. We point that out. They are not your normal \$6,000 a year wage earner. They are people who are in business and have variations in their business activity.

Senator Eck said you don't have data that combines state and federal payments with this packet but do you have that information available. Most of what we have seen in the Governor's proposal looks at those combinations.

Gary Carlson said we can show a net impact within the data base of those particular taxpayers, netting the federal difference and state to cause an increase or decrease. This would conform with the presentation from the Department of Revenue combining the effect. He said he could make that available.

Senator Neuman said on the graph on average dollar decrease in Montana 1988 taxes under Ramirez' tax proposal, it was stated by Patrick Hanley that the decrease to the upper end was \$2,163 but the graph shows \$675.

Gary Carlson said that one goes off the graph. Some of these are off the graph because the ranges are so broad.

Senator Neuman said you show a lot of distortion between the various tax groups. He asked if it was possible to do tax reform that is revenue neutral, without having distortions in the various classes.

Pat Hanley said probably not. It probably isn't possible to do tax reform without having some movement among the brackets.

Senator Neuman said if we take the proposal that you advance, the flat 25% type approach, won't that higher marginal rate tend to be a red flag to businesses that want to come to Montana because we would have to have such a high rate.

Gary Carlson said that is a very difficult PR point to make, that Montana's rate is 25%. The important point you have to take, if you really seriously consider the proposal, is that it is not 25% of taxable income, it is 25% of the federal tax rate. In the 15% range that equates to the 3.75 range.

Senator Hirsch said in Mr. Carlson's comments he talked about the NOL's carry back and carry forward and how they impact small business and incorporated farms in Montana. He is wondering if Mr. Carlson has run any average return or selective group of returns to give an

idea of how that change will affect those businesses given the Governor's proposal.

Gary Carlson said all the graphs seen this morning are individual income tax returns. The proposal in SB 307 is just affecting the corporate NOL's. There is no proposal in the Governor's proposal to impact the individual tax filers NOL. That covers the individual proprietor, those that are in partnerships, those that are in small business corporations. They are not impacted by the change in NOL's promulgated by the bill.

Senator Hirsch said a subchapter farm would be affected by the sole proprietorship, would it not.

Gary Carlson said no, the sub-S corporation is not affected.

Senator Halligan said he does not know exactly what is in the Ramirez bill. He asked Mr. Carlson if he could go through a few of the things Ramirez is doing.

Gary Carlson said the rates have been reduced from the current rate structure that you have on page 2 of the Montana return, handed out with Exhibit 1. The Ramirez bill takes the rates on page 2 and changes them, reducing them to try to take care of the impact of the windfall. At the same time, the rates also changed the brackets. So, the 0-13 also changed.

Senator Halligan asked how Ramirez dealt with capital gains and some of the changes that the feds made.

Gary Carlson said the impact was just let the windfall happen and lower the rates.

Senator Mazurek asked if Mr. Carlson had done any detailed evaluation on the loss of the federal tax paid deduction, combined joint filers requiring to be filed joint at the state level and retirement income. He asked Mr. Carlson if he could elaborate on how he sees the impact of those three features.

Gary Carlson said we are trying to calculate the impact of the consolidation of married, filing separately to determine a fixed number. To have true simplification, that is being proposed, you have to start somewhere and its either start with federal taxable income, and then you can control that by the rates in the Governor's bill. That would mitigate the loss of the deduction for federal income taxes. We do not have the data to specifically calculate the individuals on the federal itemized deduction.

We are trying to come up with numbers on the married, filing separately issues in the state.

Senator Crippen said he liked the idea of a flat percentage of federal tax. That would then piggyback on the federal tax, which would eliminate the deduction that we presently have for the federal taxes paid. What effect would you have on this if you did that, but allowed a deduction after that.

Gary Carlson said he knows the Department of Revenue has the talent to design the form to work. But, again, that is not true simplification when you start doing that. It is possible to mitigate that, but you can mitigate that just as easily with the rates.

Senator Crippen said then as an alternative you would say let's take that into account with the use of rates. He asked how he would do that.

Gary Carlson said you would have to make some assumptions and definitely impact brackets differently from the standpoint of the rate you select as the single rate. He sees that as a rate that could be changed easily by the legislature.

Senator Eck said when you talked about the flat percentage of the federal tax, you described the kind of form and there was the percent of tax and then three or four adjustments. What were the adjustments.

Gary Carlson said the adjustments are the same as those that the Governor's simple tax return shows.

Senator Eck said how about the various credits that we have, the credit that we just passed for capital companies, for instance.

Gary Carlson said those are items on the lower part of the return.

Senator Halligan said since we are talking of a possible sales tax, is it possible to do a scenario using the various proposals we have here and the impact of the non-deductibility of that at the federal level and see what the impact on income tax payers would be at the various levels.

Gary Carlson said it would be very difficult from the data base they have.

Senator Halligan asked John LaFaver if he could provide information showing what a sales tax of 4-5% would have on the various income groups, given federal tax reform and non-deductibility.

John LaFaver said he would certainly attempt to respond to whatever requests come from the Senate Taxation Committee. He is not aware of an analysis that he could pull off the shelf. To do the kind of analysis that they have done on the income tax, depends heavily on what the sales tax looks like, what products are being taxed and what products are being excluded.

Senator McCallum advised that Representative Phillips had requested a few minutes of the committee's time to speak on SB 307.

Representative Phillips, House District 33, gave testimony in opposition to the repealer in SB 307 that active duty military pay is exempt from state income tax. A copy of his written statement and a proposed amendment to SB 307 is attached as Exhibit 2.

Senator Mazurek said he would be curious to hear the Department's response to the presentation by the Montana Society of CPA's.

John LaFaver said he had an opportunity to go over this data with the CPA's last evening. He said this data is not worthless but one has to be cautious in looking at this to the extent that it gives the impression that this is a representative sample of Montana taxpayers. That is wrong. The CPA's have said that a number of ways and a number of times it is not a statistically valid sample of Montana taxpayers. The first chart that they have, the one that says percentage increase in 1988 federal taxes compared to 1985 federal taxes and then it shows the income brackets from 0-10 and then over 75. That chart gives the impression that we are looking at 100% of Montana taxpayers and the chart gives the impression that the average would be somewhere around 30-40, but the average taxpayer is less than 10. The average taxpayer is way to the left. What this is showing is an analysis of a select group of taxpayers that are above average. The chart in the state analysis which says percent who change, state income tax, page 4 in the income tax portion, there are a number of bars that represent what percent, by income level, the taxpayers who pay more or less. In looking at the information furnished by the Department and the information that was furnished by the CPA's, the CPA's information is not

aggregate information, it is only a small part of the total information in terms of analyzing what the impact on Montanans is. One of the obvious examples of their samples is that 44% have capital gains and only 16% of total Montana taxpayers have capital gains. The information that they have presented is not inaccurate but it is not representative of all of Montana taxpayers. He asked the committee and the Society of CPA's if he could have access to their data base and relate that to the comprehensive data base that the Department is using.

Senator Crippen asked Mr. LaFaver if he was overlooking the fact that the graphs presented by the Montana Society of CPA's deal with actual returns.

John LaFaver said so do our graphs.

Senator Crippen said if that is the case then we should probably look at all the graphs.

John LaFaver said the data that we use and methodology that we use has been analyzed by the Bureau of Business Research at the University of Montana and they agree that the methodology in the data base we are using, accurately portrays the entire population of Montana taxpayers. Also, this committee, and the legislature as a whole, has hired an outside expert to look at the bottom line numbers that we came up with and the conclusions of that analysis is that we are apart from his analysis by a small fraction of one percent.

Senator McCallum said if the Montana Society of CPA's has no objection to your using their data base, the committee has no objection.

John LaFaver asked if the committee would like to see a comparison or not.

Senator McCallum said what he wants to see is what they will be showing on actual returns and what will happen to actual returns. His understanding is that is what the Society is going to try to put together. Not an average because averages can mean so much. Whenever you bring something down to neutral, one will come down and one will go up.

Gary Carlson said as to the availability of the data base, there is nothing secret, we can put it onto two floppy disks and the Department can have the information as soon as they want it.

George Anderson, CPA, Helena, said the only thing that bothers him about the graphs is he thinks there is a complete difference between the two data bases. He

believes the Montana Society of CPA's shows the windfall in their increases and decreases and he does not believe the information furnished by the Department shows the windfall, but after the windfall.

John LaFaver said there are two charts in the report that was passed out that include the so called windfall. One is a pie chart that says percent who change, total income taxes, old law to proposed law. That includes the so called windfall. The bar chart that is under that pie chart, likewise shows the windfall. What both of those charts show, is that for total Montana taxpayers, 77% will pay less total income tax at the federal and at the state level combined, including the windfall, than they paid without federal or state tax reform.

Senator Halligan said even the specific data that you will come up with this week or next week, will not deal with behavioral changes of taxpayers by 1988.

Gary Carlson said that is very true. We will take exact 1985 data and interpret it for 1988.

The additional information referred to in these minutes dealing with individual actual returns, which was presented by the Montana Society of CPA's to the House Taxation Committee, is attached in Exhibit 1.

ADJOURNMENT: The meeting adjourned at 9:25 A.M.


SENATOR GEORGE McCALLUM, Chairman

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ROLL CALLTAXATION

COMMITTEE

50th LEGISLATIVE SESSION -- 1987

Date 2-24-87

| 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.

SENATE

Taxation

COMMITTEE

BILL

SB 307

VISITORS' REGISTER

DATE

2-24-87

Please note bill no.

(check one)

NAME

REPRESENTING

BILL #

SUPPORT

OPPOSE

Larry B. Carlson

Mt. Society of CPAs

307

Hemis Z. Adams

Mt. Society of CPAs

307

Zelma Dawson

retired persons-

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY

NAME: ATRICK W. FINLEY DATE: 2/24/81

ADDRESS: 3110 BRAYTON ST BILLINGS MT

PHONE: 257-2831

REPRESENTING WHOM? MONTANA Society of CPAL

APPEARING ON WHICH PROPOSAL: SB-307

DO YOU: SUPPORT? _____ AMEND? OPPOSE? _____

COMMENTS: _____

PLEASE LEAVE ANY PREPARED STATEMENTS WITH THE COMMITTEE SECRETARY.

NAME :

DATE :

ADDRESS :

PHONE :

REPRESENTING WHOM?

APPEARING ON WHICH PROPOSAL:

DO YOU:

SUPPORT?

AMEND?

OPPOSE?

COMMENTS:

PLEASE LEAVE ANY PREPARED STATEMENTS WITH THE COMMITTEE SECRETARY.

February 24, 1987

Testimony by Gary B. Carlson, CPA
on Behalf of
The Montana Society of Certified Public Accountants

Report to Montana Legislators

- o Impact of the 1986 Tax Reform Act on Montana Taxpayers
- o Implications of Selected Proposals to Reform Montana Income Taxes

This database and report was developed by the voluntary efforts of members of the Montana Society of Certified Public Accountants, staff members, and a volunteer staff teacher from the Great Falls Vocational Technical Center.

We have in excess of 1700 hours invested in the database development, which equates to one year of work by a CPA staff member of one of our firms.

Our purpose:

- o Independence
- o Specific data based on information in our database
- o Provide additional information for decision making
- o Directed to reflect a relationship of alternatives:
 - A relational database
 - o Windfall
 - o Montana Tax 1988 with no change
 - o SB 307
 - o HB 444--because it was available

SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

FILE NO. SR.307

Caution--as explained later, our lower income groups may not be; most likely is not representative of all filers. It represents those in our data. We caution you that Montanans may have different strategies than the nation.

We used "live" data--actual returns for 1985.

We will emphasis numerous times that our report is based on the 500 actual 1985 returns in the database we developed. It was not prepared to depict the exact impact on all Montana taxpayers. It DOES NOT show TOTAL REVENUES.

(Review SUMMARY OF DATABASE METHODOLOGY, page 2 of Report to Montana Legislators.)

We requested 52 specific data items from CPA firms, and 62 responded.

We have created a RELATIONAL database from the information. We then utilized the actual data from the 1985 returns filed, which differs from the 1984 information base utilized by the Department of Revenue and the 1981 database used by the Policy Economics Group.

We then determined the impact of the Tax Reform Act of 1986 on EACH of the returns placed in the database INDIVIDUALLY. We went through each of the returns to assess the changes caused by the Tax Reform Act of 1986.

This is where our database may be significantly different from others.

We identified the specific impact after the Tax Reform Act of 1986 as we were best able. We will review the significant assumptions on page 3 in a moment.

SENATE TAXATION

EXHIBIT NO. /

DATE 2-24-87

BILL NO. S.B. 207

Fraser, Lual

SUMMARY OF
DATABASE METHODOLOGY

The database was created using a questionnaire requesting 52 specific items from actual Federal and state tax returns filed by Montana residents for the 1985 tax year. The 52 questions included such items as husband's and wife's occupations; earnings and wages; pension income; interest income; various itemized deductions; Federal and state adjusted gross income and filing status on the Federal and state returns. *THE PAID*

The questionnaire was sent to all Montana Society of CPA practitioners; 62 firms submitted information for the 500 returns used in the database.

The total amount of 1985 Federal tax paid was \$5,122,000; the total amount of 1985 Montana tax paid was \$1,026,000.

Methodology

Each CPA preparer was instructed to select and submit a variety of tax returns from client files. The selection process, therefore, was not statistical and does not allow for the extrapolation of data to all Montana individual taxpayers.

The effects shown on the various taxpayers in this database may or may not be representative of other Montana taxpayers within each bracket.

The MSCPA data has not been adjusted for behavioral changes which may occur, due to changes in Federal tax law.

SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

*We have created a relational
data base — from the information*

It is important to emphasize the database is 500 actual returns. We did NOT adjust for behavior response. We did NOT adjust for the new tax advice we CPAs will be offering to our clients to adjust behavior based upon the new law! We converted actual returns through utilization of a recognized tax software program to project taxable income in 1988, reflecting the impacts of the Tax Reform Act of 1986.

(* Refer to SUMMARY OF SIGNIFICANT ASSUMPTIONS. *)

All our assumptions were intended to be conservative.

GRAPH #1

This is a summary graph which shows the relationship of the 1985 actual Montana income taxes paid based upon the 500 returns in our database to other proposals.

The vertical axis reflects dollars of Montana income taxes payable by various groups of taxpayers.

Each color depicts a separate proposal:

| | |
|--------|---|
| RED | Actual 1985 Montana Taxes |
| GREEN | 1988 Tax with No Change in Law |
| PURPLE | SB 307 Proposal |
| BLUE | HB 444 Ramirez--return a portion of the so-called windfall |

This bill was available so we utilized it--Rep.

Ramirez has publicly stated the rates need adjustment.

The measurement of the projected windfall from the returns in the Montana Society of CPA database initially is the difference between the red bar and the green bar.

SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

SUMMARY OF SIGNIFICANT ASSUMPTIONS

In completing this analysis, certain assumptions were made to simplify calculations and to make calculations possible when information was not available. We believe the application of these assumptions does not have a material effect on the analysis results.

Following is a list of assumptions used in the various tax calculations:

- o The database was developed using actual 1985 income tax return information. The information was recalculated to reflect the changes effected by the Tax Reform Act of 1986 and various Montana income tax proposals.
- o No assumptions were made regarding taxpayer behavior in response to tax law changes.
- o The impact of the Residential Property Tax Credit, under the SB 307 proposal, was not included in the tax calculations. Although this tax credit may have a favorable impact on many Montana taxpayers (particularly lower income taxpayers), information to make the calculations was not available.
- o We assumed IRA contribution deductibility limitations will not apply to any taxpayers in the database.
- o All interest other than home mortgage interest has been assumed to be personal interest and has been reduced by 60%.
- o Miscellaneous itemized deductions have been reduced by the 2% threshold adopted in TRA '86.
- o Moving expenses, not subject to the 2% threshold under Federal law, have been subjected to the threshold for purposes of this analysis.
- o Passive losses were assumed to be 100% deductible up to \$25,000; the deduction was reduced by 60% for amounts over \$25,000. The phase-out, effective for incomes over \$100,000, has been ignored.
- o Investment credit recapture has been ignored.
- o It was not possible to calculate the effects of the proposed Montana alternative minimum tax for purposes of this analysis.
- o Investment credit (eliminated under Federal law) was assumed to be eliminated for Montana income tax purposes. All other tax credits have been treated as though unaffected by the tax law changes.

- o All adjustments to income and deductions resulting from federal and proposed Montana tax law changes have been made to the "column A-taxpayer" none to the "B"

The horizontal axis is 1985 federal taxable income in 000s (thousands). We have consistently retained each taxpayer in each of these ranges for each analysis.

You will see this axis--federal taxable income--remains the same on almost all graphs.

To illustrate the change in tax projected, let's look at a copy of this graph. (not in the report)

GRAPH #2

Dropped the over 75,000 taxpayers ('85 Federal taxable income) to change the horizontal axis (not in your book) from \$16,500 to \$6,000.

The \$20-30 columns on graph #2 shows:

| | |
|----------------------------|---------------------------------------|
| The 1985 Tax | \$ 798 |
| 1988 Tax, no change in Law | \$1050 a change of \$252 (32% change) |
| Gov. 1988 | \$1400 a change of \$602 |
| Ramirez | \$ 987 |

Each of the graphs Pat Hanley will momentarily present to you will show each of the proposals separately. We will conclude showing this graph.

GRAPH #3 (Your second)

This graph is placed here to help you set the relationship between adjusted gross income and taxable income.

(Look at your copy of the Montana Return <Form 2>, Page 1, Line 22.)

SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

Adjusted Gross Income is the bar portion of the graph. The line shows taxable income, the difference being basically itemized deductions and exemptions. (Taxable income is line 43 page 2)

Again we retain the same ranges of 1985 federal taxable income in the horizontal axis for comparability.

We emphasis again to you these returns are CPA prepared returns--they may not be representative of taxpayers across Montana, even though we had 62 firms from large and small towns across the state submit returns.

We recognize the clients we have in the \$0-10,000 range of taxable income are most likely not the same as the self-prepared returns filed or those of H & R Block. They may have different attributes, which in 1985, placed the return in this range.

In the remainder of the presentation, we stress in the open face graphic presentation in the report--YOU MUST ALWAYS utilize the percent and the dollar graphs, assimilating them. They are NOT fairly presented separately. Each could be misrepresentative separately.

I now introduce Pat Hanley from Billings, a member of the Montana Society of CPAs' State Taxation Committee and member of our database group to present the Selected Database Attributes and further graphs.

*** Hanley Presentation Took Place ***

The next graph we present to you is the percent of federal tax to Montana tax, comparing the various proposals.

SENATE TAXATION

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The percent is equal to the single rate concept we have proposed for further simplification. The vertical axis shows actual 1985 Montana returns to 1985 federal returns. If you run a line across the graph at 20%, all but one range is below.

Each relationship is determined for each proposal:

PURPLE 1988 Montana no change to 1988 Federal - drawing a line across the graph at the 25% level shows that most of the percentages are at or below 25%.

GREEN

RED

Attached to our concerns regarding SB 307, you have a schedule of rates shown as:

*** See MONTANA EFFECTIVE TAX RATES (FOR EXAMPLE ONLY) MARRIED
FILING JOINTLY--1987 & 1988 ***

Finally, we return to our starting graph, which summarized the three proposals and 1985 actual Montana taxes.

*** QUESTIONS ***

Presentation next Tuesday with the House Taxation Committee.

- Provide specific examples
- Tables which relate to the graphs

SENATE TAXATION
EXHIBIT NO. 1
DATE 2-24-87
BILL NO. S.B. 307

MONTANA EFFECTIVE TAX RATES
(FOR EXAMPLE ONLY)
MARRIED FILING JOINTLY - 1987

| Federal tax rate | | Montana % of federal tax rate | | Montana effective tax rate |
|---------------------|-------|-------------------------------------|---|----------------------------------|
| 11% | times | 25% | = | 2.75% |
| 15% | times | 25% | = | 3.75% |
| 28% | times | 25% | = | 7.00% |
| 35% | times | 25% | = | 8.75% |
| 38.5% | times | 25% | = | 9.625% |

MARRIED FILING JOINTLY - 1988

| | | | | | |
|--------------|-----|-------|-----|---|-------|
| 29750 | 15% | times | 25% | = | 3.75% |
| 29750-71900 | 28% | times | 25% | = | 7.00% |
| 71900-171090 | 33% | times | 25% | = | 8.25% |
| 171090 | 28% | times | 25% | = | 7.00% |

SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

FORM 2

1986 — Montana Individual Income Tax Return — 1986 S.B.307

OR FISCAL year beginning _____, 1986 and ending _____, 19 _____

PLACE LABEL HERE

Correct label if necessary.

File on or before April 15, 1987 (Fiscal year see instructions).

| | | | | |
|---------------------------------|-------------------------------|------------------------------|---|----------|
| LAST NAME | First Name & Initial | Your Social Security No. | Chief Occupation Enter code no. from page 14 of instructions | Yours |
| Spouse's Last Name If Different | Spouse's First Name & Initial | Spouse's Social Security No. | | Spouse's |
| MAILING ADDRESS | | City | State | Zip Code |

| | | | | | | |
|----------------------------|-----------------------------------|---|--|---|--|--|
| Filing Status Check One | 1 <input type="checkbox"/> Single | 2 <input type="checkbox"/> Married filing joint return | 3 <input type="checkbox"/> Married and both filing separate returns on this form | 4 <input type="checkbox"/> Married and both filing separate returns on separate forms | 5 <input type="checkbox"/> Married filing separate return and spouse is not filing | 6 <input type="checkbox"/> Unmarried Head of Household |
|----------------------------|-----------------------------------|---|--|---|--|--|

| | | | | | |
|-------------------------------|--|---|---|---------------------|--------------------------|
| Residency Status Check One | 1 <input type="checkbox"/> Resident Full Year | 2 <input type="checkbox"/> Nonresident Full Year | 3 <input type="checkbox"/> Resident Part Year | Give date of change | State moved to: From: |
|-------------------------------|--|---|---|---------------------|--------------------------|

If married filing separate on this form is elected, use Column A for yourself and Column B for spouse.
For all other returns, use Column A only.

| EXEMPTIONS | Regular | 65 or Over | Blind | COLUMN A (For single joint, separate, or head of household) | COLUMN B (For spouse only when filing separate, and box 3 is checked) |
|--|--------------------------|--------------------------|--------------------------|---|---|
| 1. Yourself | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | 1 | |
| 2. Spouse | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | 2 | 2 |
| 3. Number of exemptions claimed for dependents. See page 3 of instructions | | | | 3 | 3 |
| 4. Number of exemptions claimed for handicapped children. See page 3 of instructions | | | | 4 | 4 |
| 5. Add lines 1, 2, 3, and 4 for TOTAL number of exemptions | | | | 5 | 5 |

INCOME REPORTED ON FEDERAL RETURN

YOU MAY ROUND TO NEAREST DOLLAR

| | | | |
|---|-----|--|-----|
| 6. Wages, salaries, tips, etc. | 6. | | 6. |
| 7. Interest income (Attach Federal Schedule B if over \$400) | 7. | | 7. |
| 8. Dividend income (Less federal exclusion) (Attach Schedule B if over \$400) | 8. | | 8. |
| 9. Net business income (Attach Federal Schedule C) | 9. | | 9. |
| 10. Capital gain or (loss) (Attach Federal Schedule D) | 10. | | 10. |
| 11. Supplemental gains or (losses) (Attach Federal Form 4797) | 11. | | 11. |
| 12. Rents, royalties, partnerships, estates, trusts, etc. (Attach Federal Schedule E) | 12. | | 12. |
| 13. Net farm income (Attach Federal Schedule F) | 13. | | 13. |
| 14. Taxable portion of Social Security | 14. | | 14. |
| 15. Other income (Specify; fees, retirement, State Ref. _____ etc.) | 15. | | 15. |

| | | |
|------------------------------|-------|-----|
| 16. Total of lines 6 thru 15 | Total | 16. |
|------------------------------|-------|-----|

Adjustments from Income:

| | | | |
|--|-------|-----|-----|
| 17. Moving expense (Attach Federal Schedule 3903) | 17. | | 17. |
| 18. Employee business expenses (Attach Federal Schedule 2106) | 18. | | 18. |
| 19. Payments to an IRA, Keogh, and other retirement plans | 19. | | 19. |
| 20. Other adjustments: (Marriage deduction, etc.) (Attach list) | 20. | | 20. |
| 21. Total of lines 17 thru 20 | Total | 21. | |
| 22. Adjusted gross income same as federal return (Line 16 minus line 21) | | 22. | |

ADDITIONS TO INCOME

SEE PAGE 3 OF INSTRUCTIONS

| | | | |
|---|-------|-----|-----|
| 23. Interest on state, county or municipal bonds (Non-Montana) | 23. | | 23. |
| 24. Federal income tax refunds received (For taxes deducted in an earlier year) | 24. | | 24. |
| 25. Other additions: (Marriage deduction, social security, etc.) | 25. | | 25. |
| 26. Transfer allocation of income | 26. | | 26. |
| 27. Total additions to income (Add lines 23 thru 26) | Total | 27. | |
| 28. Add lines 22 and 27, enter result | | 28. | |

REDUCTIONS OF INCOME

SEE PAGE 4 OF INSTRUCTIONS

| | | | |
|---|-------|-----|-----|
| 29. Enter private retirement income, \$360 or total (Whichever is smaller) | 29. | | 29. |
| 30. Interest exclusion for elderly | 30. | | 30. |
| 31. Interest exclusion for savings bonds, etc. (Specify) | 31. | | 31. |
| 32. Income from sources outside Montana (Part-year & nonresidents only) | 32. | | 32. |
| 33. Exempt retirement income (Specify) | 33. | | 33. |
| 34. State refund (If included in line 15 above) | 34. | | 34. |
| 35. Other reductions (Specify; tips, social security, Indian Reservation, etc.) | 35. | | 35. |
| 36. Transfer allocation of income | 36. | | 36. |
| 37. Total reductions to income (Add lines 29 thru 36) | Total | 37. | |
| 38. Line 28 minus line 37. Enter amount on line 39, page 2 | | 38. | |

DO NOT USE THIS SPACE

ATTACH PAYMENT HERE

ATTACH WITHHOLDING STATEMENTS HERE

| Last Name and Initial | Social Security Number — — | COLUMN A (For single joint, separate or head of household) | COLUMN B (For spouse only when filing separate, and box 3 is checked) |
|--|--|--|---|
| 39. Montana adjusted gross income (From line 38) 39. | | | |
| DEDUCTIONS—Check one | | | |
| 40. <input type="checkbox"/> (A) Itemized Deductions: Enter total from Form 2A, line 85 <input type="checkbox"/> (B) Standard Deduction: Enter 20% of line 39 but not more than \$1,990. Not more than \$3,980 if filing joint or head of household . . . 40. | | | |
| 41. Line 39 minus line 40 and enter balance 41. | | | |
| EXEMPTIONS | | | |
| 42. Multiply \$1,060 times the number of exemptions on line 5 | | | |
| Nonresidents and part-year residents see instructions, page 12 & 13 42. | | | |
| 43. Taxable income. Line 41 minus line 42 (But not less than zero) 43. | | | |
| 44. Tax from tax table below 44. | | | |
| 45. Tax on lump sum distributions (See instructions page 5). 45. | | | |
| 46. Total tax—Add lines 44 and 45. Total 46. | | | |
| 47. Credits from Form 2A, line 93 47. | | | |
| 48. Balance—Line 46 minus line 47 and enter difference (But not less than zero) 48. | | | |
| 49. Investment credit recapture from Form 2A, Schedule V 49. | | | |
| 50. Public Campaign Fund. You and your spouse each may contribute \$1.00 . 50. | | | |
| 51. For each of the programs below you and your spouse each may contribute \$5, 10, 20 or any amount. Enter totals in boxes. See instructions for details. | | | |
| <div style="display: flex; justify-content: space-between;"> <div> Nongame Wildlife Program <div style="border: 1px solid black; width: 100px; height: 20px; display: flex; align-items: center;">52.</div> </div> <div> Child Abuse Prevention <div style="border: 1px solid black; width: 100px; height: 20px; display: flex; align-items: center;">53.</div> </div> <div> Agriculture in MT schools <div style="border: 1px solid black; width: 100px; height: 20px; display: flex; align-items: center;">54.</div> </div> </div> | | Enter grand total of boxes 52, 53 & 54 . . . 51. | |
| 55. Total tax—Add lines 48, 49, 50 and 51 Total 55. | | | |
| 56. Combine amounts shown on line 55, columns A & B 56. | | | |
| 57. Montana tax withheld (Attach withholding statements) . . . 57. | | | |
| Payments 58. Payments on 1986 estimated tax and amounts credited and from previous year 58. | | | |
| Credits 59. Homeowner or Renter Credit from Form 2EC 59. | | | |
| 60. Total of lines 57 thru 59 Total 60. | | | |
| 61. Combine amounts shown on line 60 columns A & B 61. | | | |
| 62. If line 61 is larger than line 56 enter amount OVERPAID 62. | | | |
| 63. Amount of line 62 to be Refunded to You (Line 62 minus line 63 if crediting an estimate to 1987) 63. | | | |
| Refund or Tax Due | 64. Amount of line 62 to be credited to 1987 estimated tax 64. | | |
| | 65. If line 56 is larger than line 61 enter TAX DUE. Attach check or money order for full amount if \$1.00 or more, payable to State Treasurer TAX DUE→ 65. | | |
| Mail to: Income Tax Division P.O. Box 5805 Montana Dept. of Revenue Helena, Montana 59604 | | Late filing penalty . . . 66. Late payment penalty . . . 67. Interest . . . 68. Total of Lines 65, 66, 67, 68 . . . 69. | |

Name, Address and Telephone number of preparer

Make remittance payable to State Treasurer

If you do not need state income tax forms and instructions mailed to you next year, check box. ☐

I declare under penalty of false swearing that the information in this return and attachments is true, correct and complete.

Your signature and date

Telephone Number

 Spouse's signature and date
 (If filing jointly or combined separate returns, both must sign)

TAX TABLE

If Taxable Income on Line 43 is:

| Over | But not over | Multiply by | and Subtract = Tax |
|---------|--------------|-------------|--------------------|
| \$ 0 | \$ 1300 | x 2% | \$ 0 |
| \$ 1300 | \$ 2600 | x 3% | \$ 13 |
| \$ 2600 | \$ 5300 | x 4% | \$ 39 |
| \$ 5300 | \$ 7900 | x 5% | \$ 92 |
| \$ 7900 | \$ 10600 | x 6% | \$ 171 |

If Taxable Income on Line 43 is:

| Over | But not over | Multiply by | and Subtract = Tax |
|----------|--------------|-------------|--------------------|
| \$ 10600 | \$ 13200 | x 7% | \$ 277 |
| \$ 13200 | \$ 18500 | x 8% | \$ 409 |
| \$ 18500 | \$ 26500 | x 9% | \$ 594 |
| \$ 26500 | \$ 46400 | x 10% | \$ 859 |
| \$ 46400 | — | x 11% | \$ 1323 |

Example = taxable income \$6000 x 5% (.05) = \$300 subtract \$92 = \$208 tax

Social Security Number

Medical and Dental Expenses

Prescription medicines, drugs, insulin,
doctors, dentists, hospitals, Ins. prems.,
transportation, lodging, hearing aids,

70. dentures, eyeglasses Total 70.

71. Enter 5% of line 39, Form 2 71.

72. Line 70 minus line 71 and enter balance in applicable column

(If less than zero enter zero.) 72.

Taxes

Federal Income Tax (Do not include self-employment tax)

73. Paid by withholding or declaration in 1986 73.

74. Balance of 1985 tax paid in 1986 74.

75. Additional tax for years _____ paid in 1986 75.

Other taxes (Do not include Montana income tax).

76. Real estate, personal property, motor vehicle fees 76.

77. Other deductible taxes (Specify) _____ 77.

Interest Expense

78. Home mortgage interest 78.

79. Credit cards and charge accounts 79

80. Other (List) ▶ _____

80.

81. **Contributions** 81

82. Child and Dependent Care Expense—Montana Form 2441M

(Federal schedule not accepted) 82

83. **Casualty and Theft Losses** (Less exclusion—attach federal schedule) . . . 83.84. **Miscellaneous Deductions** (List) Dues, political contributions, etc. _____

84

85. Total Deductions—

Add lines 72 thru 84. Enter your total here, and on Form 2, line 40 . . . 85

SCHEDULE II — CREDITS AGAINST TAX

86. Credit allowed residents for income taxes paid to other states or countries
(From Schedule III) 86

87. Contractor's gross receipts tax credit (Attach computation) 87

88. Investment credit (From Schedule IV) 88

89. Credit for installation of nonfossil energy systems (From Form 2B) 89

90. Credit for investment in energy conservation installations (From Form 2C) 90

91. Credit for wind-powered generation equipment (From Form 2WPC) 91

92. All other credits attach detail explanation. 92

93. **Total credits**—Enter here and on Form 2, line 47. 93

100% TOTAL STUDENTS 25% MALE 75% FEMALE 100% WHITE

SENATE TAXATION

EXHIBIT NO. /

DATE 2-24-87

BILL NO. S.B. 307

Last Name and Initial

Social Security Number

SCHEDULE III — CREDIT ALLOWED RESIDENTS FOR INCOME TAXES PAID OTHER STATES OR COUNTRIES

(See page 7 of instructions)

ATTACH COPY OF OUT-OF-STATE RETURN

1. Adjusted gross income from other state or country included in Montana gross income 1.
2. Total Montana adjusted gross income from line 39 of return 2.
3. Income tax liability to other state or country 3.
4. Montana tax liability from line 46 of Form 2 4.
5. Line (1) divided by line (2), but not more than 100% 5.
6. Multiply amount on line (4) by the percentage on line (5) 6.
7. Allowable credit is the smaller of the amount on line (3) or (6). Enter here and on line 86, Schedule II 7.

| COLUMN A (For yourself, joint separate or single) | | COLUMN B (For spouse) | |
|---|---|-----------------------|---|
| | | | |
| | | | |
| | | | |
| | | | |
| | % | | % |
| | | | |
| | | | |

SCHEDULE IV — INVESTMENT CREDIT

(See page 7 of instructions)

1. Allowable investment credit from line 7 of 1986 federal Form 3468 1.
2. Enter 5% of line 1 (Not to exceed \$500) 2.
3. Carryover of unused Montana investment credit (Attach breakdown by year) 3.
4. Tentative Montana investment credit (Add lines 2 and 3) 4.
5. Tax from line 46 of Form 2 5.
6. (a) Credit for income taxes paid to other states and countries 6.a
- (b) Contractor's gross receipts tax credit 6.b
7. Add lines 6 (a) and (b) 7.
8. Line 5 minus line 7 8.
9. Enter here and on line 88, Schedule II, the amount from line 4 or line 8, whichever is smaller. 9.

| COLUMN A (For yourself, joint separate or single) | | COLUMN B (For spouse) | |
|---|--|-----------------------|--|
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |

NOTE: 1. Married persons filing separately will each use \$500 as the limits if both qualify for the credit.
 2. The unused portion of the 1986 investment tax credit **may not** be carried back or carried over.

SCHEDULE V — RECAPTURE OF INVESTMENT CREDIT

| | COLUMN—A | | | COLUMN—B | | |
|---|-------------------------------|--------------------------------|--------------------------------|--|--------------------------------|--------------------------------|
| | Column A-1 Pre-81 Property | Column A-2 1981-82 Property | Column A-3 1983-85 Property | Column B-1 Pre-81 Property | Column B-2 1981-82 Property | Column B-3 1983-85 Property |
| Total tentative recapture from Line 14 of 4255 .. | 1. | 1. | 1. | 1. | 1. | 1. |
| Line 1 column A-1 times 20% .. | 2. | | | 2. | ◀ Line 1 Column B-1 times 20% | |
| Line 1 Column A-2 | | | | | | ◀ Line 1 Column B-2 times 30% |
| 3. Times 30% .. | | 3. | | | 3. | |
| 4. Line 1 Column A-3 times 5% .. | | | 4. | Line 1 Column B-3 times 5% .. | ▶ | 4. |
| 5. Total tentative Montana recapture tax Add lines 2, 3, and 4 Column A .. | | | 5. | Add Lines 2, 3, and 4 Column B .. | ▶ | 5. |
| 6. Previous Montana investment credit unused. | | | 6. | Previous Montana investment credit unused. | ▶ | 6. |
| 7. Montana investment credit recapture Line 5 minus Line 6 .. | | | 7. | MT investment credit recapture Line 5 minus Line 6 .. | ▶ | 7. |

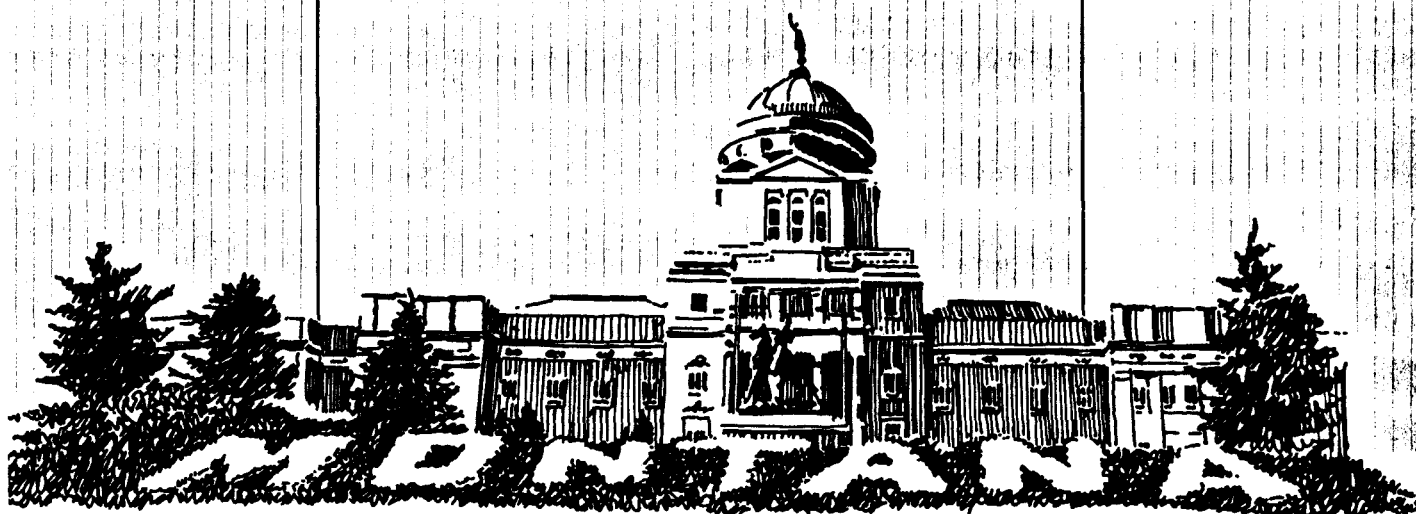
Enter these amounts on Line 49, Form 2. Do not use this amount to reduce your current year investment credit.



REPORT

TO MONTANA LEGISLATORS

- IMPACT OF THE 1986 TAX REFORM ACT ON MONTANA TAXPAYERS
- IMPLICATIONS OF SELECTED PROPOSALS TO REFORM MONTANA INCOME TAXES



presented by
THE MONTANA SOCIETY OF CERTIFIED PUBLIC ACCOUNTANTS

FEBRUARY, 1987

SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

FILE NO. S.B. 307

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TABLE OF CONTENTS

1. Transmittal letter
2. Summary of Database Methodology
3. Summary of Significant Assumptions
4. Exhibits
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 - o Tables
 - o Selected database attributes

SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307



THE MONTANA SOCIETY OF CERTIFIED PUBLIC ACCOUNTANTS
Diamond Block Building • 44 West Sixth Avenue • P.O. Box 138 • Helena, Montana 59624-0138 • Telephone 406/442-7301

MEMBERS OF THE SENATE AND HOUSE TAXATION COMMITTEES:

At your request, the accompanying analysis has been developed on the basis of information accumulated from 1985 individual Federal and state income tax returns.

The database:

- o assesses the impact of the 1986 Federal Tax Reform Act on Montana taxpayers
- o reflects the effects of SB 307 and HB 444
- o shows the impact of no change in the current rate tax structure

The database includes responses from over 60 Montana CPA firms, representing 500 CPA-prepared income tax returns. The returns were not selected using a statistically valid method. Consequently the information is not necessarily representative of all Montana taxpayers.

The information has not been audited and, accordingly, we can express no opinion on the accuracy, completeness or reasonableness of the information. The information should be read in the context of the assumptions used (more fully described on page 3). The accompanying exhibits provide selected database details.

The purpose of this presentation is to provide additional data to assist tax proposal analysis. We are available to discuss the report in more detail.

Members of the Montana Society of CPAs appreciate the opportunity to present this information to you.

Helena, Montana
February 24, 1987

Montana Society of
Certified Public Accountants

SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

SUMMARY OF DATABASE METHODOLOGY

The database was created using a questionnaire requesting 52 specific items from actual Federal and state tax returns filed by Montana residents for the 1985 tax year. The 52 questions included such items as husband's and wife's occupations; earnings and wages; pension income; interest income; various itemized deductions; Federal and state adjusted gross income and filing status on the Federal and state returns.

The questionnaire was sent to all Montana Society of CPA practitioners; 62 firms submitted information for the 500 returns used in the database.

The total amount of 1985 Federal tax paid was \$5,122,000; the total amount of 1985 Montana tax paid was \$1,026,000.

Methodology

Each CPA preparer was instructed to select and submit a variety of tax returns from client files. The selection process, therefore, was not statistical and does not allow for the extrapolation of data to all Montana individual taxpayers.

The effects shown on the various taxpayers in this database may or may not be representative of other Montana taxpayers within each bracket.

The MSCPA data has not been adjusted for behavioral changes which may occur, due to changes in Federal tax law.

SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

SUMMARY OF SIGNIFICANT ASSUMPTIONS

In completing this analysis, certain assumptions were made to simplify calculations and to make calculations possible when information was not available. We believe the application of these assumptions does not have a material effect on the analysis results.

Following is a list of assumptions used in the various tax calculations:

- o The database was developed using actual 1985 income tax return information. The information was recalculated to reflect the changes effected by the Tax Reform Act of 1986 and various Montana income tax proposals.
- o No assumptions were made regarding taxpayer behavior in response to tax law changes.
- o The impact of the Residential Property Tax Credit, under the SB 307 proposal, was not included in the tax calculations. Although this tax credit may have a favorable impact on many Montana taxpayers (particularly lower income taxpayers), information to make the calculations was not available.
- o We assumed IRA contribution deductibility limitations will not apply to any taxpayers in the database.
- o All interest other than home mortgage interest has been assumed to be personal interest and has been reduced by 60%.
- o Miscellaneous itemized deductions have been reduced by the 2% threshold adopted in TRA '86.
- o Moving expenses, not subject to the 2% threshold under Federal law, have been subjected to the threshold for purposes of this analysis.
- o Passive losses were assumed to be 100% deductible up to \$25,000; the deduction was reduced by 60% for amounts over \$25,000. The phase-out, effective for incomes over \$100,000, has been ignored.
- o Investment credit recapture has been ignored.
- o It was not possible to calculate the effects of the proposed Montana alternative minimum tax for purposes of this analysis.
- o Investment credit (eliminated under Federal law) was assumed to be eliminated for Montana income tax purposes. All other tax credits have been treated as though unaffected by the tax law changes.
- o All adjustments to income and deductions resulting from federal and proposed Montana tax law changes have been made to the "column A-taxpayer"; none to the "column B-spouse."

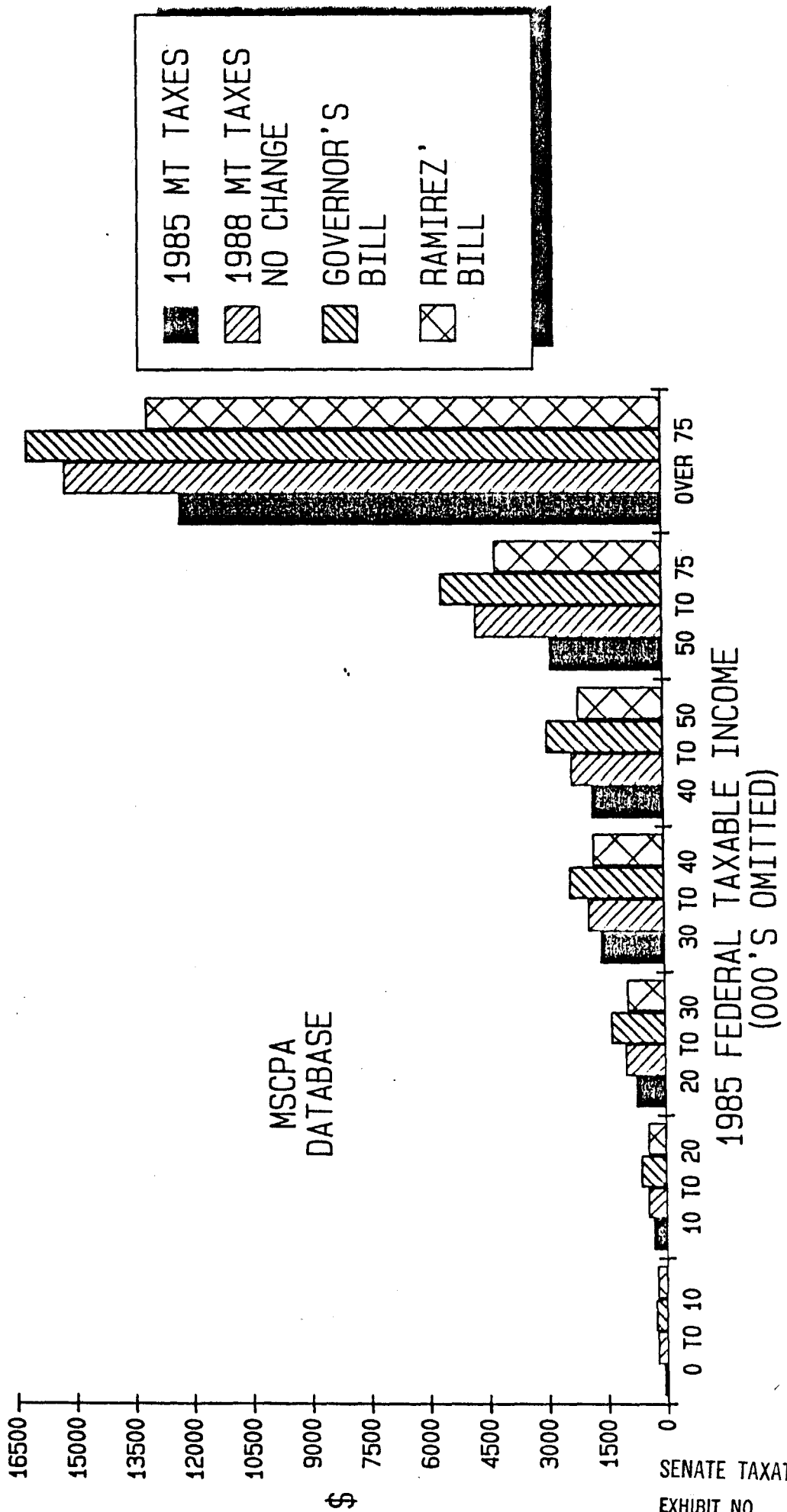
SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

MONTANA TAXES COMPARING VARIOUS PROPOSALS



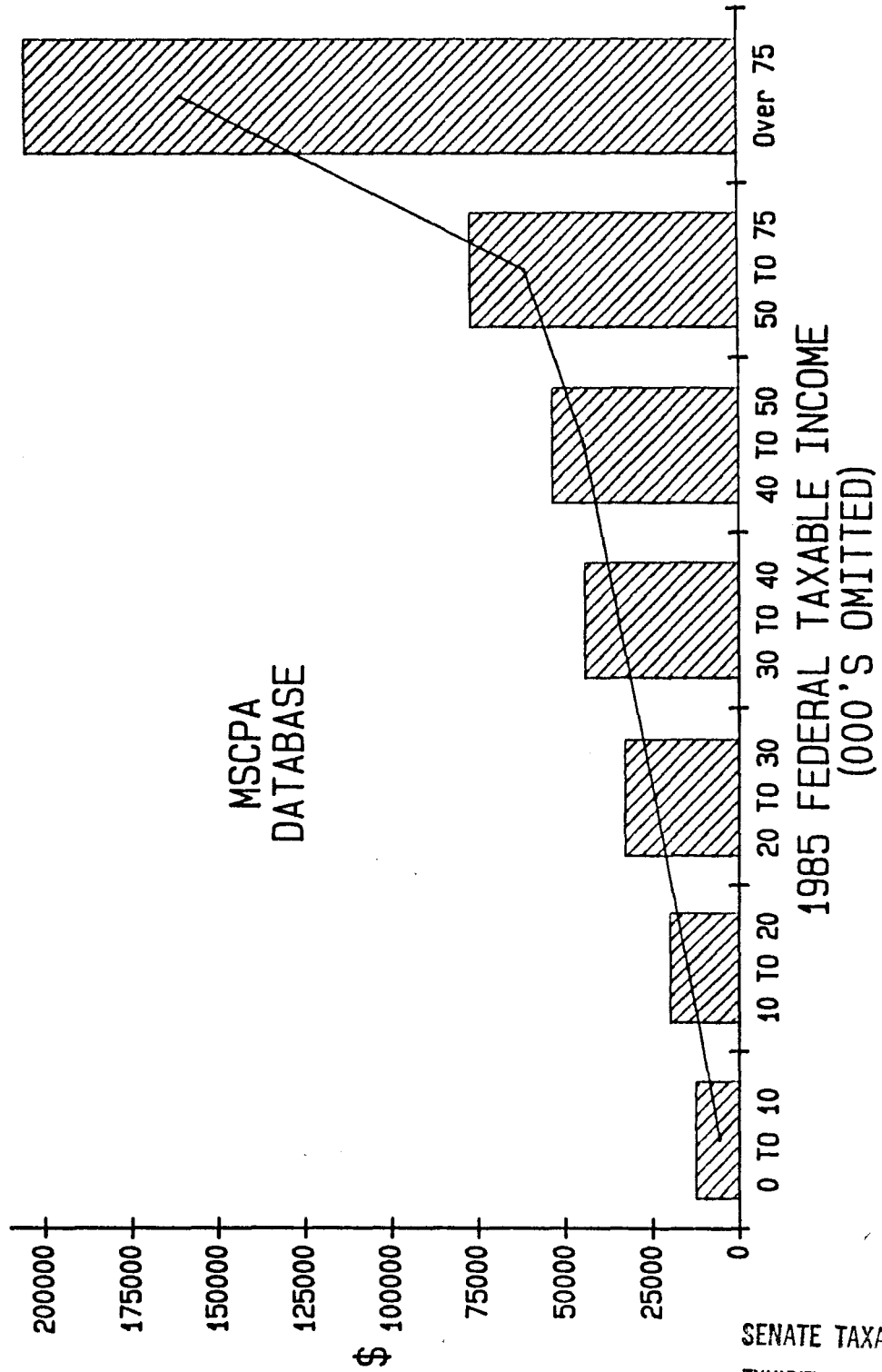
SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

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1985 FEDERAL AGI COMPARED TO 1985 FEDERAL TAXABLE INCOME



SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

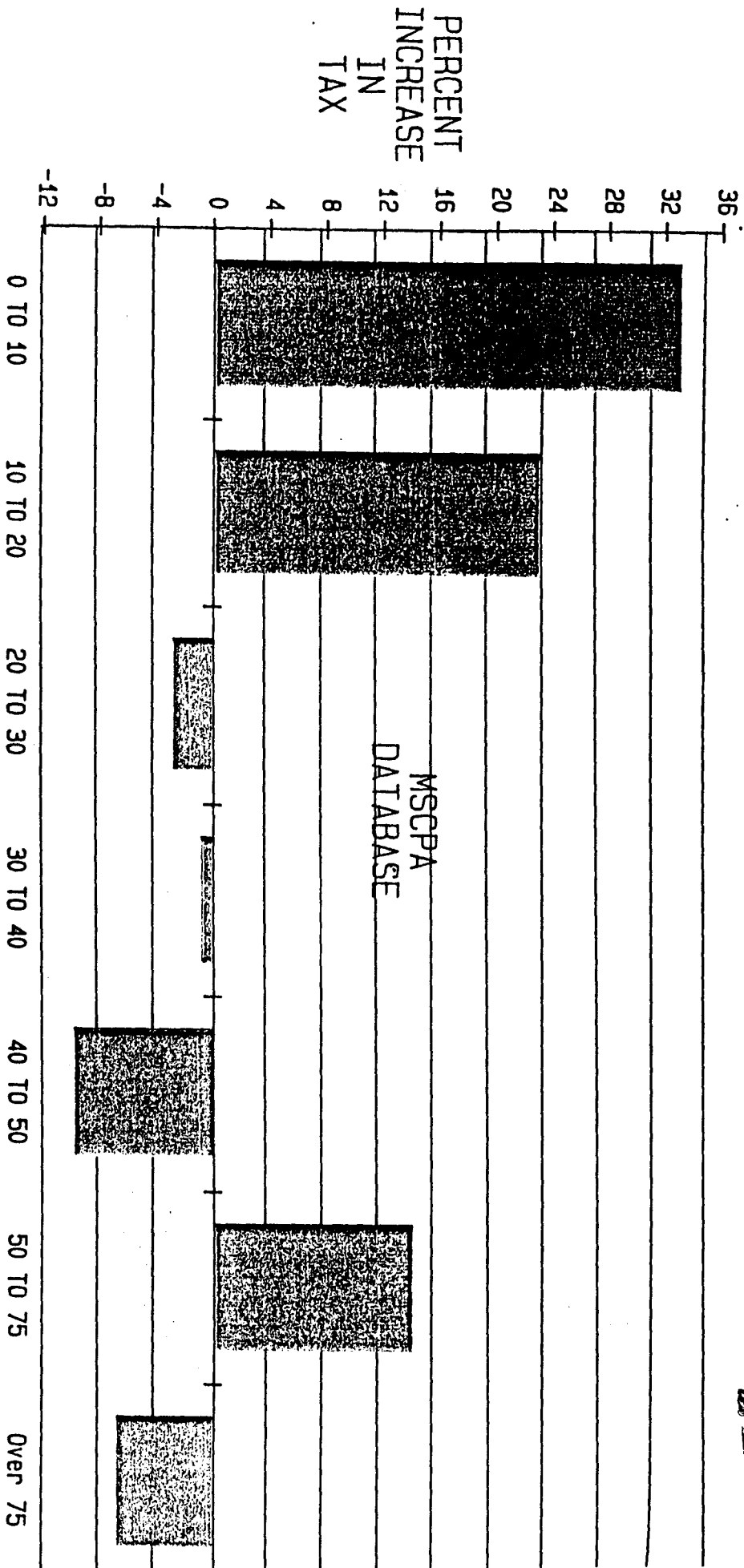
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ADDITIONAL INFORMATION

PERCENTAGE INCREASE IN 1988 FEDERAL TAXES COMPARED TO 1985 FEDERAL TAXES PAID

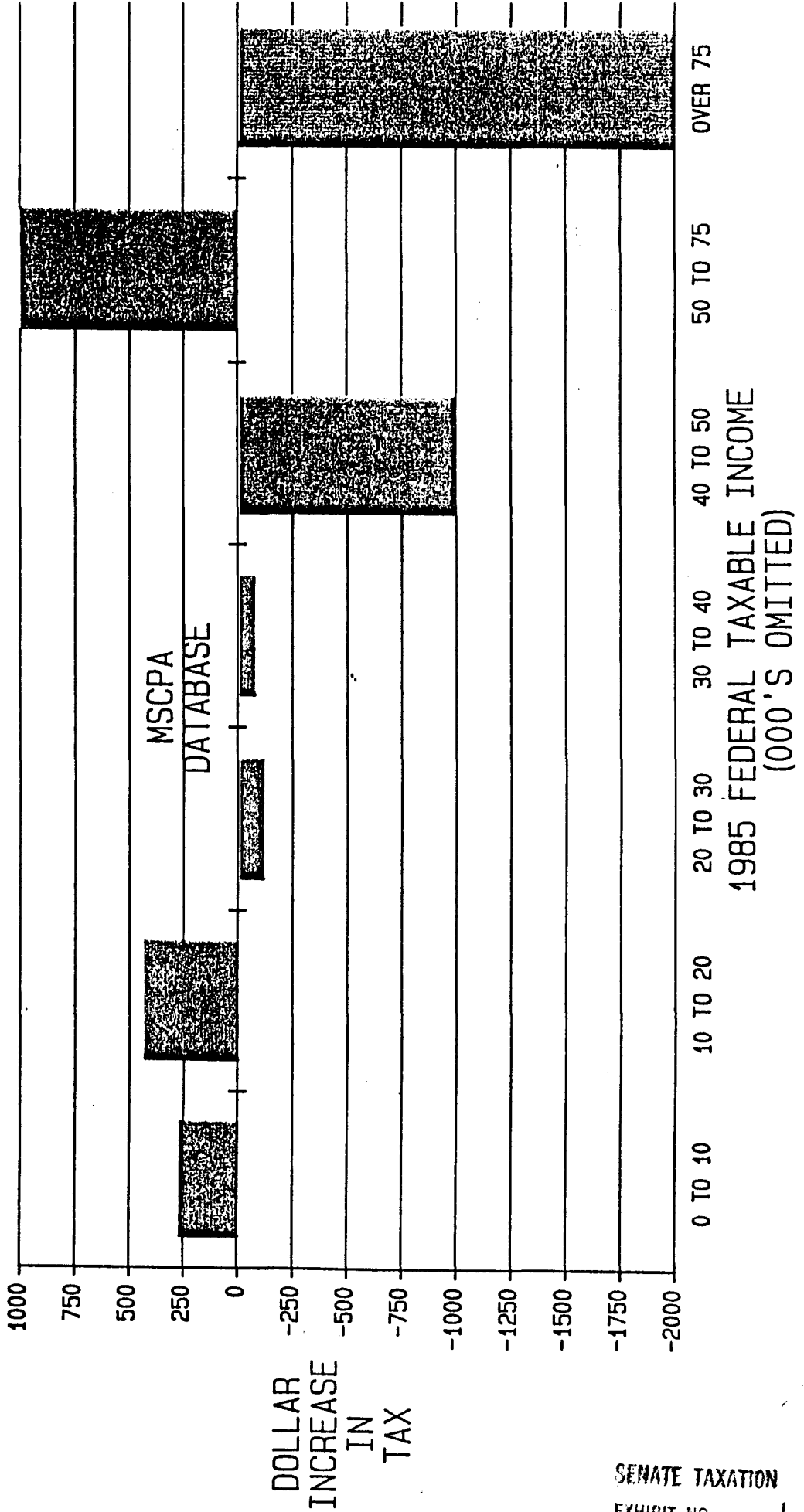
SENATE TAXATION

EXHIBIT NO. 1
DATE 2-24-87
BILL NO. S.B. 307



1985 FEDERAL TAXABLE INCOME
(000'S OMITTED)

AVERAGE DOLLAR INCREASE IN 1988 FEDERAL TAXES COMPARED TO 1985 FEDERAL TAXES PAID



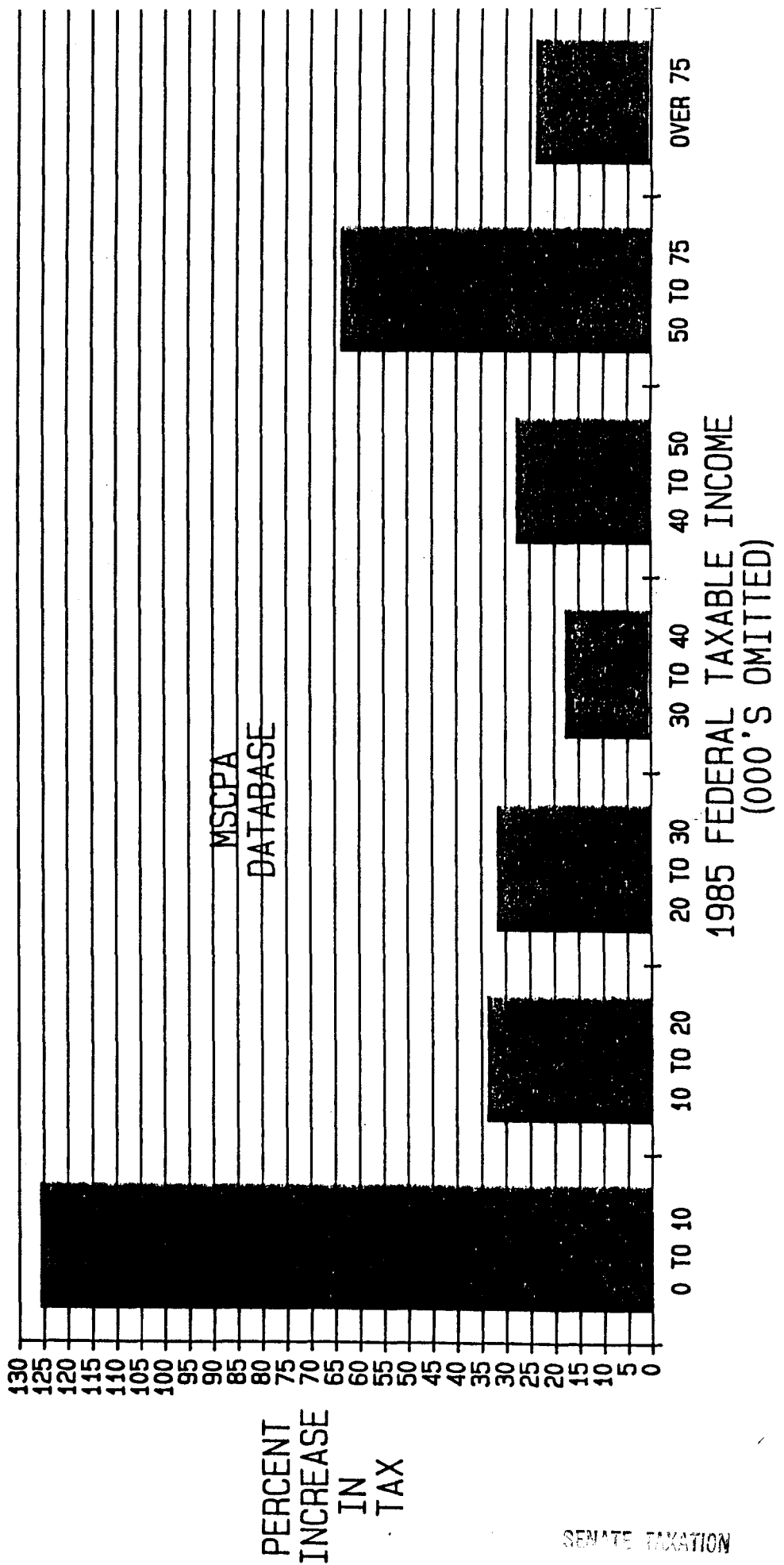
SENATE TAXATION

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DATE 2-24-87

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PERCENTAGE INCREASE IN 1988 MONTANA
TAXES WITH NO CHANGE IN MONTANA TAX
LAW COMPARED TO 1985 TAXES PAID



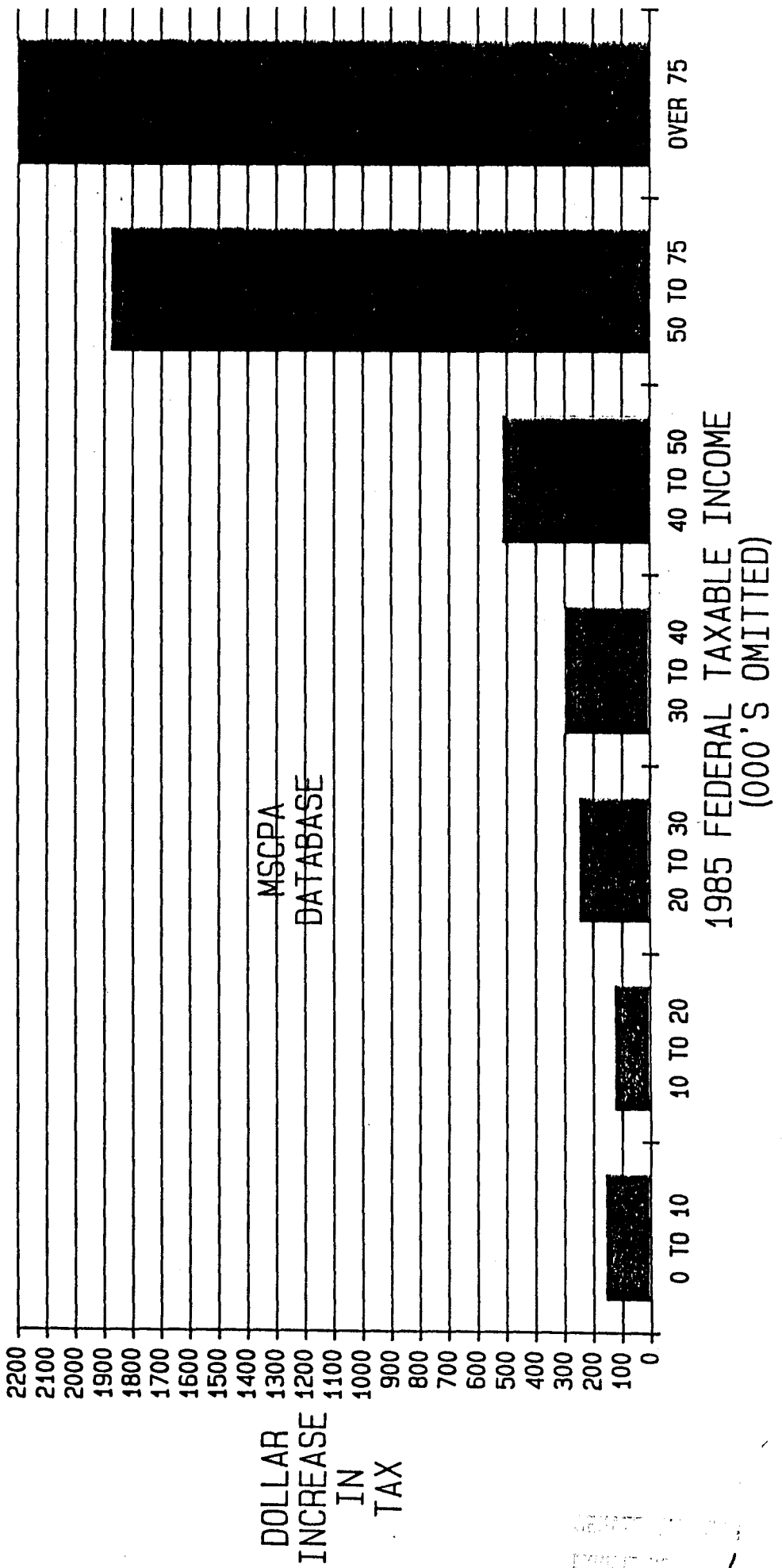
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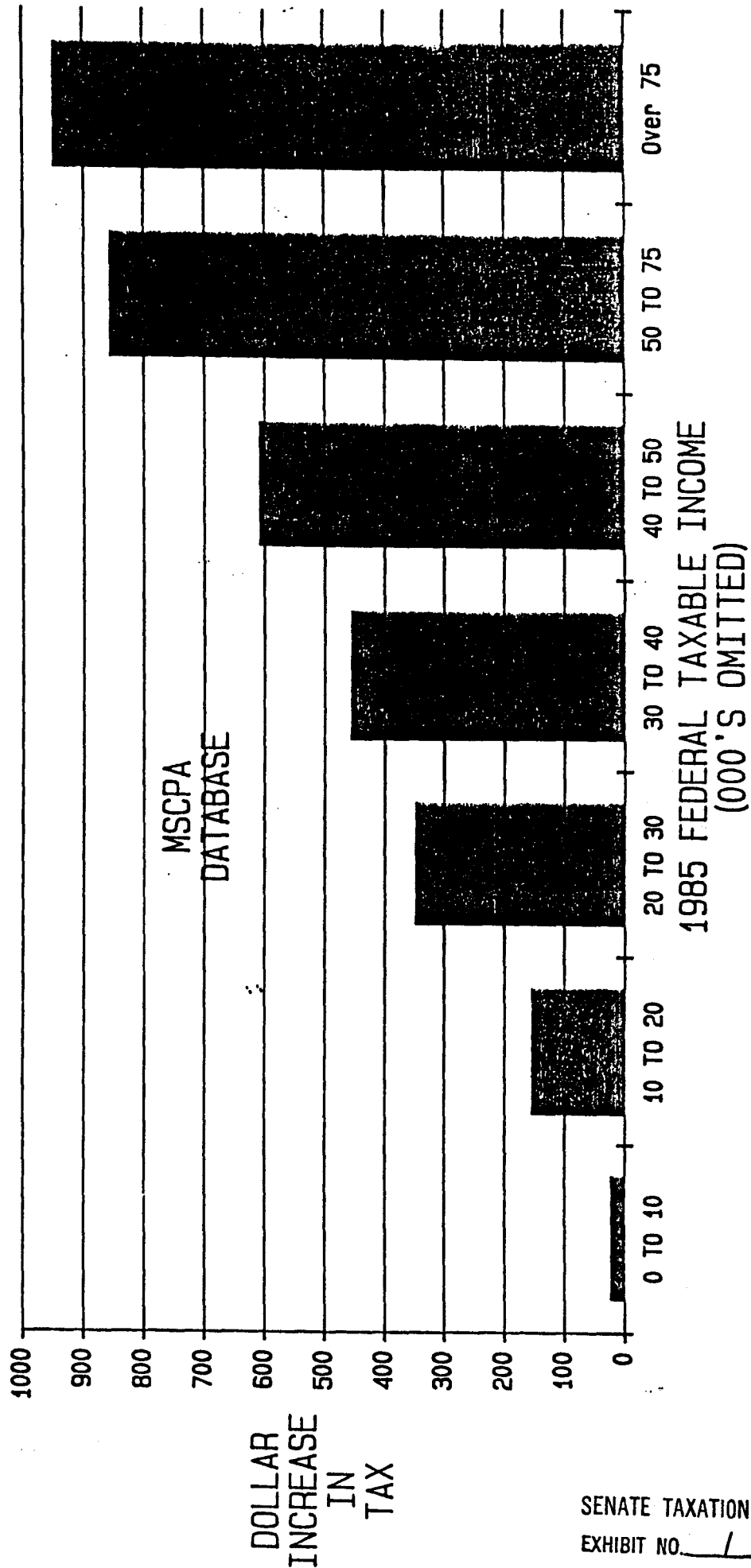
DATE 2-24-87

BILL NO. S.B. 301

AVERAGE DOLLAR INCREASE IN 1988 MONTANA TAXES
WITH NO CHANGE IN MONTANA TAX LAW
COMPARED TO 1985 TAXES PAID



AVERAGE DOLLAR INCREASE IN 1988 MONTANA TAXES
 UNDER GOVERNOR'S TAX PROPOSAL
 COMPARED TO 1988 MONTANA TAXES WITH NO
 CHANGE IN MONTANA TAX LAW



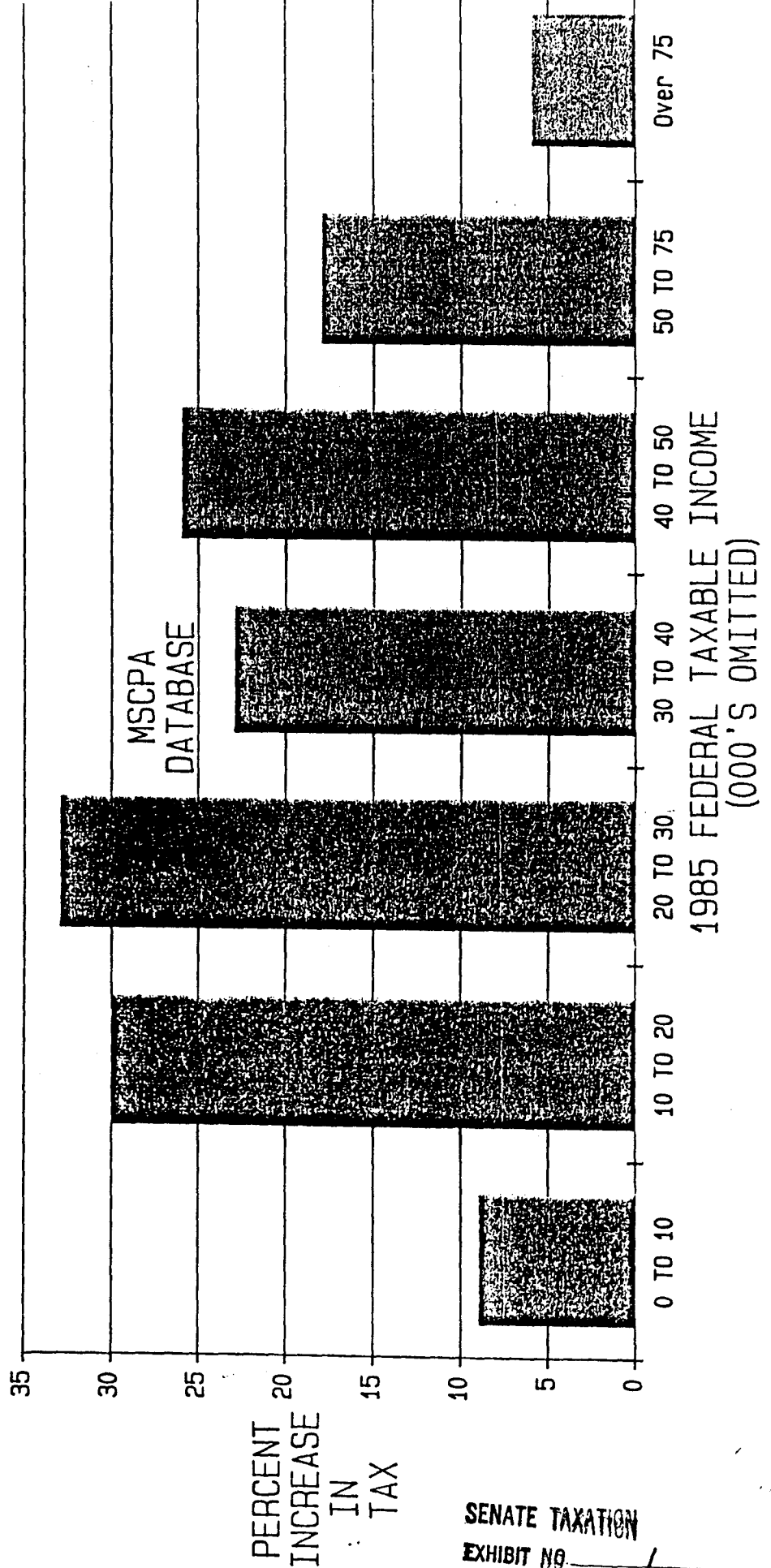
SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. 307

PERCENTAGE INCREASE IN 1988 MONTANA
TAXES UNDER GOVERNOR'S TAX PROPOSAL
COMPARED TO 1988 TAXES WITH NO CHANGE
IN MONTANA TAX LAW



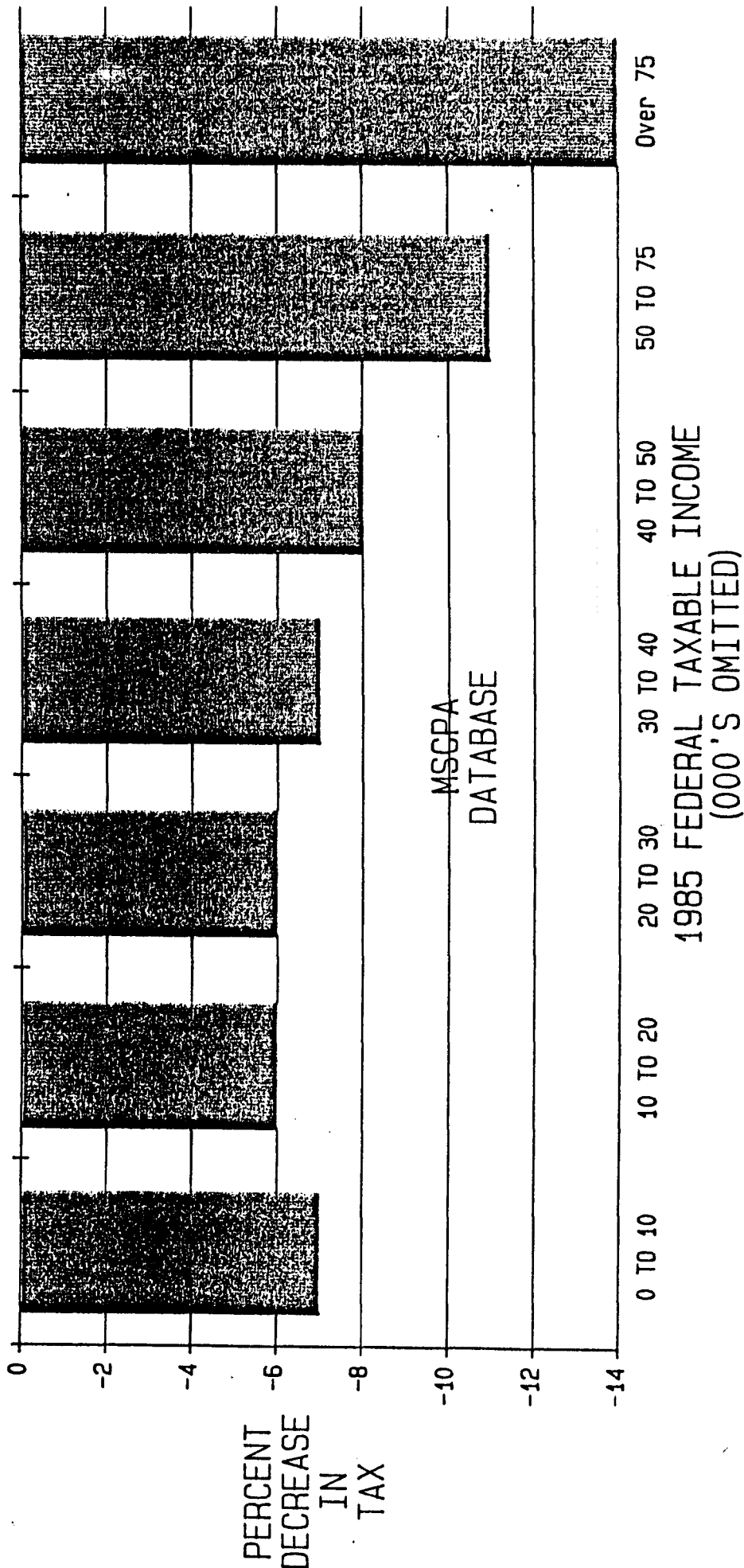
SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 301

PERCENTAGE DECREASE IN MONTANA
TAXES UNDER REP. RAMIREZ TAX
PROPOSAL COMPARED TO 1988 TAXES WITH NO
CHANGE IN MONTANA TAX LAW



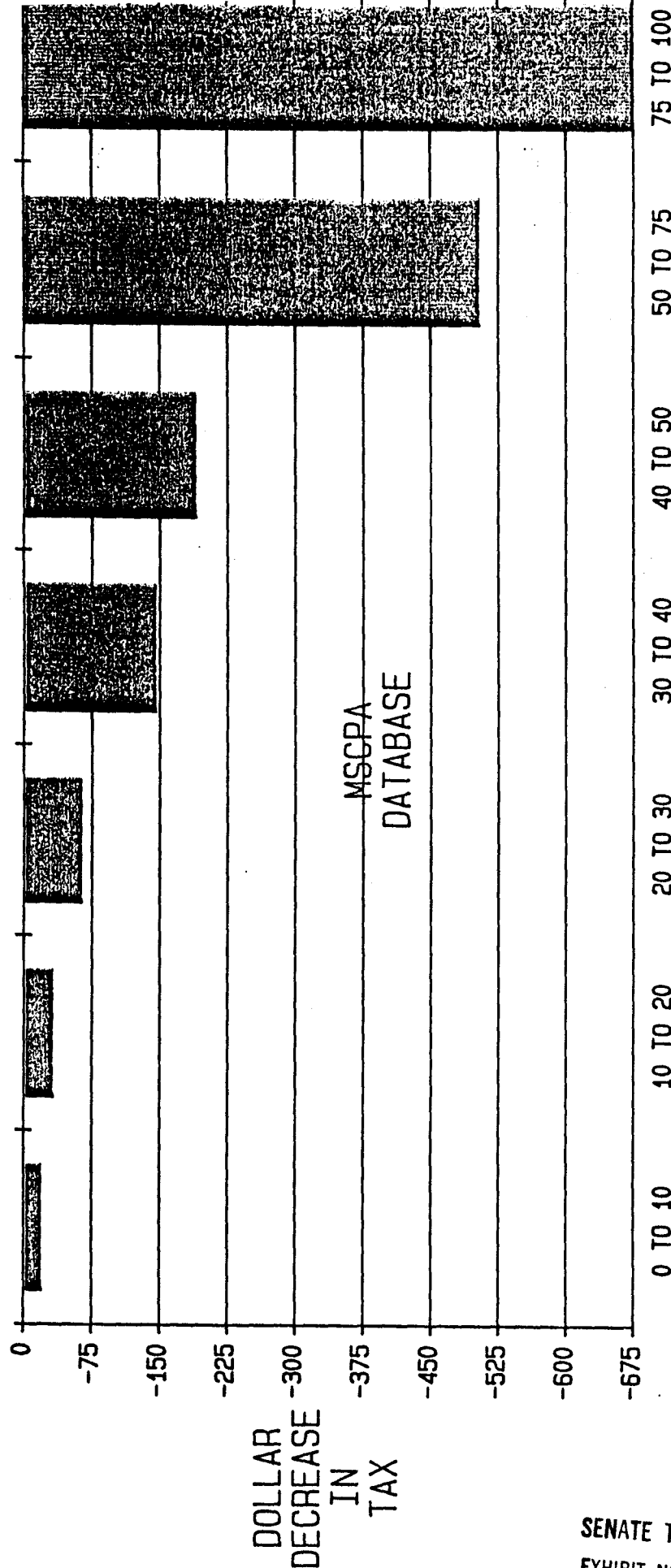
SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 367

AVERAGE DOLLAR DECREASE IN 1988 MONTANA TAXES
 UNDER REP. RAMIREZ TAX PROPOSAL
 COMPARED TO 1988 MONTANA TAXES WITH NO
 CHANGE IN MONTANA TAX LAW



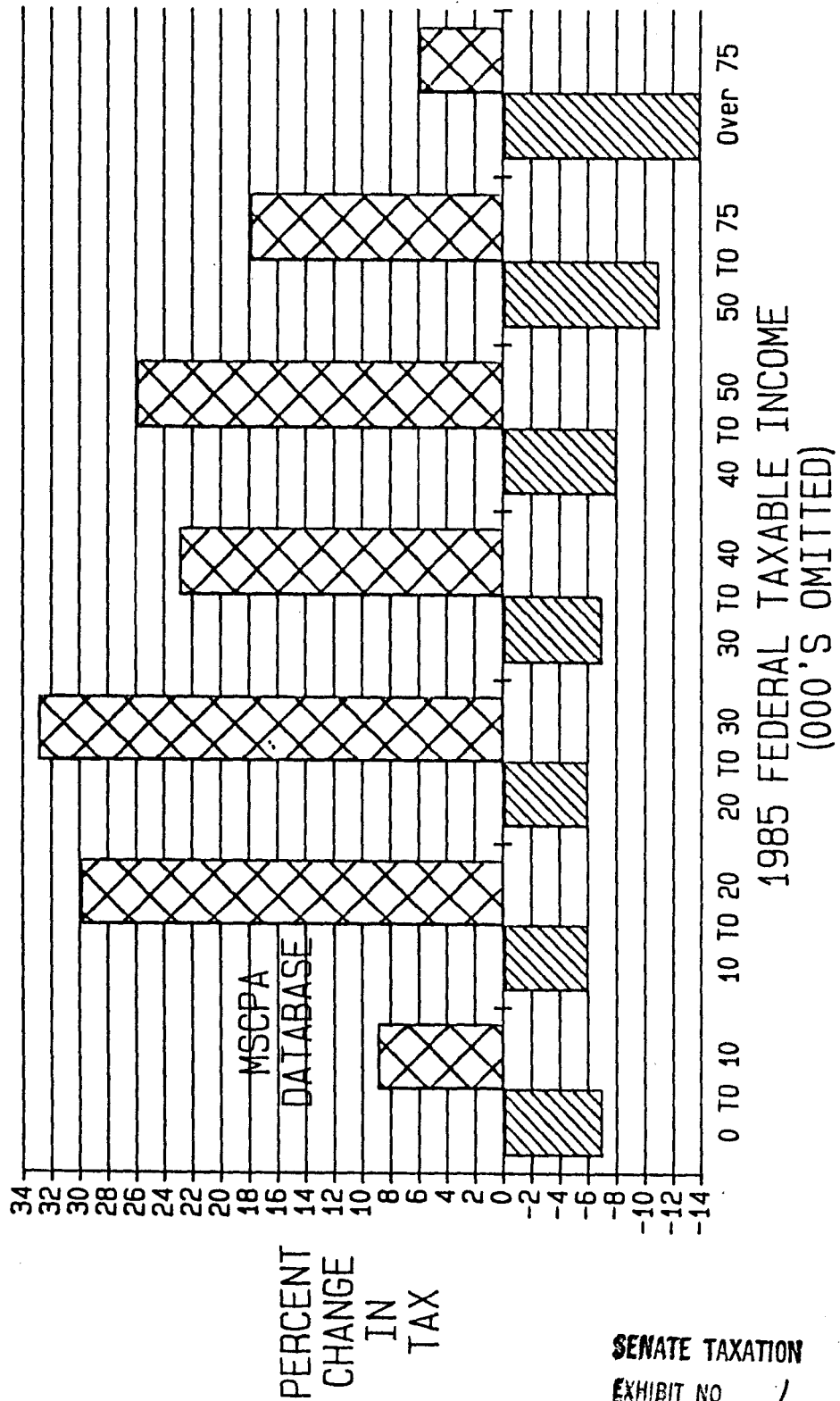
SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

PERCENTAGE CHANGE IN MONTANA TAXES
UNDER REP. RAMIREZ' BILL
AND UNDER THE GOVERNOR'S BILL
COMPARED TO 1988 TAXES WITH NO MT TAX LAW CHANGE



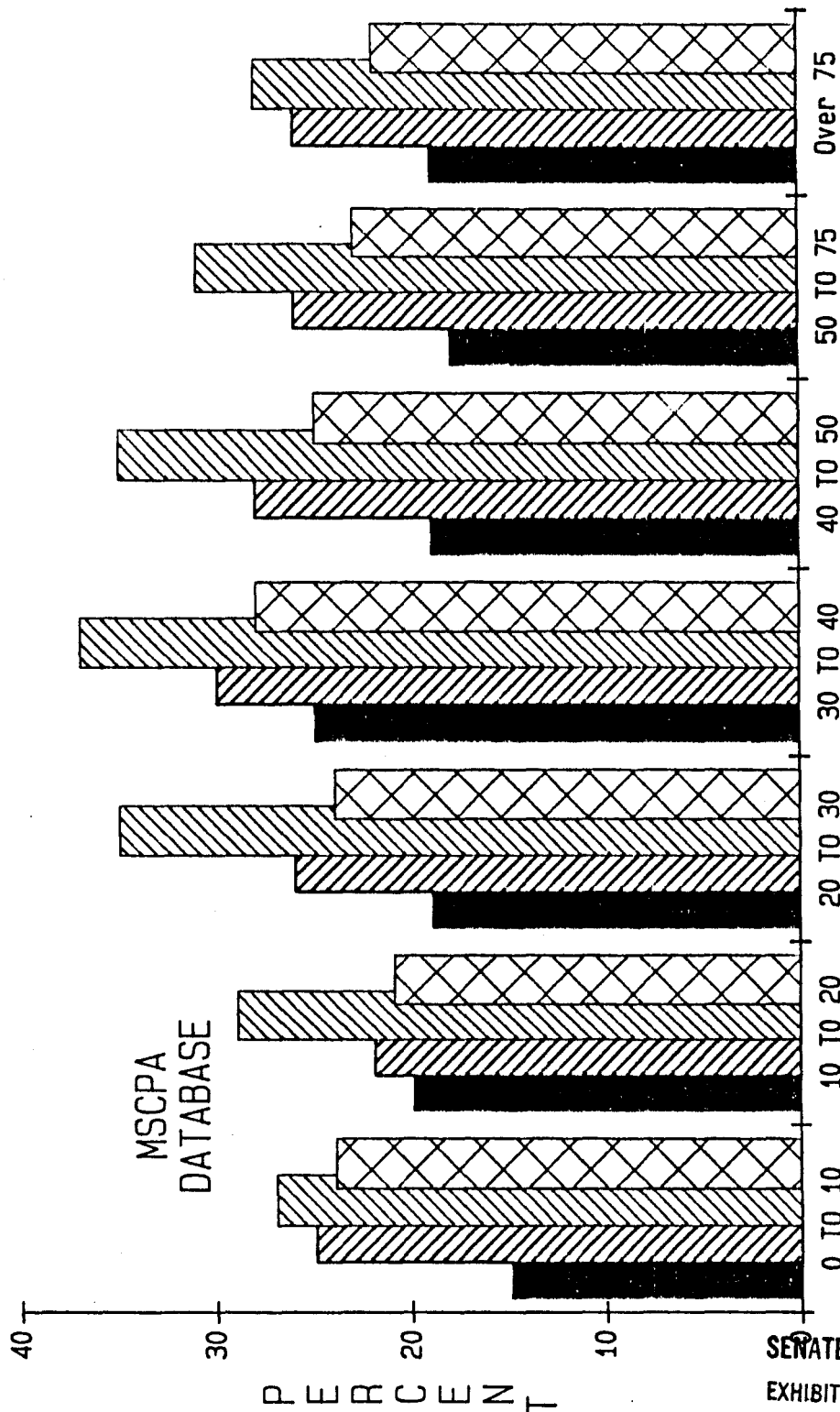
SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

PERCENT OF MONTANA TAX TO FEDERAL TAX



1985 FEDERAL TAXABLE INCOME
(000'S OMITTED)

SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO S.R. 387

SENATE TAXATION

EXHIBIT NO. 1DATE 2-24-87BILL NO. S.B. 307

SELECTED DATABASE ATTRIBUTES

Number of returns in database

with 1985 Federal taxable income between:

| | | |
|---|----|--------------|
| below 0 | 40 | |
| 0 - 10,000 | 78 | |
| 10,000 - 20,000 | 84 | |
| 20,000 - 30,000 | 83 | |
| 30,000 - 40,000 | 79 | |
| 40,000 - 50,000 | 44 | |
| 50,000 - 75,000 | 46 | |
| over 75,000 | 46 | |
| | | 500 |
| Number of preparers submitting returns | | 62 |
| Number of self-employed businesses included | | 191 |
| Number of farmers or ranchers included | | 68 |
| Number of returns where at least one taxpayer is retired | | 96 |
| Number of returns claiming IRA deductions | | |
| - single status, AGI more than \$35,000 | | 10 |
| - married status, AGI more than \$50,000 | | 84 |
| Number of returns which include taxable unemployment benefits | | 9 |
| Number of returns with a Federal filing status of "married filing joint" and a Montana filing status of "married filing separately on one form" | | 259 |
| Number of returns claiming exclusions for retirement benefits | | |
| - Railroad retirement | 5 | |
| - PERS/Teachers retirement | 24 | |
| - Other | 60 | |
| | | 89 |
| Number of returns claiming elderly interest exclusion | | 92 |
| Number of returns claiming passive losses | | 24 |
| Number of returns claiming exemptions for children | | 476 |
| Number of returns showing profits on Schedule C | | 145 |
| Number of returns showing losses on Schedule C | | 46 |
| Number of returns showing profits on Schedule F | | 28 |
| Number of returns showing losses on Schedule F | | 49 |
| Number of returns showing long-term capital gains deductions | | 221 |
| Total amount of 1985 Federal taxable income | | \$18,127,394 |
| Total amount of Federal tax paid (1985) | | \$ 5,122,623 |
| Total amount of Federal taxes claimed as itemized deductions on Montana returns | | \$ 5,664,469 |
| Total amount of 1985 Montana taxable income | | \$11,451,013 |
| Total amount of 1985 Montana income taxes paid | | \$ 1,026,105 |

We extend special recognition to the following people for the commitment and personal sacrifice they exhibited to complete the database used in this report.

Kent Borglum
Coordinator

Roger Stone
Great Falls Vo-Tech
Programming and Illustration

Bill Eidel
Junkermier, Clark, Campanella, Stevens PC
Graphics

Ron Aker
Technical

Pat Hanley
Technical

The Junkermier, Clark, Campanella, Stevens firm for the support provided to Kent and the Task Force

The 62 MSCPA firms who provided the tax return information to develop the database.

Others involved:

Fletcher Mulvaney and Edward Clinch
Galusha, Higgins & Galusha

Bonnie Swanson and Kathy Johnson
Anderson ZurMuehlen & Co. PC

Kirsten Johnson
Peat, Marwick, Mitchell & Co.

Monte Malnaa

SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. 00

Aggie Hamilton.



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MONTANA SOCIETY OF CERTIFIED PUBLIC ACCOUNTANTS

SUPPLEMENTAL INFORMATION

TO THE REPORT TO MONTANA LEGISLATORS

BY THE

MONTANA SOCIETY OF CERTIFIED PUBLIC ACCOUNTANTS

MARCH 3, 1987

SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

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MONTANA SOCIETY OF CERTIFIED PUBLIC ACCOUNTANTS

Supplemental Information to the Report to Montana Legislators

The MSCPA has prepared an analysis of information based on 1985 individual income tax returns. It reflects income tax effects of the 1986 Tax Reform Act on certain Montana taxpayers. The analysis was delivered to the Senate Taxation Committee February 24, 1987. At the time the information was presented, committee members requested the MSCPA to provide additional information. The attached supplemental information was developed in response to the request.

The supplemental information consists primarily of the following:

- o Additional graphical information with respect to the analysis presented in the February 24, 1987 report.
- o Specified information presented in tabular form providing additional detail with respect to the graphical information presented in the February 24, 1987 report.
- o Calculations of income taxes for hypothetical income taxpayers based upon 1985 income tax and related narrative comments.

As stated in the transmittal letter for the February 24, 1987 report, the purpose of this presentation is to provide additional data to assist in the analysis of various tax proposals. Members of the Montana Society of CPAs are available to discuss this information in more detail.

Members of the Montana Society of CPAs appreciate the opportunity to present this information to you.

Helena, Montana
March 3, 1987

SENATE TAXATION

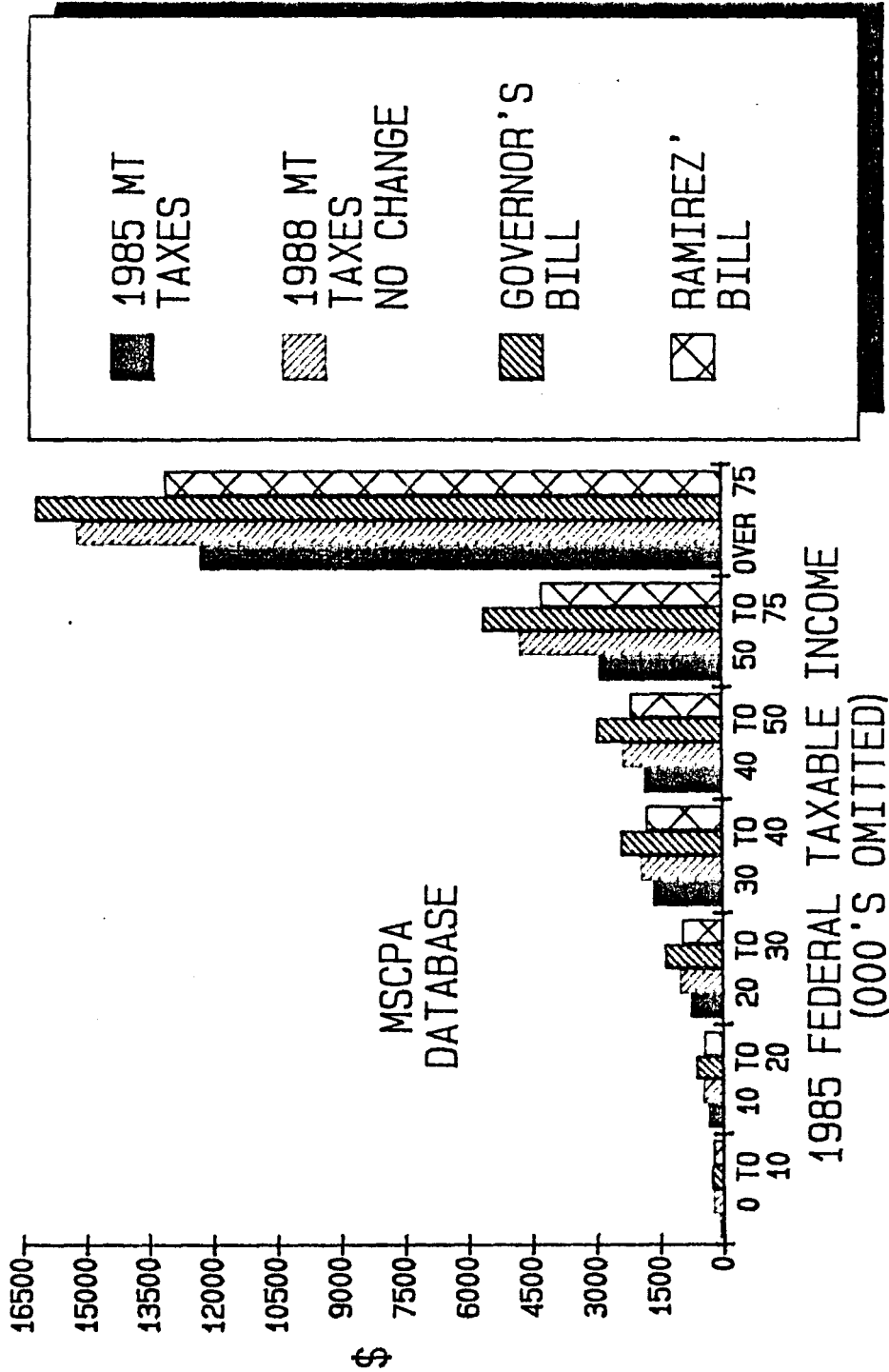
EXHIBIT NO. /

DATE 2-24-87

BILL NO. S.B. 307

Montana Society of
Certified Public Accountants

MONTANA TAXES COMPARING VARIOUS PROPOSALS



AVERAGE TAXES PAID, TOTALS

| TAXABLE INCOME | MONTANA TAX 1985 | MONTANA TAX 1988 | MONTANA TAX GOVERNOR | MONTANA TAX RAMIREZ | FEDERAL TAX 1988 | FEDERAL TAX 1985 |
|----------------|------------------|------------------|----------------------|---------------------|------------------|------------------|
| 0 TO 10 | 129 | 291 | 316 | 272 | 1,152 | 869 |
| 10 TO 20 | 382 | 513 | 669 | 481 | 2,340 | 1,895 |
| 20 TO 30 | 798 | 1,051 | 1,400 | 987 | 4,041 | 4,157 |
| 30 TO 40 | 1,667 | 1,971 | 2,428 | 1,825 | 6,592 | 6,669 |
| 40 TO 50 | 1,867 | 2,386 | 2,956 | 2,195 | 8,636 | 9,632 |
| 50 TO 75 | 2,915 | 4,794 | 5,652 | 4,289 | 18,319 | 16,075 |
| OVER 75 | 12,286 | 15,222 | 16,173 | 13,105 | 58,226 | 62,532 |

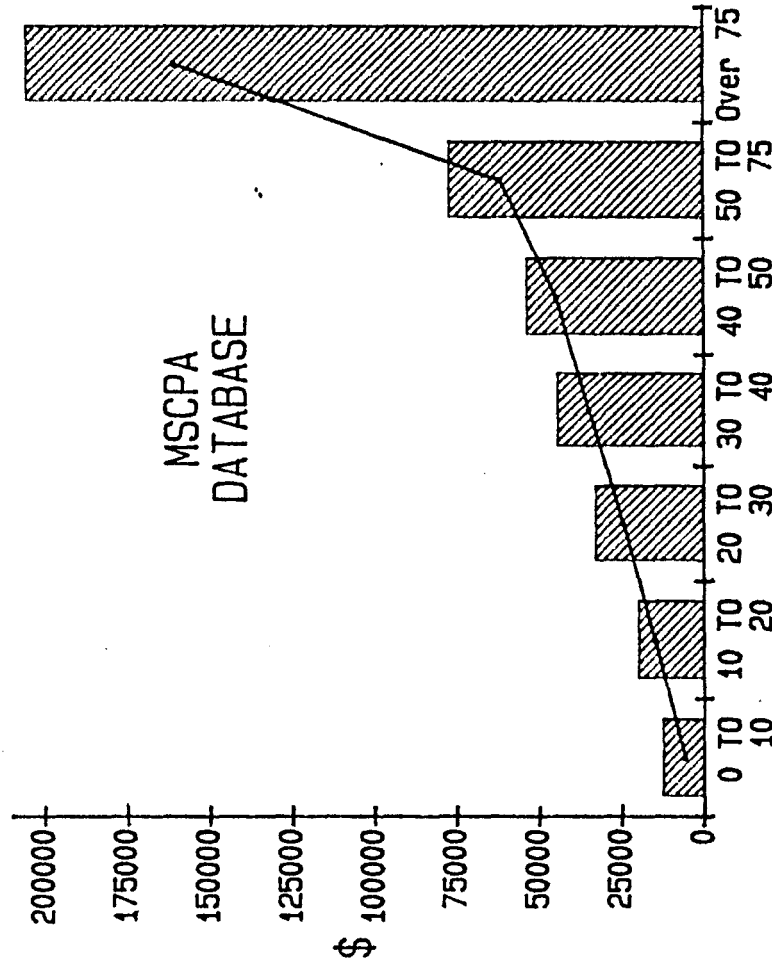
SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

1985 FEDERAL AGI COMPARED TO 1985 FEDERAL TAXABLE INCOME



1985 FEDERAL TAXABLE INCOME
 (000'S OMITTED)

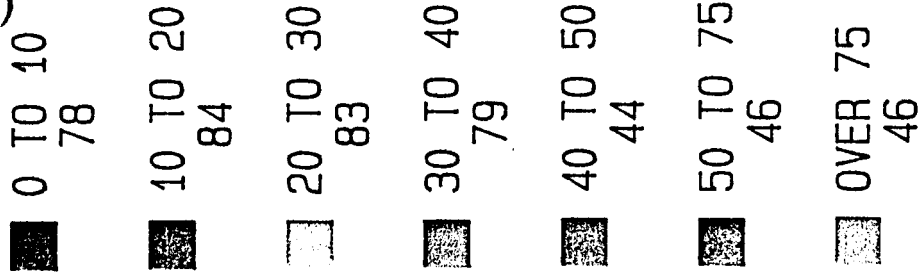
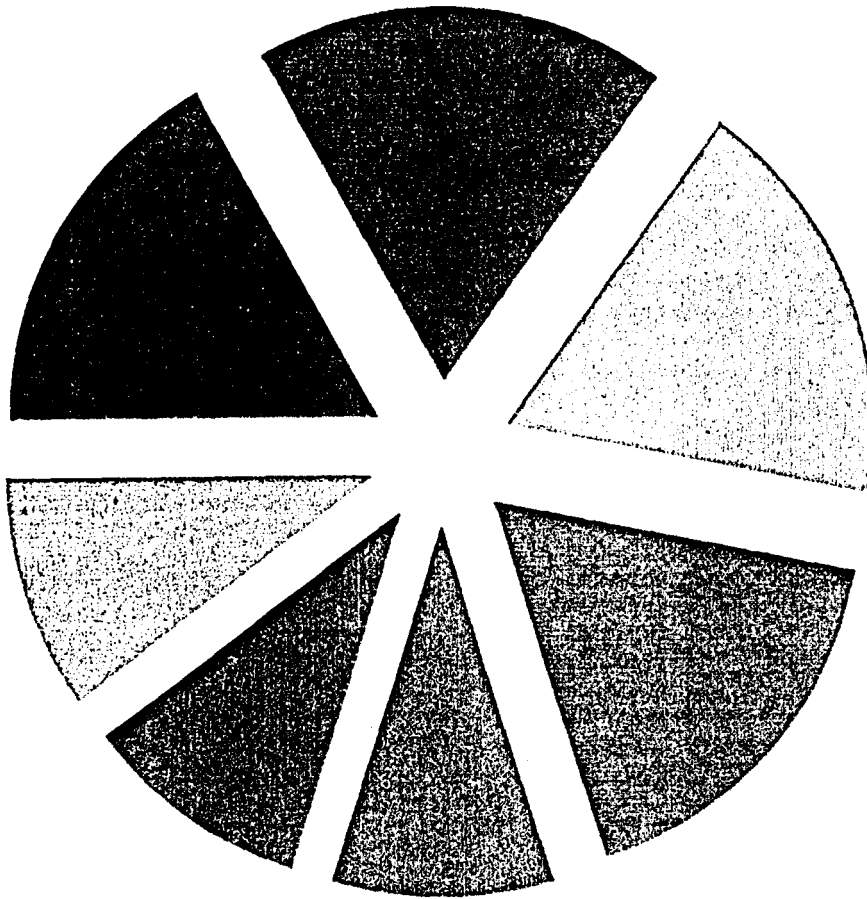
SENATE TAXATION

COMMITTEE ON

2-24-87

5.B. 207

MSCPA NUMBER OF RETURNS BY INCOME DATABASE



TOTAL TAXES PAID BY BRACKET

| TAXABLE INCOME | MONTANA TAX 1985 | MONTANA TAX 1988 | MONTANA TAX GOVERNOR | MONTANA TAX ROMIREZ | FEDERAL TAX 1988 | FEDERAL TAX 1985 | NUMBER IN EACH RANGE |
|----------------|------------------|------------------|----------------------|---------------------|------------------|------------------|----------------------|
| 0 TO 10 | 10,049 | 22,707 | 24,640 | 21,201 | 89,871 | 67,786 | 78 |
| 10 TO 20 | 32,105 | 43,095 | 56,202 | 40,418 | 196,528 | 159,177 | 84 |
| 20 TO 30 | 66,263 | 87,226 | 116,209 | 81,904 | 335,428 | 345,046 | 83 |
| 30 TO 40 | 131,713 | 155,702 | 191,797 | 144,186 | 520,790 | 526,834 | 79 |
| 40 TO 50 | 82,169 | 105,002 | 131,830 | 96,578 | 379,985 | 423,829 | 44 |
| 50 TO 75 | 134,110 | 220,543 | 259,991 | 197,308 | 842,696 | 739,465 | 46 |
| OVER 75 | 565,153 | 700,191 | 743,951 | 602,842 | 2,678,388 | 2,876,475 | 46 |

PRIVATE TAXATION
 2-24-87
 S.B. 307

NUMBER OF TAXPAYERS WHO HAVE A CHANGE IN TAXES BY BRACKET

| TAXABLE INCOME | NO CHANGE IN TAX LAW | GOVERNOR'S CHANGE | RAMIREZ' CHANGE |
|-------------------|-------------------------|----------------------|--------------------|
| 0 TO 10 | INCREASE | 47 | 41 |
| | NO CHANGE | 13 | 9 |
| | DECREASE | 18 | 28 |
| 10 TO 20 | INCREASE | 62 | 60 |
| | NO CHANGE | 6 | 1 |
| | DECREASE | 16 | 23 |
| 20 TO 30 | INCREASE | 71 | 76 |
| | NO CHANGE | 3 | 0 |
| | DECREASE | 9 | 7 |
| 30 TO 40 | INCREASE | 68 | 71 |
| | NO CHANGE | 1 | 0 |
| | DECREASE | 10 | 8 |
| 40 TO 50 | INCREASE | 38 | 43 |
| | NO CHANGE | 1 | 0 |
| | DECREASE | 5 | 1 |
| 50 TO 75 | INCREASE | 46 | 43 |
| | NO CHANGE | 0 | 0 |
| | DECREASE | 0 | 3 |
| OVER 75 | INCREASE | 42 | 36 |
| | NO CHANGE | 1 | 0 |
| | DECREASE | 3 | 10 |

SENATE JOURNAL

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

MSCPA DATABASE

LARGEST INCREASE (DECREASE) AND AVERAGE CHANGE
FROM 1985 MONTANA INCOME TAXES BY BRACKET

| TAXABLE INCOME | | NO CHANGE IN TAX LAW | GOVERNOR'S CHANGE | RAMIREZ' CHANGE |
|-------------------|------------------|-------------------------|----------------------|--------------------|
| 0 TO 10 | LARGEST INCREASE | 2,504 | 943 | 21 |
| | LARGEST DECREASE | (320) | (706) | 242 |
| | AVERAGE | 162 | 25 | (19) |
| 10 TO 20 | LARGEST INCREASE | 5,141 | 3,502 | 0 |
| | LARGEST DECREASE | (4,821) | (1,162) | (586) |
| | AVERAGE | 131 | 156 | (32) |
| 20 TO 30 | LARGEST INCREASE | 4,211 | 1,817 | 21 |
| | LARGEST DECREASE | (1,033) | (2,703) | (527) |
| | AVERAGE | 253 | 349 | (64) |
| 30 TO 40 | LARGEST INCREASE | 11,147 | 2,276 | 0 |
| | LARGEST DECREASE | (7,300) | (3,121) | (1,991) |
| | AVERAGE | 304 | 457 | (146) |
| 40 TO 50 | LARGEST INCREASE | 10,189 | 2,571 | 0 |
| | LARGEST DECREASE | (630) | (7,236) | 1,509 |
| | AVERAGE | 519 | 610 | (191) |
| 50 TO 75 | LARGEST INCREASE | 35,815 | 4,236 | 0 |
| | LARGEST DECREASE | 10 | (4,241) | 5,456 |
| | AVERAGE | 1,879 | 858 | (505) |
| OVER 75 | LARGEST INCREASE | 53,376 | 25,800 | 0 |
| | LARGEST DECREASE | (2,499) | (11,599) | (13,480) |
| | AVERAGE | 2,936 | 951 | (2,116) |

EXHIBIT NO. 1
DATE 2-24-87
ILL NO. 5.B.307

Narrative Comments on Individual Income Tax Calculations

These comments summarize and provide some general observations with respect to the attached calculations for seventeen hypothetical individual Montana taxpayers; the comments on the individual calculations should be read in conjunction with the calculations. The purpose of the individual calculations and this explanation is to provide an insight to the tax implications for Montana residents from the Tax Reform Act of 1986 and various other Montana income tax proposals.

The comments are intended to assist you in understanding the detail calculations attached. The taxpayer categories were selected arbitrarily to reflect the impact on various income groups and types to taxpayers. These profiles are not intended to be a representative portrayal of all Montana taxpayers.

Taxpayers Not Required to File Returns or Pay Tax for Montana

The following table presents the minimum income levels for which Montana residents are required to file a Montana income tax return in 1985, 1988, (current law and the Ramirez HB 444), and under the Governor's proposal.

| | Single | Married with no children | Married with two children | Married with both over 65 | Head of Household with two children |
|---|----------|-----------------------------|------------------------------|------------------------------|--|
| Montana 1985 and 1988 | \$ 1,300 | 2,600* | 5,200* | 5,200* | 3,900* |
| Montana - Governor's proposal - 1988 | 4,950** | 8,900** | 12,800** | 10,100** | 10,250** |

* Ignores any inflation adjustment for 1988

**Does not reflect the filing requirement to obtain proposed residential property tax credit.

The table above is useful in analyzing the impact of the Tax Reform Act of 1986 and proposed Montana changes on low income taxpayers. It appears the Governor's proposal would drop a significant number of individuals from the tax rolls.

SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

Taxpayer Calculations and Assumptions

The attached individual income tax calculations are based upon hypothetical data. The intention of the presentation is to provide a view as to how changes and proposed changes in the Federal and Montana tax law may affect different taxpayers. The hypothetical information and presentation of information has been simplified in an attempt to provide both useful and concise information.

The following assumptions have been used in the attached calculations:

1. Taxpayers who did not itemize for Federal Income tax did not itemize on Montana.
2. Taxpayers itemizing for Federal purposes were assumed to have a state income tax deduction (Montana tax deducted on Federal returns) equal to 15% of total Federal itemized deductions.
3. For the Residential Property Tax Credit calculation, it was assumed "Total Income" equaled "Gross Household Income" and property tax paid (or rent equivalent) was as follows:

| Total Income | Property Tax |
|----------------------|--------------|
| <hr/> | |
| < \$10,000 | \$400 |
| \$10,000 to \$19,999 | \$600 |
| \$20,000 to \$29,999 | \$800 |
| \$30,000 to \$45,000 | \$1,000 |

4. The Federal income tax deduction for Montana itemizers is equal to Federal income tax calculated for the respective year.
5. Taxpayers making an IRA contribution in 1985 qualified to deduct a contribution in 1988.
6. Alternative minimum tax implications have been ignored to simplify the presentation. However, the alternative minimum tax under the Governor's proposal may have a significant impact on some taxpayers.

SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

Comments on Calculations for Hypothetical Taxpayers

Low Income Taxpayers (pages 11 and 12)

The calculations for the low income group are included on pages 11 and 12 of the attached calculations. The low income group includes calculations for three taxpayers with total income ranging from \$2,500 to \$7,500. 1985 Federal taxable income ranges from \$1,460 to \$3,190. The first low income calculation is for a student with \$2,500 of wage income. The 1985 Montana tax of \$19 decreases a small amount under both the 1988 current law and the Ramirez bill. The student's Montana tax is eliminated under the Governor's proposal. The student receives no benefit from the residential property tax credit under the Governor's proposal: students are specifically excluded from qualification.

The other two wage earners in the low income category remain at zero tax or show slight decreases under the 1988 current law and the Ramirez bill. Both of these taxpayers qualify for the residential property tax credit under the Governor's bill and would receive refunds under this proposal in the \$300 - \$400 range.

Middle Income Taxpayers (pages 11 and 12)

This group includes three married taxpayers each with two dependent children. Total income ranges from \$10,000 to \$20,000 for the group and 1985 Federal taxable income ranges from \$5,840 to \$15,340. These taxpayers show decreasing levels of income tax under all of the proposals. Two of the lower income taxpayers included in this group qualify for the residential property tax credit under the Governor's proposal.

SUMMARY OF INDIVIDUAL INCOME TAX FOR TAXPAYERS BASED UPON VARIOUS ASSUMED INCOME AND DEDUCTION LEVELS

| Taxpayer: Job Description Spouse: Job Description Filing Status Exemptions | LOW INCOME | | | | MIDDLE INCOME | | | |
|---|--------------|--------------------------|--------------------------|--------------------------|--------------------------|--------------------------|--------------------------|--------------------------|
| | STUDENT | WAGE EARNER HOMEMAKER | WAGE EARNER HOMEMAKER | WAGE EARNER HOMEMAKER | WAGE EARNER HOMEMAKER | WAGE EARNER HOMEMAKER | WAGE EARNER HOMEMAKER | WAGE EARNER HOMEMAKER |
| | Single 1 | Joint 4 | Joint 4 | Joint 4 | Joint 4 | Joint 4 | Joint 4 | Joint 4 |
| 1985 Federal Taxable Income | \$1,460 | \$840 | \$3,190 | \$5,840 | \$10,840 | \$15,340 | | |
| 1985 Fed Tax | \$0 | \$0 | \$0 | \$254 | \$913 | \$1,602 | | |
| 1985 MT Taxable Inc:Taxpayer :Spouse | \$960 \$0 | (\$160) \$0 | \$1,680 \$160 | \$3,840 \$0 | \$7,840 \$0 | \$8,880 \$2,960 | | |
| 1985 MT Taxable Inc:Combined | \$960 | (\$160) | \$1,840 | \$3,840 | \$7,840 | \$11,840 | | |
| 1988 MT Taxable Inc:Taxpayer :Spouse | \$920 \$0 | (\$320) \$0 | \$1,560 \$120 | \$3,680 \$0 | \$7,680 \$0 | \$8,760 \$2,920 | | |
| 1988 MT Taxable Inc:Combined | \$920 | (\$320) | \$1,680 | \$3,680 | \$7,680 | \$11,680 | | |
| Montana Taxable Income - Gov | (\$2,450) | (\$7,000) | (\$5,300) | (\$2,800) | \$2,200 | \$7,200 | | |

MONTANA TAX AND AGGREGATE MONTANA AND FEDERAL TAX

| | | | | | | |
|----------------------------|------|------|---------|-------|---------|---------|
| 1985 Montana Tax | \$19 | \$0 | \$41 | \$115 | \$301 | \$443 |
| Montana & Federal Tax | \$19 | \$0 | \$41 | \$369 | \$1,214 | \$2,045 |
| 1988 Montana Tax | \$18 | \$0 | \$36 | \$108 | \$293 | \$434 |
| Montana & Federal Tax | \$18 | \$0 | \$36 | \$108 | \$293 | \$434 |
| 1988 Montana-Gov Tax | \$0 | ** | (\$400) | ** | \$16 | \$342 |
| Montana-Gov & Federal Tax | \$0 | ** | (\$400) | ** | \$346 | \$1,422 |
| 1988 Montana Tax - Ramirez | \$15 | \$15 | \$33 | \$99 | \$278 | \$412 |
| Montana-Ram & Federal Tax | \$15 | \$15 | \$33 | \$99 | \$278 | \$412 |

*Percentage of respective 1985 tax.
**Percentage invalid due to \$0 or negative tax.

MIDDLE INCOME

LOW INCOME

| | | | | | | |
|-------------------------------|-----------|-----------|-----------|-----------|----------|----------|
| W-2 Income (wages):Taxpayer | 2,500 | 5,000 | 6,000 | 10,000 | 15,000 | 15,000 |
| W-2 Income (wages):Spouse | 0 | 0 | 1,500 | 0 | 0 | 5,000 |
| Sch D:Gross Capital Gains | 0 | 0 | 0 | 0 | 0 | 0 |
| Long Term Gain Excl. | 0 | 0 | 0 | 0 | 0 | 0 |
| Pension Income | 0 | 0 | 0 | 0 | 0 | 0 |
| Sch E:Passive Income/(Loss) | 0 | 0 | 0 | 0 | 0 | 0 |
| Sch F:Farm Income/(Loss) | 0 | 0 | 0 | 0 | 0 | 0 |
| Other Ordinary Income/(Loss) | 0 | 0 | 0 | 0 | 0 | 0 |
| Total Income | \$2,500 | \$5,000 | \$7,500 | \$10,000 | \$15,000 | \$20,000 |
| Adjustments from Income | 0 | 0 | 150 | 0 | 0 | 500 |
| Federal Adjusted Gross Income | \$2,500 | \$5,000 | \$7,350 | \$10,000 | \$15,000 | \$19,500 |
| Itemized Deductions | 0 | 0 | 0 | 0 | 0 | 0 |
| Zero Bracket Amount | 0 | 0 | 0 | 0 | 0 | 0 |
| Exemptions | (1,040) | (4,160) | (4,160) | (4,160) | (4,160) | (4,160) |
| 1985 Federal Taxable Income | \$1,460 | \$840 | \$3,190 | \$5,840 | \$10,840 | \$15,340 |
| 1988 Federal Taxable Income | (\$2,450) | (\$7,800) | (\$5,300) | (\$2,800) | \$2,200 | \$7,200 |
| 1988 Fed Tax | \$0 | \$0 | \$0 | \$0 | \$330 | \$1,080 |
| 1988 Montana Tax - Gov | \$0 | \$0 | \$0 | \$0 | \$88 | \$342 |
| Residential property credit* | N/A | \$400 | \$344 | \$208 | \$72 | N/A |
| 1988 Montana-Gov Net Tax | \$0 | (\$400) | (\$344) | (\$208) | \$16 | \$342 |

*Computation is based upon assumptions made for illustration purposes.

SENATE LEGISLATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

High/Mid Income Taxpayers (pages 14 and 15)

This taxpayer group consists of married taxpayers filing jointly; each couple has two children. Total income ranges from \$25,000 to \$50,000; 1985 Federal taxable income ranges from \$17,380 to \$37,130. Two of the taxpayers in this group are presumed to have working spouses. All these taxpayers itemized deductions on their 1985 tax returns.

The Montana tax change in 1988 under current law and the Ramirez bill is minimal for these taxpayers. All of the taxpayers in this group show moderate percentage increases in Montana tax under the Governor's proposal. The first two taxpayer profiles reflect increases of 15% and 27% respectively under the Governor's proposal. This increase primarily is the result of the Governor's proposal to delete the current tax provision which allows spouses who have income for Montana tax purposes to file separately on one return. The increase in the exemption amount for Federal purposes in 1988 (and under the Governor's proposal) partially mitigates the increase in tax.

Farm Income/Loss (pages 14 and 15)

The three taxpayers included in this group have incomes varying from \$10,000 to \$90,000; two of the taxpayers also have capital gains (presumably from the disposition of farm land and/or breeding livestock). The first taxpayer, with \$10,000 solely from farm income, pays less than \$100 in Montana tax under the 1985 law, in 1988 under current law and the Ramirez bill. Under the Governor's proposal, this taxpayer would qualify for residential property tax credit and receive a refund of \$208.

The other two farmers, with higher income levels and capital gains, show significant increases under all Montana 1988 scenarios. This is due, primarily, to the loss of the capital gains deduction. The Governor's proposal which discontinues Federal income tax deductions also has an impact on these taxpayers.

SCHEDULE F: FARM INCOME/(LOSS)

| | | | | | | |
|-------------------------------|----------|----------|----------|-----------|----------|-----------|
| W-2 Income (wages):Taxpayer | 15,000 | 20,000 | 50,000 | 0 | 0 | 0 |
| W-2 Income (wages):Spouse | 10,000 | 15,000 | 0 | 0 | 0 | 0 |
| Sch D:Gross Capital Gains | 0 | 0 | 0 | 0 | 10,000 | 100,000 |
| Long Term Gain Excl. | 0 | 0 | 0 | 0 | (6,000) | (60,000) |
| Pension Income | 0 | 0 | 0 | 0 | 0 | 0 |
| Sch E:Passive Income/(Loss) | 0 | 0 | 0 | 0 | 0 | 0 |
| Sch F:Farm Income/(Loss) | 0 | 0 | 0 | 10,000 | 25,000 | 50,000 |
| Other Ordinary Income/(Loss) | 0 | 0 | 0 | 0 | 0 | 0 |
| Total Income | \$25,000 | \$35,000 | \$50,000 | \$10,000 | \$29,000 | \$90,000 |
| Adjustments from Income | 1,000 | 5,500 | 2,250 | 0 | 0 | 0 |
| Federal Adjusted Gross Income | \$24,000 | \$29,500 | \$47,750 | \$10,000 | \$29,000 | \$90,000 |
| Itemized Deductions | (6,000) | (7,500) | (10,000) | 0 | (6,000) | (10,000) |
| Zero Bracket Amount | 3,540 | 3,540 | 3,540 | 0 | 3,540 | 3,540 |
| Exemptions | (4,160) | (4,160) | (4,160) | (4,160) | (4,160) | (4,160) |
| 1985 Federal Taxable Income | \$17,380 | \$21,380 | \$37,130 | \$5,840 | \$22,380 | \$79,380 |
| 1988 Federal Taxable Income | \$11,200 | \$15,700 | \$29,950 | (\$2,800) | \$21,200 | \$132,200 |
| 1988 Fed Tax | \$1,680 | \$2,355 | \$4,519 | \$0 | \$3,180 | \$36,164 |
| 1988 Montana Tax - Gov | \$582 | \$926 | \$2,066 | \$0 | \$1,366 | \$10,246 |
| Residential property credit* | N/A | N/A | N/A | \$208 | N/A | N/A |
| 1988 Montana-Gov Net Tax | \$582 | \$926 | \$2,066 | (\$208) | \$1,366 | \$10,246 |

*Computation is based upon assumptions made for illustration purposes.

SEPARATE TRANSACTION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

Capital Gains (Pages 18 and 19)

This taxpayer had wage income of \$65,000, capital gains of \$100,000, and \$15,000 in other income (interest and dividend). The taxpayer shows a significant percentage and tax increase under all three of the Montana 1988 scenarios, primarily due to the losses of the capital gains exclusion and the deduction for Federal income tax under the Governor's proposal. The change in Federal capital gains tax policy appears difficult to control with a separate Montana tax policy.

Passive Income/Loss (pages 18 and 19)

The individual in this category is a high income taxpayer with significant passive losses. The taxpayer profile reflects significant increases in all three Montana tax scenarios, a result of the Federal changes affecting the deduction of passive losses.

High Income (pages 18 and 19)

This married couple has a combined wage income of \$100,000; itemized deductions of \$10,000 and IRA contributions of \$4,000. The Ramirez bill neutralizes the impact of the Tax Reform Act of 1986. Tax increases under the current law in 1988 and the Governor's proposal. The Federal income tax deduction loss is a significant factor in the increase under the Governor's proposal.

Retired Individuals (pages 18 and 19)

The first taxpayer in this group is a single, retired teacher with pension income of \$10,000 and interest income of \$3,000. This individual pays less than \$30 in Montana tax under all scenarios except for the Governor's proposal; tax liability would then be \$393. The Governor's percentage increase should be reviewed carefully in conjunction with the dollar increase. Perhaps this large percentage increase is a distortion of the dollar economic impact to this taxpayer.

The second taxpayer in this category is assumed to be a retired Montana Highway Patrolman with wage income of \$15,000, pension income of \$15,000, and \$10,000 of interest and dividend income. The taxpayer receives small decreases in Montana income tax under current law in 1988 and under the Ramirez bill. The Governor's proposal impacts the taxpayer unfavorably as a result of the elimination of preferential treatment for certain retired public employees. The Federal law does not provide preferential treatment for this type of retirement income. Such treatment is more a matter of preference than of economic or tax policy.

SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. S.B. 307

MONTANA SOCIETY OF CERTIFIED PUBLIC ACCOUNTANTS
SUMMARY OF INDIVIDUAL INCOME TAX FOR TAXPAYERS BASED UPON VARIOUS ASSUMED INCOME AND DEDUCTION LEVELS

| Taxpayer: Job Description Spouse: Job Description Filing Status Exemptions | CAPITAL GAINS | | PASSIVE LOSS | | HIGH INCOME | | RETIREMENT PERSONS: PENSION INCOME | |
|---|--|--|--|--|--|--|---|--|
| | ***** | | ***** | | ***** | | ***** | |
| | WAGE EARNER HOMEMAKER Joint 4 | WAGE EARNER HOMEMAKER Joint 4 | WAGE EARNER HOMEMAKER Joint 4 | WAGE EARNER HOMEMAKER Joint 4 | WAGE EARNER WAGE EARNER Joint 4 | WAGE EARNER WAGE EARNER Joint 4 | RETIRED TEACHER RETIRED MHP Single 1 | WAGE EARNER WAGE EARNER Joint 3 |
| 1985 Federal Taxable Income | \$102,130 | \$79,380 | \$79,380 | \$82,880 | \$82,880 | \$36,880 | \$1,960 | \$36,880 |
| 1985 Fed Tax | \$32,845 | \$22,899 | \$22,899 | \$22,403 | \$22,403 | \$6,611 | \$1,382 | \$6,611 |
| 1985 MT Taxable Inc:Taxpayer :Spouse | \$67,995 \$0 | \$55,191 \$0 | \$55,191 \$0 | \$46,703 \$14,234 | \$46,703 \$14,234 | \$1,920 \$17,010 | \$1,360 \$0 | \$1,920 \$17,010 |
| 1985 MT Taxable Inc:Combined | \$67,995 | \$55,191 | \$55,191 | \$60,937 | \$60,937 | \$18,930 | \$1,360 | \$18,930 |
| 1988 MT Taxable Inc:Taxpayer :Spouse | \$117,008 \$0 | \$93,726 \$0 | \$93,726 \$0 | \$49,628 \$15,209 | \$49,628 \$15,209 | \$1,840 \$16,970 | \$1,320 \$0 | \$1,840 \$16,970 |
| 1988 MT Taxable Inc:Combined | \$117,008 | \$93,726 | \$93,726 | \$64,837 | \$64,837 | \$18,810 | \$1,320 | \$18,810 |
| Montana Taxable Income - Gov | \$154,950 | \$120,200 | \$120,200 | \$78,200 | \$78,200 | \$30,500 | \$8,050 | \$30,500 |

MONTANA TAX AND AGGREGATE MONTANA AND FEDERAL TAX

| | | | | | | |
|----------------------------|----------|----------|----------|---------|---------|------|
| 1985 Montana Tax | \$6,178 | \$4,770 | \$4,572 | \$28 | \$1,002 | 99% |
| Montana & Federal Tax | \$39,023 | \$27,669 | \$26,975 | \$1,410 | \$7,613 | 74% |
| 1988 Montana Tax | \$11,570 | \$9,009 | \$8,972 | \$28 | \$997 | 99% |
| Montana & Federal Tax | \$55,242 | \$41,213 | \$23,315 | \$1,236 | \$5,670 | 74% |
| 1988 Montana-Gov Tax | \$12,066 | \$9,286 | \$5,926 | \$393 | \$2,110 | 210% |
| Montana-Gov & Federal Tax | \$55,738 | \$41,490 | \$24,269 | \$1,601 | \$6,783 | 89% |
| 1988 Montana Tax - Ramirez | \$9,983 | \$7,829 | \$4,523 | \$27 | \$944 | 94% |
| Montana-Ram & Federal Tax | \$53,655 | \$40,033 | \$22,866 | \$1,235 | \$5,617 | 74% |

*Percentage of respective 1985 tax.

**Percentage invalid due to \$0 or negative tax.

| | CAPITAL GAINS ***** | PASSIVE LOSS ***** | HIGH INCOME ***** | RETIRED PERSONS: PENSION INCOME ***** |
|-------------------------------|------------------------|-----------------------|----------------------|--|
| W-2 Income (wages): Taxpayer | 65,000 | 75,000 | 75,000 | 0 |
| W-2 Income (wages): Spouse | 0 | 0 | 25,000 | 0 |
| Sch D: Gross Capital Gains | 100,000 | 0 | 0 | 0 |
| Long Term Gain Excl. | (60,000) | 0 | 0 | 0 |
| Pension income | 0 | 0 | 0 | 10,000 |
| Sch E: Passive Income/(Loss) | 0 | (80,000) | 0 | 0 |
| Sch F: Farm Income/(Loss) | 0 | 0 | 0 | 0 |
| Other Ordinary Income/(Loss) | 15,000 | 100,000 | 0 | 3,000 |
| Total Income | \$120,000 | \$95,000 | \$100,000 | \$13,000 |
| Adjustments from Income | 2,250 | 0 | 6,500 | 0 |
| Federal Adjusted Gross Income | \$117,750 | \$95,000 | \$93,500 | \$13,000 |
| Itemized Deductions | (15,000) | (15,000) | (10,000) | 0 |
| Zero Bracket Amount | 3,540 | 3,540 | 3,540 | 0 |
| Exemptions | (4,160) | (4,160) | (4,160) | (3,120) |
| 1985 Federal Taxable Income | \$102,130 | \$79,380 | \$82,880 | \$11,960 |
| 1988 Federal Taxable Income | \$154,950 | \$120,200 | \$78,200 | \$8,050 |
| 1988 Fed Tax | \$43,672 | \$32,204 | \$18,343 | \$1,208 |
| 1988 Montana Tax - Gov | \$12,066 | \$9,286 | \$5,926 | \$393 |
| Residential property credit* | N/A | N/A | N/A | N/A |
| 1988 Montana-Gov Net Tax | \$12,066 | \$9,286 | \$5,926 | \$393 |

*Computation is based upon assumptions made for illustration purposes.

SENATE TAXATION

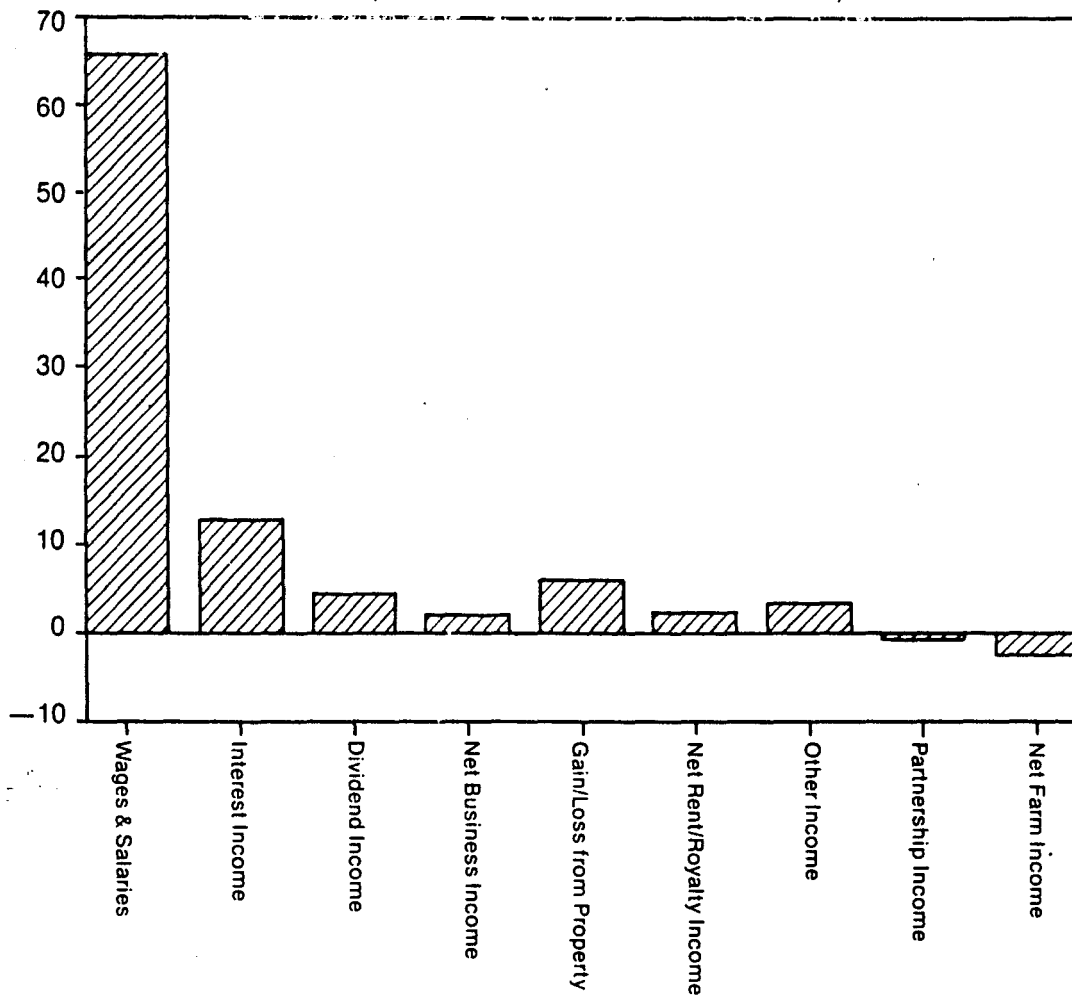
EXHIBIT NO. 1

DATE 2-24-87

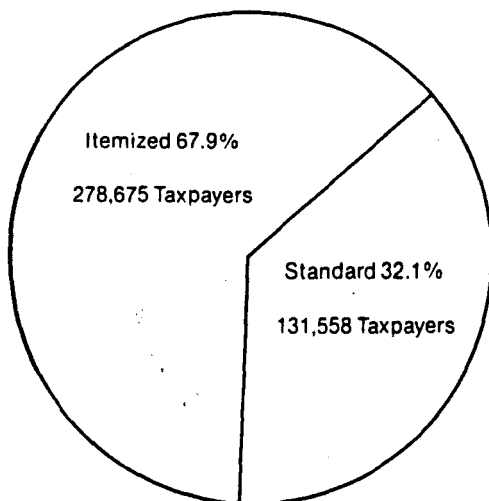
BILL NO. S.B. 307

Components of Reported Income

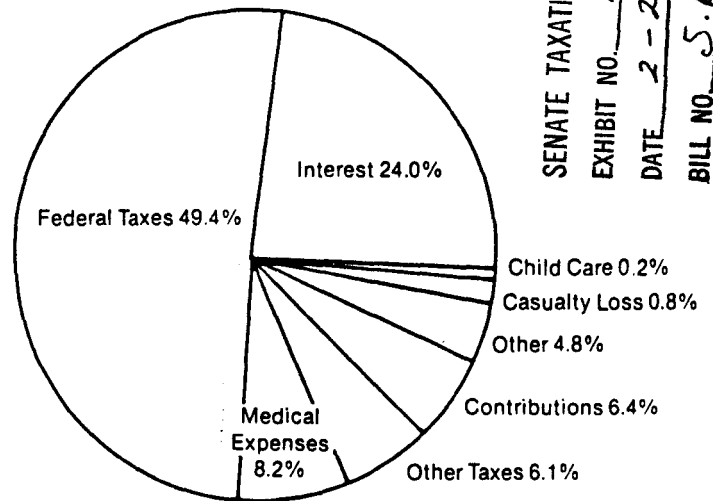
(Percent Distribution — 1982 Returns)



Deductions 1982 Returns



Number of Taxpayers Claiming Standard Deduction and Itemizing



Type of Deduction (by %) Claimed on Itemized Returns

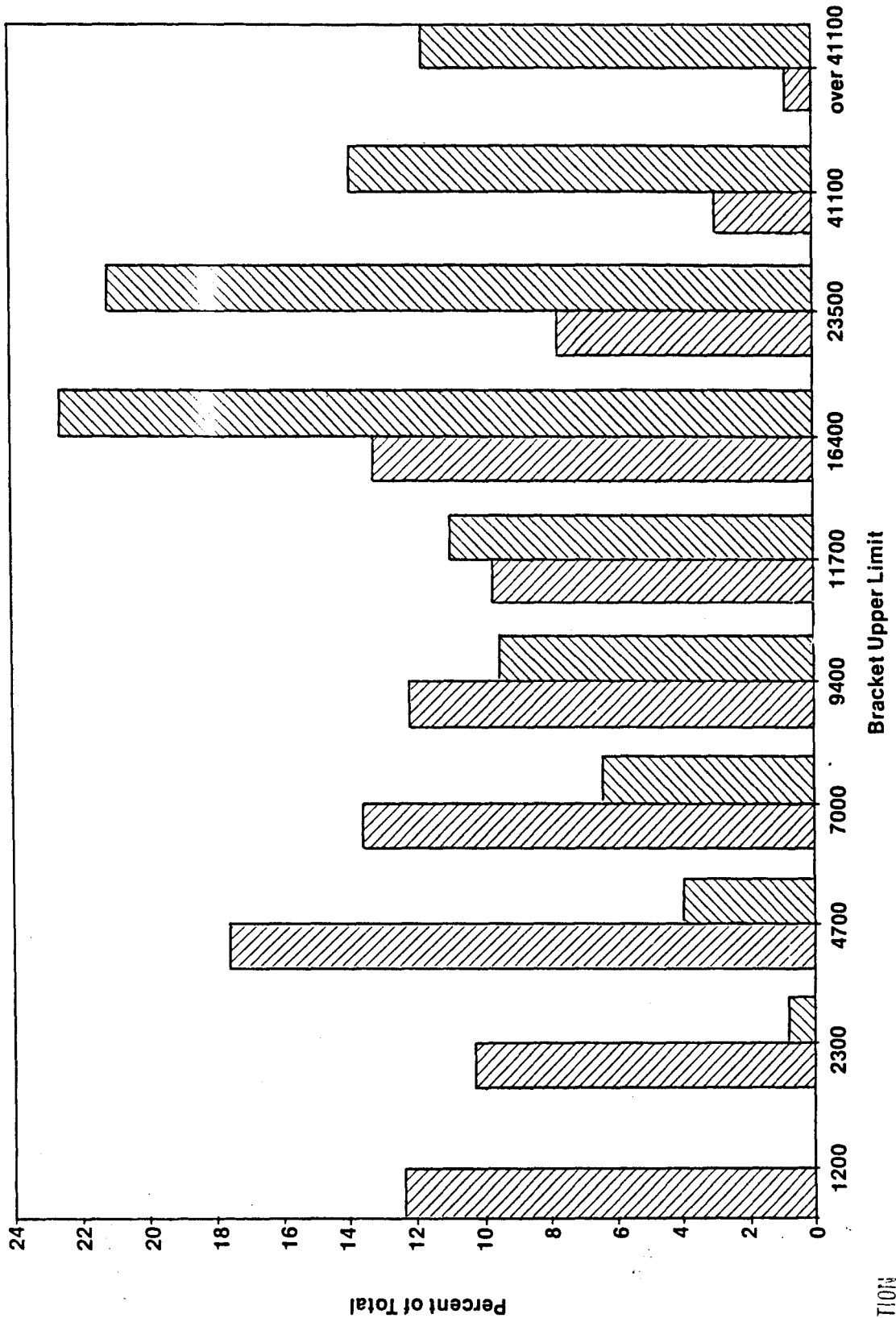
SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. 5.B. 307

Percentage of Returns and Tax Paid
(By Income Brackets in 1982)



SENATE TAXATION

EXHIBIT NO. 1

DATE 2-24-87

BILL NO. 307

Montana Individual Income Tax Returns for 1982

(Summary of Returns Received and Processed as of December 6, 1983)

| Montana Taxable Income Bracket | Number of Returns* | Total Number of Returns Showing Itemized Deductions | Total of Itemized Deductions Taken | Total Returns Showing Standard Deductions | Total of Standard Deductions Taken | Total Montana Adjusted Gross Income | Total Montana Taxable Income | Total Tax Paid By Bracket |
|--------------------------------|--------------------|---|------------------------------------|---|------------------------------------|-------------------------------------|------------------------------|---------------------------|
| < or = 0 | 55,197 | 26,566 | 214,193,940 | 28,631 | 5,459,564 | 191,271,085 | 0 | 0 |
| 1,000-1,999 | 36,557 | 15,939 | 34,400,167 | 20,618 | 8,543,938 | 109,187,365 | 18,390,994 | 376,329 |
| 2,000-2,999 | 34,557 | 16,400 | 37,929,283 | 18,157 | 12,520,873 | 149,531,146 | 51,379,363 | 1,135,864 |
| 3,000-3,999 | 29,324 | 15,429 | 41,584,017 | 13,895 | 13,447,470 | 171,293,096 | 73,007,745 | 1,907,910 |
| 4,000-4,999 | 25,601 | 14,477 | 43,230,049 | 11,124 | 13,706,821 | 185,451,914 | 89,353,619 | 2,678,027 |
| 5,000-5,999 | 23,410 | 14,448 | 49,154,556 | 8,962 | 13,356,719 | 204,778,260 | 105,203,297 | 3,399,156 |
| 6,000-6,999 | 21,280 | 13,927 | 53,445,416 | 7,353 | 12,663,998 | 217,406,738 | 116,872,243 | 4,099,211 |
| 7,000-7,999 | 19,859 | 14,404 | 58,858,713 | 5,455 | 10,384,842 | 231,594,737 | 129,096,957 | 4,826,956 |
| 8,000-8,999 | 18,739 | 14,575 | 64,996,256 | 4,164 | 10,384,842 | 246,367,475 | 140,387,998 | 5,575,185 |
| 9,000-9,999 | 17,430 | 14,237 | 68,440,163 | 3,193 | 6,879,264 | 254,163,761 | 148,003,418 | 6,230,969 |
| 10,000-10,999 | 16,687 | 14,387 | 74,546,503 | 2,300 | 5,266,855 | 268,564,529 | 158,323,930 | 6,991,594 |
| 11,000-11,999 | 14,747 | 13,015 | 73,039,379 | 1,732 | 4,187,460 | 289,507,735 | 154,691,033 | 7,200,738 |
| 12,000-12,999 | 13,827 | 12,537 | 77,642,751 | 1,290 | 3,305,560 | 266,520,669 | 158,885,907 | 7,726,542 |
| 13,000-13,999 | 11,894 | 10,924 | 73,017,436 | 970 | 2,490,911 | 247,925,334 | 148,591,847 | 7,569,880 |
| 14,000-14,999 | 10,581 | 9,855 | 70,866,383 | 726 | 1,883,052 | 237,246,308 | 142,756,331 | 7,579,512 |
| 15,000-15,999 | 9,256 | 8,696 | 66,038,809 | 560 | 1,453,760 | 221,287,501 | 134,186,414 | 7,375,020 |
| 16,000-16,999 | 8,061 | 7,618 | 61,677,637 | 443 | 1,136,960 | 205,359,005 | 124,854,349 | 7,062,211 |
| 17,000-17,999 | 6,758 | 6,455 | 56,376,350 | 303 | 786,720 | 183,537,956 | 111,364,780 | 6,467,325 |
| 18,000-18,999 | 5,615 | 5,356 | 50,151,586 | 259 | 672,320 | 161,942,218 | 98,171,640 | 5,876,337 |
| 19,000-19,999 | 4,776 | 4,561 | 44,782,955 | 215 | 538,560 | 144,678,138 | 88,253,198 | 5,425,871 |
| 20,000-20,999 | 3,795 | 3,646 | 36,570,205 | 149 | 385,440 | 119,824,584 | 73,921,633 | 4,652,990 |
| 21,000-21,999 | 3,285 | 3,164 | 34,130,974 | 121 | 290,400 | 109,434,759 | 67,304,051 | 4,326,164 |
| 22,000-22,999 | 2,644 | 2,548 | 29,020,972 | 96 | 281,600 | 92,449,451 | 56,809,610 | 3,719,484 |
| 23,000-23,999 | 2,280 | 2,170 | 25,365,691 | 110 | 156,640 | 82,489,064 | 51,259,364 | 3,411,806 |
| 24,000-24,999 | 1,811 | 1,749 | 22,038,003 | 62 | 163,680 | 69,213,518 | 42,523,960 | 2,874,839 |
| 25,000-25,999 | 1,428 | 1,361 | 18,215,081 | 67 | 105,600 | 56,806,744 | 34,956,827 | 2,407,636 |
| 26,000-26,999 | 1,255 | 1,210 | 16,875,726 | 45 | 107,360 | 52,055,175 | 31,982,806 | 2,242,035 |
| 27,000-27,999 | 1,067 | 1,021 | 14,492,821 | 46 | 103,840 | 45,448,182 | 28,271,559 | 2,014,153 |
| 28,000-28,999 | 908 | 866 | 12,849,711 | 42 | 80,960 | 40,112,878 | 24,942,120 | 1,802,355 |
| 29,000-29,999 | 786 | 751 | 11,710,880 | 35 | 36,122,585 | 36,122,585 | 22,385,134 | 1,639,620 |
| 30,000-30,999 | 631 | 599 | 10,099,829 | 32 | 77,440 | 30,330,594 | 18,599,568 | 1,379,166 |
| 31,000-31,999 | 546 | 513 | 8,332,588 | 33 | 79,200 | 26,445,529 | 16,652,936 | 1,249,274 |
| 32,000-32,999 | 460 | 431 | 7,996,611 | 29 | 70,400 | 23,685,030 | 14,490,624 | 1,098,565 |
| 33,000-33,999 | 334 | 391 | 7,221,464 | 29 | 68,640 | 21,932,253 | 13,644,179 | 1,044,397 |
| 34,000-34,999 | 308 | 309 | 6,066,714 | 25 | 66,880 | 18,109,423 | 11,195,062 | 865,019 |
| 35,000-35,999 | 298 | 279 | 5,508,781 | 25 | 66,880 | 16,966,163 | 10,622,384 | 827,556 |
| 36,000-36,999 | 254 | 238 | 5,298,599 | 16 | 35,200 | 15,215,235 | 10,578,396 | 830,779 |
| 37,000-37,999 | 248 | 228 | 5,197,807 | 20 | 35,200 | 15,161,973 | 9,267,405 | 733,212 |
| 38,000-38,999 | 232 | 214 | 5,001,733 | 18 | 44,000 | 14,566,315 | 9,305,603 | 741,597 |
| 39,000-39,999 | 184 | 169 | 3,358,021 | 15 | 35,200 | 11,093,732 | 8,926,881 | 715,922 |
| 40,000-40,999 | 1,288 | 1,199 | 31,741,621 | 89 | 207,680 | 91,996,140 | 7,268,613 | 586,662 |
| 50,000-59,999 | 535 | 495 | 15,425,512 | 40 | 82,720 | 56,905,202 | 4,750,026 | 4,750,026 |
| 60,000-69,999 | 316 | 303 | 10,893,121 | 13 | 35,200 | 29,211,335 | 2,585,710 | 2,585,710 |
| 70,000-79,999 | 174 | 163 | 7,022,159 | 11 | 26,400 | 32,088,036 | 20,414,494 | 1,874,926 |
| 80,000-89,999 | 130 | 124 | 6,318,765 | 6 | 12,320 | 17,667,833 | 13,011,055 | 1,227,112 |
| 90,000-99,999 | 88 | 87 | 4,769,006 | 1 | 1,760 | 11,009,630 | 11,009,630 | 1,058,568 |
| 100,000-109,999 | 76 | 74 | 4,020,320 | 2 | 5,280 | 8,355,505 | 8,355,493 | 815,882 |
| 110,000-119,999 | 43 | 38 | 3,870,047 | 5 | 12,320 | 12,207,067 | 7,990,508 | 789,808 |
| 120,000- | 253 | 246 | 31,775,797 | 7 | 17,600 | 94,395,503 | 4,939,850 | 492,947 |
| Totals- | 410,233 | 278,675 | 1,721,024,917 | 131,558 | 129,927,151 | 5,026,529,502 | 2,970,553,794 | 158,789,644 |

Montana Individual Income Tax Returns for 1983
(Summary of Returns Received and Processed as of January 8, 1985)

| BILL NO. <u>82-27-0</u> | | S.B. <u>307</u> | | Montana <u>Number</u> | | Returns of | | Total | | Total Number | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | | Total | |
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MONTANA SOCIETY OF CPA'S
LEGISLATIVE COMMITTEE
SUMMARY OF CONCERNS
SENATE BILL 307

I. INDIVIDUAL INCOME TAX PROVISIONS

1. Flat percentage of federal tax

Simplification could be taken as far as a fixed percentage of federal tax, instead of a percentage of federal income. The advantages are many, while the only serious drawback is the percentage will have to be fairly high, which will have a negative public relations value. The negative public relations value, however, could be handled as is illustrated on the attached tax rate tables.

SB307 eliminates the ability of married couples to file separately on their Montana income tax returns. Filing separately under current Montana law results in a significant tax savings for couples who can file separately. Basing Montana tax on federal tax would mitigate the penalty for these married couples because the federal tax rates for married couples filing jointly are lower than those for single persons.

2. Alternative minimum tax (AMT)

Aside from the public relations value of using the lower percentage of income (lower than a percentage of federal tax), there is no reason for Montana to have its own AMT structure, form, and administrative costs.

One-line on the tax return providing for a flat percentage of federal AMT would suffice, and may well be more equitable. Adopting an AMT will result in a negative public relations perception on the part of the business world. Care should be exercised.

3. AMT for non-residents

By implementing SB307, non-residents will be subject to a Montana AMT. This tax will be calculated on the basis of the ratio that their Montana adjusted gross income bears to their federal adjusted gross income.

This method will result in severe distortions. For example, a wealthy California taxpayer who is subject to a federal AMT because of large deductions for accelerated depreciation on California real estate investments could be subjected to

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a excessive Montana tax even though the Montana income consisted only of capital gains.

The Montana AMT for non-residents should be based on the ratio of Montana AMT income to total federal AMT income.

4. S corporation shareholders

Current Montana law allows a shareholder in an S corporation which has not elected to be treated as an S corporation in Montana to deduct this income on the individual return.

SB307 repeals that deduction. Implementing SB307 will cause the same income to be taxed both at the individual level and at the corporate level in Montana. A provision to handle this problem equitably should be considered.

5. Non-resident deductions

Although all other taxpayers will determine Montana tax on the basis of federal taxable income, non-residents are allowed only a few, specific itemized deductions. Taxes, interest other than for a home mortgage, and miscellaneous itemized deductions are disallowed.

This causes a hardship for non-residents. For example, a non-resident would be denied an itemized deduction for investment interest on indebtedness carried on Montana property, even though that same property may have generated the income which necessitated filing a Montana return.

We can't identify any significant reasons why non-residents shouldn't base their Montana tax on a prorated portion of their federal taxable income, just as residents and part-year residents.

6. Innocent spouse rule

We commend the administration for including an innocent spouse rule, but fear the provision may become window dressing rather than substance.

The provision provides, in part, "...unless the department determines, based on the criteria in section 6013(e) of the Internal Revenue Code, that a spouse is relieved of liability." (emphasis added)

While it is understandable that a determination will have to be made by the Department, they have had the ability to authorize corporations to file consolidated returns, but chose not to allow many to do so. Accordingly, we feel the

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provision should direct the Department to accept the rule if the criteria are met.

7. Extension of time for filing

Under federal law, a 4-month automatic extension is available for filing an individual income tax return. An additional 2 months may be granted for good cause. Under existing Montana law, an automatic extension is granted for the entire 6-month period, without requiring cause.

SB307 proposes to allow only a 2-month automatic extension, and requires cause for the additional 4 months. This provision gives paid preparers and Montana taxpayers 4 deadlines to monitor. Except for fiscal year taxpayers, individual returns are due on April 15th. With an automatic extension, the federal return is due on August 15th, but the Montana return would be due on June 15th. All calendar year returns, with the appropriate extensions, become due on October 15th, at the latest.

The proposed law requires not only an unnecessary and duplicative Montana form applying for an extension, but also requires a copy of the federal form be attached. It would be much simpler to require a taxpayer to file only a copy of the federal extension request.

The provision also provides that "...filing of an appeal from a denial of the application for another extension does not stay the time for filing the return". In other words, if a taxpayer requests the additional extension and it is denied, the late filing penalties will automatically apply. Although no protection is provided taxpayers in similar circumstances by the Internal Revenue Code, the IRS provides a 10-day grace period once a request for extension has been denied. We propose some assurance be given that a similar protection will be afforded to Montana taxpayers.

8. Federal tax refunds

It appears that section 17 of the bill should cover federal tax refunds received in years after 1987, which are refunds of federal taxes deducted on Montana returns for years prior to 1987. Refunds will be paid to taxpayers after 1987 as a result of amended returns, NOL carrybacks, and audits. The taxable portion of the refund, however, should be limited to the extent that the taxpayer has obtained a tax benefit from deducting the tax when it was paid.

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9. Tax exempt bonds

SB307 will serve to deny tax-exempt status for Montana municipal bonds which do not meet the tax-exemption requirements of the Internal Revenue Code. The Legislature should be aware of this result, since it may be a major policy decision which should be addressed independently of tax reform.

10. Penalties and interest

(a) Amount

Sections 57 through 67 of SB307 propose changes in the laws dealing with delinquent returns, late payment, and understatement of tax. The penalty and interest provisions, when viewed together, are a little frightening.

The penalty resulting from a late payment or delinquent return can reach as high as 30% of total tax, and the penalty for understating the tax would be an additional 25% of the tax.

While we do not oppose assessing penalty and interest to improve and enforce collection of taxes and compliance with the tax laws, the proposed penalty and interest sections may be somewhat excessive.

(b) Abatement

Again, the Department of Revenue has been given the discretion to waive or abate penalties where reasonable cause exists. However, it has been our experience that penalties are rarely waived, because the statute does not direct the department to waive penalties when reasonable cause exists.

The existing statutes do not provide for any possible waiver or abatement of interest, even where assessing interest may unnecessarily cause a hardship. A provision should be added to SB307 to allow for the waiver, abatement, or compromise of interest charges where the taxpayer has reasonable cause for the late payment and where the assessment of interest would be an undue hardship for the taxpayer.

(c) Time for determining

The Department of Revenue presently interprets the statute as requiring that penalties and interest be assessed on the basis of an originally filed return, even though the correct

tax might be determined at a later date and an amended return filed.

This treatment unfairly adds to the tax burden of those who over-report their income, but who have filed or paid late. These same taxpayers could have avoided penalty and interest altogether by filing a return which reflected no tax, and then paying their legitimate tax on an amended return at a later date. This interpretation would motivate a knowledgeable taxpayer to file a fraudulent return. The public interest would be better served by a provision which adjusted penalties and interest if an amended return was filed.

Internal Revenue Code section 6651(c)(2), three lines long, is such a provision as we would like to see added to address fairness and equity in the penalty sections.

II. CORPORATE INCOME TAX PROVISIONS

1. Alternative Minimum Tax

As tax professionals, we have serious reservations about the corporate alternative minimum tax, for the following reasons:

- taxpayers lack awareness or understanding of the alternative minimum tax,
- the AMT is very often an insidious tax bite,
- it may cause business to relocate out of state, and
- there is a lack of good data with respect to its impact.

The attached chart illustrates the AMT calculations for individuals and corporations. These calculations require preparation of a separate depreciation schedule and, in many cases, require other accounting adjustments which are not described except in the Internal Revenue Code.

We believe that it is extremely important for the Department of Revenue to determine specifically which industries and Montana businesses will be impacted. We suspect it may be banks, utilities, mining, oil and gas and other large corporate taxpayers.

2. Net operating loss (NOL) carrybacks and carryovers

To use an old cliché, this provision is tantamount to swatting flies with a baseball bat.

Many small businesses and family farms are organized as

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corporations. Many of these businesses incur net operating losses frequently. It is quite common in the cattle business to operate at a loss for 5 to 10 years, and then report a substantial profit because of a herd dispersal (not always voluntary) or because of a brief improvement in cattle prices.

The incorporated farm or small business deserves NOL carryovers and carrybacks to offset high income in the year in which the farm or business is sold. Even though the taxable income may be high, by the time the creditors are paid, there is not always enough money left for retirement.

Liberal NOL carryback and carryover provisions are needed to eliminate hardships caused these businesses. This provision is more important to small business and start-up companies than to large corporate taxpayers.

If a few banks are causing budget problems for local governments, the Legislature should review the distribution of the corporate license tax or limit the NOL carryback provision for banks, allowing only a carryforward rather than a carryback.

While we believe this is most likely the reason for the proposal, it seems unfair to single out banks. They are major tax revenue contributors to Montana during the "good times". If NOL carrybacks create revenue problems for local government, then the alternative is to discontinue carrybacks and lengthen the carryforward period, for example, to 10 years.

III. UNITARY TAX

Most Montana CPA's do not deal with the unitary tax, and the Montana Society of CPA's has not performed the in-depth analysis of the unitary tax provisions of SB307 as was done for the individual and corporate income tax provisions. However, several of our members have pointed out that compliance with the water's edge election would be very burdensome. The proposed election form seems to reflect the accumulated frustrations of the Department of Revenue in dealing with multi-national companies, rather than a reasonable approach to the problem.

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FILE NO. S. R. 307

MONTANA EFFECTIVE TAX RATES
(FOR EXAMPLE ONLY)
MARRIED FILING JOINTLY - 1987

| Federal tax rate | | Montana % of federal tax rate | | Montana effective tax rate |
|---------------------|-------|-------------------------------------|---|----------------------------------|
| 11% | times | 25% | = | 2.75% |
| 15% | times | 25% | = | 3.75% |
| 28% | times | 25% | = | 7.00% |
| 35% | times | 25% | = | 8.75% |
| 38.5% | times | 25% | = | 9.625% |

MARRIED FILING JOINTLY - 1988

| | | | | |
|-----|-------|-----|---|-------|
| 15% | times | 25% | = | 3.75% |
| 28% | times | 25% | = | 7.00% |
| 33% | times | 25% | = | 8.25% |
| 28% | times | 25% | = | 7.00% |

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BILL NO. S.B. 307

ALTERNATIVE MINIMUM TAX COMPUTATION

| | Individual | Corporate |
|--|---|----------------|
| Start with | Adj. gross income | Taxable income |
| Deduct: | Casualty losses, medical expenses in excess of 10% of AGI, estate tax ded'n, & qualified interest | |
| Add back "tax preference items" | | |
| - ACRS depreciation in excess of 150% declining balance method for personal property | yes | yes |
| - ACRS depreciation in excess of st. line for real property | yes | yes |
| - Research and experimentation costs | yes | |
| - Completed contract accounting income over % completion method | yes | yes |
| - 100% of the gain on an installment sale (subject to certain exceptions) | yes | yes |
| - 5-year amortization of pollution control facilities | yes | yes |
| - Untaxed appreciation on charitable contributions of appreciated property | yes | yes |
| - Mining and exploration and development costs (excess of expense over 10-year amortization) | yes | yes |
| - Intangible drilling costs in excess of 65% of net income from oil, gas & geothermal properties | yes | yes |
| - Incentive stock options (excess of fair market value over purchase price) | yes | |
| - Percentage depletion | yes | yes |
| - Circulation expenditures (excess of expense over 3-year amortization) | yes | |
| - Passive losses | yes | |
| - Tax-exempt interest on nonessential function bonds (issued after 8/7/86) | yes | yes |
| - Excess of 1/2 of financial statement income over taxable income | | yes |
| - Reserves for bad debt losses of financial institutions | | yes |
| Deduct exemption: | \$40,000 joint \$30,000 single \$20,000 married, filing sep. | \$40,000 |
| Phased out for alternative minimum taxable income in excess of | \$150,000 | \$150,000 |
| Equals | alternative minimum taxable income | |
| Taxed at | 21% | 20% |

(Alternative minimum tax is paid if greater than regular tax)

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The Big Sky Country

MONTANA HOUSE OF REPRESENTATIVES

REPRESENTATIVE JOHN E. PHILLIPS

HOUSE DISTRICT 33

HOME ADDRESS:

1200 32ND STREET SOUTH—NO. 61
GREAT FALLS, MONTANA 59405

COMMITTEES:

STATE ADMINISTRATION
FISH, WILDLIFE & PARKS
EDUCATION & CULTURAL
RESOURCES

February 23, 1987

TESTIMONY BEFORE THE SENATE
TAXATION COMMITTEE ON SENATE BILL 307

Mr. Chairman and members of the Senate Taxation Committee, for the record I'm Representative John Phillips, District 33, Great Falls.

I'm here before you to testify for a group of people who couldn't be with you today due to commitments around the globe and whom I'm sure that over 99% of them are unaware that what is happening with this piece of legislation, may affect them.

Buried within this massive bill is a repealer that deletes one small section of the codes which says in effect, that active duty military pay is exempt from state income tax.

Normally we look at taxes as something we pay for which the taxing authority provides us a service. I would simply ask each of you what service the state of Montana is providing to that young sailor from Missoula on a carrier in the Mediterranean, the soldier from Billings peering across no man's land in Korea, the airman from the Bitterroot looking at a radar scope on some lonely mountain top in Alaska or even the marine from Miles City living it up down in Oceanside, California.

You may say that's a pretty decent argument but what about the troops at Malmstrom, they live in the state and we provide service for them. Maybe, but how much? For the individual living at Malmstrom, the Air Force provides police and fire protection, maintains and lights the streets and the Federal Government kicks in to the Great Falls school system to educate their kids (over \$850,000 last year). They pay the same gas taxes at the pump for the roads they drive on, the same liquor and beer taxes, and if a resident, the same auto license fees as every other Montanan.

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If they live and own a home downtown, they pay the same property tax as everyone else. If renting, taxes are no doubt considered in the monthly rent.

Actually, about one in ten of the G I's stationed at Malmstrom claim Montana residence (approximately 400). Many of those are native Montanans. I would expect that if this measure passes several of the ones who are not native Montanans and maybe some who are, would be looking around to claim residency in a state where the tax was exempt or there was no state income tax. This same reaction would probably occur among some native Montanans stationed in other states which exempt or have no state income tax when they find Montana has changed their tax laws.

While this proposal may pick up a bit of revenue, it may also have some detrimental effects. It would provide more work for the Department of Revenue in auditing returns, and checking out folks who disappeared from the system by changing residence. Some innocent people who return to Montana after military service may face a battle with DOR proving they didn't have a tax liability. Further, I think it would discourage people from becoming residents and eventually retiring here. Which in my view is like creating another job with the cleanest money you could bring into the state economy.

Montanans have always been proud of the patriotism their young people have shown throughout the years and have shown their gratitude by giving the military and veterans special consideration. In fact, the concept is framed in Montana's Constitution.

We are all aware of the money crunch the state is in but do we really want to send this kind of message to the folks who are defending our freedom throughout the world. It has been stated that the changes proposed in this bill is to make the tax system more fair for everyone but I ask you is it really fair to tax someone who is not receiving any services whatsoever from the state.

I have a proposed amendment to Senate Bill 307 which would leave the exemption in the codes. I urge you to support it.

Again, most Montanans in uniform today are unaware of this proposal, but I think if they knew what was happening they would appreciate the fact that someone is here speaking for them.

Mr. Chairman, I thank the committee for allowing me to present this testimony.

John E. Phillips
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Representative

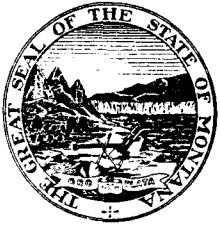
JEP/be

SENATE TAXATION

EXHIBIT NO. 2

DATE 2-24-87

BILL NO. S.R. 200



The Big Sky Country

MONTANA HOUSE OF REPRESENTATIVES

REPRESENTATIVE JOHN E. PHILLIPS

HOUSE DISTRICT 33

HOME ADDRESS:

1200 32 ND STREET SOUTH—NO. 61
GREAT FALLS, MONTANA 59405

COMMITTEES:

STATE ADMINISTRATION
FISH, WILDLIFE & PARKS
HUMAN SERVICES & AGING

PROPOSED AMENDMENTS TO SB 307

Title line 22: strike 15-30-117, add 15-30-115 and 15-30-117

Page 145 line 17: strike 15-30-117, add 15-30-115 and
15-30-117

Submitted by,

John Phillips
Representative

JP/be

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FISH, WILDLIFE & PARKS
EDUCATION & CULTURAL
RESOURCES

February 23, 1987

TESTIMONY BEFORE THE SENATE
TAXATION COMMITTEE ON SENATE BILL 307

Mr. Chairman and members of the Senate Taxation Committee, for the record I'm Representative John Phillips, District 33, Great Falls.

I'm here before you to testify for a group of people who couldn't be with you today due to commitments around the globe and whom I'm sure that over 99% of them are unaware that what is happening with this piece of legislation, may affect them.

Buried within this massive bill is a repealer that deletes one small section of the codes which says in effect, that active duty military pay is exempt from state income tax.

Normally we look at taxes as something we pay for which the taxing authority provides us a service. I would simply ask each of you what service the state of Montana is providing to that young sailor from Missoula on a carrier in the Mediterranean, the soldier from Billings peering across no man's land in Korea, the airman from the Bitterroot looking at a radar scope on some lonely mountain top in Alaska or even the marine from Miles City living it up down in Oceanside, California.

You may say that's a pretty decent argument but what about the troops at Malmstrom, they live in the state and we provide service for them. Maybe, but how much? For the individual living at Malmstrom, the Air Force provides police and fire protection, maintains and lights the streets and the Federal Government kicks in to the Great Falls school system to educate their kids (over \$850,000 last year). They pay the same gas taxes at the pump for the roads they drive on, the same liquor and beer taxes, and if a resident, the same auto license fees as every other Montanan.

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If they live and own a home downtown, they pay the same property tax as everyone else. If renting, taxes are no doubt considered in the monthly rent.

Actually, about one in ten of the G I's stationed at Malmstrom claim Montana residence (approximately 400). Many of those are native Montanans. I would expect that if this measure passes several of the ones who are not native Montanans and maybe some who are, would be looking around to claim residency in a state where the tax was exempt or there was no state income tax. This same reaction would probably occur among some native Montanans stationed in other states which exempt or have no state income tax when they find Montana has changed their tax laws.

While this proposal may pick up a bit of revenue, it may also have some detrimental effects. It would provide more work for the Department of Revenue in auditing returns, and checking out folks who disappeared from the system by changing residence. Some innocent people who return to Montana after military service may face a battle with DOR proving they didn't have a tax liability. Further, I think it would discourage people from becoming residents and eventually retiring here. Which in my view is like creating another job with the cleanest money you could bring into the state economy.

Montanans have always been proud of the patriotism their young people have shown throughout the years and have shown their gratitude by giving the military and veterans special consideration. In fact, the concept is framed in Montana's Constitution.

We are all aware of the money crunch the state is in but do we really want to send this kind of message to the folks who are defending our freedom throughout the world. It has been stated that the changes proposed in this bill is to make the tax system more fair for everyone but I ask you is it really fair to tax someone who is not receiving any services whatsoever from the state.

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