HOUSE BILL 309

IN THE HOUSE

January 22, 1979

Introduced and referred to Committee on Taxation.

House BILL NO. 309

INTRODUCED BY [illegible]

A BILL FOR AN ACT ENTITLED: "AN ACT TO PROVIDE FOR THE ADJUSTMENT OF CAPITAL GAINS, INTEREST INCOME AND EXPENDITURE, AND DEPRECIATION FOR INFLATION IN CALCULATING INDIVIDUAL INCOME TAX LIABILITY; TO PROVIDE FOR THE ADJUSTMENT FOR INFLATION OF THE DEPRECIATION ALLOWANCE TAKEN IN DETERMINING CORPORATION LICENSE TAX; AMENDING SECTIONS 15-30-101, 15-30-111, AND 15-31-114, MCA; AND PROVIDING AN APPLICABILITY DATE."

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF MONTANA:

Section 1. Section 15-30-101, MCA, is amended to read:

"15-30-101. Definitions. For the purpose of this chapter, unless otherwise required by the context, the following definitions apply:

(1) "CPI" means the consumer price index, United States city average, for all items using the 1967 base of 100 as published for June of each year by the bureau of labor statistics of the United States department of labor or its successor.

(2) "CF" means a correction factor used to discount interest rates for inflation the value of which is determined by the following formula: CF=1-(Ir/In), in which

In represents interest rates and Ir represents the inflation rate.

~~(1)~~(3) "Department" means the department of revenue.

~~(2)~~(4) "Dividend" means any distribution made by a corporation out of its earnings or profits to its shareholders or members, whether in cash or in other property or in stock of the corporation, other than stock dividends as herein defined. "Stock dividends" means new stock issued, for surplus or profits capitalized, to shareholders in proportion to their previous holdings.

~~(3)~~(5) "Fiduciary" means a guardian, trustee, executor, administrator, receiver, conservator, or any person, whether individual or corporate, acting in any fiduciary capacity for any person, trust, or estate.

~~(4)~~(6) "Foreign country" or "foreign government" means any jurisdiction other than the one embraced within the United States, its territories and possessions.

(7) "Ir" means an inflation factor determined by subtracting the CPI for the previous year from the CPI for the taxable year in question and dividing the difference by the CPI for the previous year.

~~(5)~~(8) "Information agents" include all individuals, corporations, associations, and partnerships, in whatever capacity acting, including lessees or mortgagors of real or personal property, fiduciaries, employers, and all officers

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and employees of the state or of any municipal corporation or political subdivision of the state, having the control, receipt, custody, disposal, or payment of interest, rent, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable annual or periodical gains, profits, and income with respect to which any person or fiduciary is taxable under this chapter.

(9) "In" means the annual rate of interest received on an investment or paid or accrued in a taxable year on indebtedness.

(10) "IRC" means the Internal Revenue Code of 1954, as amended.

~~(6)~~(11) "Net income" means the adjusted gross income of a taxpayer less the deductions allowed by this chapter.

~~(7)~~(12) "Paid", for the purposes of the deductions and credits under this chapter, means paid or accrued or paid or incurred, and the terms "paid or incurred" and "paid or accrued" shall be construed according to the method of accounting upon the basis of which the taxable income is computed under this chapter.

(13) "PIR" means a price index ratio determined for each year by dividing the CPI, as defined in subsection (1), for a taxable year by the CPI for the previous year.

~~(8)~~(14) "Received", for the purpose of computation of

taxable income under this chapter, means received or accrued and the term "received or accrued" shall be construed according to the method of accounting upon the basis of which the taxable income is computed under this chapter.

~~(9)~~(15) "Resident" applies only to natural persons and includes, for the purpose of determining liability to the tax imposed by this chapter with reference to the income of any taxable year, any person domiciled in the state of Montana and any other person who maintains a permanent place of abode within the state even though temporarily absent from the state and has not established a residence elsewhere.

~~(10)~~(16) "Taxable income" means the adjusted gross income of a taxpayer less the deductions and exemptions provided for in this chapter.

~~(11)~~(17) "Taxable year" means the taxpayer's taxable year for federal income tax purposes.

~~(12)~~(18) "Taxpayer" includes any person or fiduciary, resident or nonresident, subject to a tax imposed by this chapter and does not include corporations."

Section 2. Section 15-30-111, MCA, is amended to read:

"15-30-111. Adjusted gross income. (1) ~~Adjusted~~ Except as provided in [sections 3 through 5], adjusted gross income shall be the taxpayer's federal income tax adjusted gross income as defined in section 62 of the Internal Revenue Code of 1954 or as that section may be labeled or amended and in addition shall include the following:

(a) interest received on obligations of another state or territory or county, municipality, district, or other political subdivision thereof;

(b) refunds received of federal income tax, to the extent the deduction of such tax resulted in a reduction of Montana income tax liability.

(2) Adjusted gross income does not include the following which are exempt from taxation under this chapter:

(a) interest income from obligations of the United States government, the state of Montana, county, municipality, district, or other political subdivision thereof;

(b) all benefits received under the Federal Employees' Retirement Act not in excess of $3,600;

(c) all benefits paid under the teachers' retirement law which are specified as exempt from taxation by 19-4-706;

(d) all benefits paid under The Public Employees' Retirement System Act which are specified as exempt from taxation by 19-3-105;

(e) all benefits paid under the highway patrol retirement law which are specified as exempt from taxation by 19-6-705;

(f) all Montana income tax refunds or credits thereof;

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(g) all benefits paid under 19-11-602, 19-11-604, and 19-11-605 to retired and disabled firefighters, their surviving spouses and orphans;

(h) all benefits paid by first- or second-class cities for the policemen's retirement system provided for by Title 19, chapter 9.

(3) In the case of a shareholder of a corporation with respect to which the election provided for under subchapter S. of the Internal Revenue Code of 1954, as amended, is in effect but with respect to which the election provided for under 15-31-202, as amended, is not in effect, adjusted gross income does not include any part of the corporation's undistributed taxable income, net operating loss, capital gains or other gains, profits, or losses required to be included in the shareholder's federal income tax adjusted gross income by reason of the said election under subchapter S. However, the shareholder's adjusted gross income shall include actual distributions from the corporation to the extent they would be treated as taxable dividends if the subchapter S. election were not in effect."

NEW SECTION. Section 3. Method of determining amount of net capital gain. (1) The provisions of the IRC relating to inclusion of net capital gains in gross income apply except that the value of net capital gain on assets held over 1 year to be included is determined as follows:

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(a) The purchase price of the asset is multiplied by the PIR for the year in which the asset was acquired by the taxpayer to determine the adjusted cost of the asset.

(b) The adjusted cost of the asset is subtracted from the price received from the sale of the asset during the taxable year in which the deduction will be taken, to determine the net capital gain.

(2) Fifty percent of the net capital gain so determined may be claimed as a deduction to gross income.

(3) The department shall include with each income tax return form a table showing the PIR for each of the past 20 years.

(4) The department shall furnish the PIR for earlier years upon request.

NEW SECTION. Section 4. Method of determining taxable income and deductions for interest exception. (1) All the provisions of the IRC relating to the inclusion of interest income in gross income and the deduction of interest paid or accrued within a taxable year on indebtedness apply except that the amount of interest included in adjusted gross income is determined as follows:

(a) interest income from each source is:

(i) multiplied by the CF shown in tables furnished by the department for the rate of interest at which the income was generated; and

(ii) included in gross income; and

(b) interest expense paid or accrued on each debt, except debt incurred for the purchase of the taxpayer's primary residence, is:

(i) multiplied by the CF shown on tables provided by the department for the rate of interest at which the interest expense was incurred or accrued; and

(ii) allowed as a deduction from gross income.

(2) When interest expense incurred on a debt was calculated at more than one rate of interest, the CF for the highest rate of interest charged on the debt is multiplied by the interest expense for the entire debt to determine the deduction allowed.

(3) Each year the department shall calculate the CF for that year for each 1/4 of 1% of interest from 0% to 50% and include a table of the values so calculated with each income tax return form.

NEW SECTION. Section 5. Method of determining amount of deduction allowed for depreciation. (1) The provisions of the IRC relating to deduction of depreciation of property used in a trade or business or held for the production of income apply except that the amount of depreciation allowed as a deduction under the IRC is:

(a) multiplied by the PIR for the year in which the taxpayer purchased the property; and

(b) allowed as a deduction to gross income.

Section 6. Section 15-31-114, MCA, is amended to read:

"15-31-114. Deductions allowed in computing income. In computing the net income, the following deductions shall be allowed from the gross income received by such corporation within the year from all sources:

(1) All the ordinary and necessary expenses paid or incurred during the taxable year in the maintenance and operation of its business and properties, including reasonable allowance for salaries for personal services actually rendered, subject to the limitation hereinafter contained, rentals or other payments required to be made as a condition to the continued use or possession of property to which the corporation has not taken or is not taking title or in which it has no equity. No deduction shall be allowed for salaries paid upon which the recipient thereof has not paid Montana state income tax; provided, however, that where domestic corporations are taxed on income derived from without the state, salaries of officers paid in connection with securing such income shall be deductible.

(2) (a) All losses actually sustained and charged off within the year and not compensated by insurance or otherwise, including a reasonable allowance for the wear and tear and obsolescence of property used in the trade or business, such allowance to be determined according to the

provisions of ~~section--167-of-the-Internal-Revenue-Code-in effect-with-respect-to-the-taxable--year~~ [section 7]. All elections for depreciation shall be the same as the elections made for federal income tax purposes. No deduction shall be allowed for any amount paid out for any buildings, permanent improvements, or betterments made to increase the value of any property or estate, and no deduction shall be made for any amount of expense of restoring property or making good the exhaustion thereof for which an allowance is or has been made.

(b) (i) There shall be allowed as a deduction for the taxable period a net operating loss deduction determined according to the provisions of this subsection. The net operating loss deduction is the aggregate of net operating loss carryovers to such taxable period plus the net operating loss carrybacks to such taxable period. The term "net operating loss" means the excess of the deductions allowed by this section, 15-31-114, over the gross income, with the modifications specified in (ii) of this subsection. If for any taxable period beginning after December 31, 1970, a net operating loss is sustained, such loss shall be a net operating loss carryback to each of the three taxable periods preceding the taxable period of such loss and shall be a net operating loss carryover to each of the five taxable periods following the taxable period of such loss. A

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net operating loss for any taxable period ending after December 31, 1975, in addition to being a net operating loss carryback to each of the three preceding taxable periods, shall be a net operating loss carryover to each of the seven taxable periods following the taxable period of such loss. The portion of such loss which shall be carried to each of the other taxable years shall be the excess, if any, of the amount of such loss over the sum of the net income for each of the prior taxable periods to which such loss was carried. For purposes of the preceding sentence, the net income for such prior taxable period shall be computed with the modifications specified in (ii)(B) of this subsection and by determining the amount of the net operating loss deduction without regard to the net operating loss for the loss period or any taxable period thereafter, and the net income so computed shall not be considered to be less than zero.

(ii) The modifications referred to in (i) of this subsection shall be as follows:

(A) No net operating loss deduction shall be allowed.

(B) The deduction for depletion shall not exceed the amount which would be allowable if computed under the cost method.

(iii) A net operating loss deduction shall be allowed only with regard to losses attributable to the business carried on within the state of Montana.

(iv) In the case of a merger of corporations, the surviving corporation shall not be allowed a net operating loss deduction for net operating losses sustained by the merged corporations prior to the date of merger. In the case of a consolidation of corporations, the new corporate entity shall not be allowed a deduction for net operating losses sustained by the consolidated corporations prior to the date of consolidation.

(v) Notwithstanding the provisions of 15-31-531, interest shall not be paid with respect to a refund of tax resulting from a net operating loss carryback or carryover.

(vi) The net operating loss deduction shall not be allowed with respect to taxable periods which ended on or before December 31, 1970, but shall be allowed only with respect to taxable periods beginning on or after January 1, 1971.

(3) In the case of mines, other natural deposits, oil and gas wells, and timber, a reasonable allowance for depletion and for depreciation of improvements; such reasonable allowance to be determined according to the provisions of the Internal Revenue Code in effect for the taxable year. All elections made under the Internal Revenue Code with respect to capitalizing or expensing exploration and development costs and intangible drilling expenses for corporation license tax purposes shall be the same as the

elections made for federal income tax purposes.

(4) The amount of interest paid within the year on its indebtedness incurred in the operation of the business from which its income is derived; but no interest shall be allowed as a deduction if paid on an indebtedness created for the purchase, maintenance, or improvement of property or for the conduct of business unless the income from such property or business would be taxable under this part.

(5) Interest income from obligations of the state or any political subdivision or municipality of the state.

(6) (a) Taxes paid within the year except the following:

(i) Taxes imposed by this part.

(ii) Taxes assessed against local benefits of a kind tending to increase the value of the property assessed.

(iii) Taxes on or according to or measured by net income or profits imposed by authority of the government of the United States.

(iv) Taxes imposed by any other state or country upon or measured by net income or profits.

(b) Taxes deductible under this part shall be construed to include taxes imposed by any county, school district, or municipality of this state.

(7) That portion of an energy-related investment allowed as a deduction under 15-32-103."

NEW SECTION. Section 7. Method of determining allowance for depreciation. (1) The allowance for depreciation is determined according to the provisions of section 167 of the IRC in effect for the taxable year except that the amount of depreciation allowed under these provisions is multiplied by the PIR for the year in which the property was purchased.

(2) The department shall provide a table showing the PIR for each of the previous 20 years to each corporation required to file a return.

(3) The department shall furnish the PIR for earlier years upon request.

Section 8. Date of applicability. This act applies to taxable years beginning after December 31, 1979.

-End-

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STATE OF MONTANA

Request No. 85-79

FISCAL NOTE

Form BD-15

In compliance with a written request received January 25, 1979, there is hereby submitted a Fiscal Note for House Bill 309 pursuant to Chapter 53, Laws of Montana, 1965 - Thirty-Ninth Legislative Assembly. Background information used in developing this Fiscal Note is available from the Office of Budget and Program Planning, to members of the Legislature upon request.

DESCRIPTION

This bill provides for the adjustment of capital gains, interest income and expenditure, and depreciation for inflation and calculating individual income tax liability; provides for the adjustment for inflation of the depreciation allowance taken in determining corporation license tax; and provides an applicability date.

FISCAL IMPACT

The Department of Revenue does not have data pertaining to capital gains, interest income, or depreciation readily available. Therefore, it is not possible to accurately determine the extent of the loss in revenue which would accompany the adoption of the proposed law. However, it is believed that this bill would have a significant effect upon individual and corporation tax receipts.

TECHNICAL NOTE

(a) The apparent intent of this bill is to exempt from taxation any increase in certain property income which may be attributable to inflation, and to inflate the depreciation deduction so as to compensate for general increases in the price level.

The definition for "PIR" in subsection (13) of Section 1 (page 3, lines 22-24) should be amended to read: "PIR" means a price index ratio, determined for each year prior to the year for which the return is filed, by dividing the CPI of the year for which the return is filed by the CPI for the prior year, where CPI is as defined in subsection (1)."

(b) The Consumer Price Index defined in subsection (1) of Section 1 is not well-defined. The Bureau of Labor Statistics currently published two such indices (U.S. City avg., all items, 1967:100), one for all urban consumers, and the other for urban wage earners and clerical workers.

Richard L. Dramy for
BUDGET DIRECTOR
Office of Budget and Program Planning
Date: 1/29/79