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Revenue and Transportation Interim Committee

58th Montana Legislature

SENATE MEMBERS
GREGORY BARKUS
JERRY BLACK
VICKI COCCHIARELLA
JON ELLINGSON
ROBERT STORY
KEN TOOLE

HOUSE MEMBERS
JOE BALYEAT
EILEEN CARNEY
RONALD DEVLIN
CHRISTINE KAUFMANN
KARL WAITSCHIES
BILL WILSON

COMMITTEE STAFF
LEANNE KURTZ, Research Analyst
JEFF MARTIN, Research Analyst
LEE HEIMAN, Staff Attorney

MINUTES

Please Note: These are summary minutes. Testimony and discussion are paraphrased and condensed. Committee tapes are on file in the offices of the Legislative Services Division. **Exhibits for this meeting are available upon request. Legislative Council policy requires a charge of 15 cents a page for copies of the document.**

Room 137, State Capitol
September 9, 2004

COMMITTEE MEMBERS PRESENT

Sen. Robert Story, Chair
Rep. Eileen Carney, Vice Chair
Sen. Greg Barkus
Sen. Jerry Black
Sen. Vicki Cocchiarella
Sen. Jon Ellingson
Sen. Ken Toole
Rep. Joe Balyeat
Rep. Ronald R. Devlin
Rep. Christine Kaufmann
Rep. Karl Waitschies
Rep. Bill Wilson

STAFF PRESENT

Jeff Martin, Research Analyst
Leanne Kurtz, Research Analyst
Diane McDuffie, Secretary

VISITORS

Visitors' list (Attachment #1)

COMMITTEE ACTION

- Voted to request on behalf of the Department of Revenue the drafting of a bill to revise the valuation of agricultural land and the funding mechanism.
- Voted to request the drafting of a committee bill for revenue estimates.

(Tape 1; Side A)

CALL TO ORDER AND ROLL CALL

The meeting was called to order by **Sen. Story** at 8:00 a.m. on Friday, September 9, 2004. The secretary noted the roll (Attachment 2).

Rep. Devlin moved to approve the July 9, 2004, minutes with the correction that Rep. Bill Wilson was present. The motion carried unanimously.

Montana Corporation License Taxes

- **Corporation tax analysis**

Terry Johnson, Principal Fiscal Analyst, Legislative Fiscal Division, presented a report on the Montana Corporation License Tax (Exhibit 1) The report consists of the following sections: 1) introduction; 2) background information; 3) historical collections; 4) tax return analysis; 5) economic relationships; and 6) conclusion.

Mr. Johnson said that LFD staff analyzed historic accounting data and specific return data to determine if changes have occurred within the corporation tax base. This report provides an analysis and conclusions drawn from both SBAS and SABHRS data and data provided by Department of Revenue (DOR) over the period of 1981 through 2004. The return data provided by the DOR was invaluable in this analysis, but was also very limited in its time span and captured data elements.

Mr. Johnson said that the corporate confidentiality statute prohibits LFD from using any corporation names or information in the report. There are known occasions where large corporations have had a significant impact on the collections of the tax but cannot be referred to in the report. These occurrences must be combined with other effects, which tends to distort the exact nature of both negative and positive impacts.

In section two, two areas of analysis provided definite conclusions about the changes of the corporate tax base, estimated taxes and adjusted taxes. The analysis suggested that estimated payments have grown at a rate of 1.7 percent annually. While estimated payments were slowly growing, inflation was growing at an average rate of 2.6 percent. Both areas of analysis point to the fact that the corporate base has lost some of its strength.

***(Tape 1*; Side B)**

- **Interstate comparisons of corporation tax rates, reporting requirements, apportionment factors, minimum tax, net operating loss periods**

Jeff Martin, Research Analyst, Legislative Services Division, provided a report on State-by-State Corporation Income Tax Comparisons. (Exhibit 2) This report discusses state-by-state comparisons of corporation income tax bases and rates, minimum corporation taxes, combined unitary reporting requirements, and apportionment factors. Table 1 shows state corporate income taxes: rates, minimum tax, combined reporting requirements, and apportionment. Table 2 shows corporation net operating loss carryback and carryforward provisions.

Mr. Martin said that twenty-eight states and the District of Columbia impose a flat rate on net income and the remainder impose graduated rates. Some states impose separate tax rates on financial institutions and other types of businesses. Several states require a minimum tax payment ranging from $10 in Oregon to $800 in California; Montana's minimum tax is $50. States that take into account the income and apportionment of parent companies and subsidiaries are known as combined unitary reporting states. Montana is one of 13 states that require combined unitary reporting. Mr. Martin also said that the income of a corporation that operates in more than one state is apportioned for tax purposes to each state in which the corporation operates. The formula used to calculate the ratio typically includes payroll, property, and sales. A net operating loss occurs when a business's deductions exceed its operating income for the tax year. The rationale for allowing net operating losses is to tax businesses on the basis of the business cycle rather than individual tax years. Nineteen states, including Montana, allow carrybacks (2-5 years) and carryforwards (5-20 years). The other states only allow carryforward of net operating losses.

(Tape 2; Side A)

Trends in the value of personal property by industry type

Randy Wilke, Department of Revenue, provided two handouts: 1) Market Value of Select Class 8 Properties, Tax Year 1990 to 2003, and 2) Class 8 Property by Business Types (Exhibits 3 and 4)

Mr. Wilke said that Exhibit 4 is a summary of individual personal property tax returns filed by taxpayers or gathered from a field audit during 2001 through 2004. Each return is identified with a specific business code. Each type of property is identified and placed in a specific classification code. The major types of property associated with respective industries are identified by the respective class codes.

Preliminary calculation of class eight trigger

T**erry Johnson, Legislative Fiscal Division**, provided a document on Personal Property Tax Trigger Calculations. (Exhibit 5)

Mr. Johnson said that class 8 property is currently taxed at 3 percent of its market value. Beginning with tax year 2004, the tax rate is reduced by 1 percent each year if the percentage growth in inflation-adjusted Montana wage and salary income is at least 2.85 percent. Using preliminary data for 2003 to determine the potential impact on the tax rate for 2006, the tax rate for tax year 2006 will probably remain at 3 percent.

Taxation of Agricultural Land

- **Department of Revenue proposal to revise valuation of agricultural land**

Randy Wilke, Department of Revenue, provided an Agricultural & Forest Land Reappraisal Proposal. (Exhibit 6) Mr. Wilke discussed the history of agricultural land assessment in Montana. The three parts to agricultural land valuation are: 1) land use classification; 2) grading land productivity; and 3) valuation system designed to be applied to the classification and grading system. The existing system of appraising agricultural land is labor intensive and cannot be maintained or reviewed with existing staff, and is not in compliance with state law. The DOR is proposing a new agricultural and forest land classification system in 2009. The proposed system would update Montana's current classification and productive grading system using data from other agencies and the federal government.

Mr. Wilke said the proposed system would bring the state into compliance with state statutes, which mandate current classification and grading of agricultural land. With approval from the Legislature, the project would begin July 1, 2005. The new tax system would be implemented January 1, 2009. Estimated project cost for agricultural land is $1,024,000 and forest land is $66,000. Funding options being considered are: 1) general fund appropriation; 2) statewide mill levy; and 3) flat tax on class 3 and class 10.

Randy Piearson, Department of Revenue, showed the committee several maps being used for assessments of agricultural and forest lands. The maps are hand drawn and very labor intensive. Mr. Piearson also discussed the pilot project completed in Cascade County using the Natural Resource Conservation Service soil survey.

Senator Barkus asked if the results of the project were communicated to the land owners in the area. Mr. Piearson said the project has not been discussed with the community.

Senator Story asked what the department is asking of the committee. Mr. Wilke requested concurrence from the committee to continue with legislation.

(Tape 2; Side B)

Dr. Myles Watts, MSU, said that the grade and classification system is badly outdated. Dr. Watts recommended the productivity be completed first and then the valuation formulation be reviewed to make sure it is consistent with productivity.

Senator Cocchiarella asked about the reliability of the soil survey. Dr. Watts said the soil survey is the best available.

Chuck Gordon, Natural Resource Conservation Service, said that soil survey mapping for Montana is 84 percent complete. Private and state lands will be done by late 2007. Remaining to be mapped will be large blocks of federal lands.

Senator Black asked if the land owners have had an opportunity to review the classification. Mr. Gordon said the information is for the landowners to use in their conservation planning and there have not been any disagreements.

MOTION: Rep. Carney moved to request the drafting of a bill (by request of the Department of Revenue) to revise the valuation method of agricultural land and the funding mechanism.

Senator Story asked Mr. Wilke if the department has decided on a funding mechanism or would someone else determine that. Mr. Wilke said probably 2 cents an acre on agricultural land since it has been used before for forest land.

Senator Cocchiarella reminded the committee that a vote for the drafting of this legislation is not an endorsement of the concept.

VOTE: Motion passed. Rep. Balyeat voted no.

<u>Liquor Store Owners Association legislative proposals</u>

Chris Byrd, President of the Liquor Store Owners Association, discussed three items for proposed legislation and requested authorization for the liquor division to work with them to draft a bill to:

- change the reimbursement for case-lot discounts that are given to bars;
- allow the sale of beer in liquor stores; and
- allow off-premise storage

(Tape 3; Side A)

- **Ownership criteria for classification as agricultural land**

Dolores Cooney, Department of Revenue, provided a handout on Ownership Definition. (Exhibit 7) Ms. Cooney said the DOR property assessment division is conducting a statewide review of agricultural and forest lands to make sure lands are properly classified and properly valued. A question has been raised in regard to qualification of agricultural land and the department's interpretation of land ownership. The department has not changed its interpretation of the phrase "under one ownership" since the current agricultural land legislation was implemented in 1986.

Ms. Cooney explained that DOR has for the first time been able to identify all tract land, forest land, and agricultural land through GIS capabilities. If any questionable property is found, the owner is notified that the property is going through a review process and is asked to contact DOR to help determine the correct classification of the property. Ms. Cooney said that some of the questions about the review are about the qualifications for agricultural land.

Senator Black asked the if land is not contiguous but under the same ownership, would that be considered as one.

Ms. Cooney said some conditions to qualify for agricultural land are: single ownership of land, or proof that variations in a name is the same owner, over 160 acres contiguous, no covenants against agricultural use, and if less than 160 acres, specific criteria must be met through an application process.

Senator Black said that farmers often separate acreage out under a corporation or a different name. They do this to secure financing and for other reasons. He suggested that in those circumstances, they be classified as a single owner. This is similar to what Farm Service Agency (FSA) does to qualify for annual farm payment and federal subsidies. Senator Black would like to see a slight adjustment in the administrative rules to correct the situation. Senator Black believes that the intent of the law was to eliminate the tax break for hobby farmers, not to catch farmers who are legitimately farming smaller pieces of non-contiguous land, or non-contiguous land under different names.

Ms. Cooney reiterated that the administrative rules on ownership have used the same criteria since 1986. She said that to change the definition without legislative guidance would be heading in the wrong direction. It would contradict all of the legal advice that DOR has received, and court decisions. Changing the criteria would create a problem because DOR does not have the ability to tell if non-contiguous land, under different names is actually single ownership. Ms. Cooney believes that any change would have to be at the direction of the Legislature.

Senator Black requested a copy of the written legal opinion. He argued that although this has been an administrative rule for many years, it has not been implemented until now, with this recent reevaluation. It is putting a lot of farmers in the situation of having their land reclassified as nonagricultural. If changing the criteria has to be done through the Legislature, Senator Black believes that legislation should be proposed to correct ownership rules and correct the current situation.

<u>Rules related to dependents for medical savings account</u>

Shona McHugh, Department of Revenue, discussed the Medical Care Savings Account. The Montana Medical Care Savings account allows Montanans to save money for medical expenses and long term health care. A question was raised as to how this act applies to grandparents in Montana who are raising their grandchildren. The present rules only allow a parent to open a Medical Care Savings account to provide medical expenses for their dependent children. The department is proposing legislation to change the definition of dependent to include minors whose grandparents are responsible for them.

<u>IRIS Update</u>

Don Hoffman, Acting Director, DOR, provided a brief update on the IRIS project. Mr. Hoffman said that Phase I of IRIS is complete. The oil and gas tax was on the new system in August. There are five taxes that are on IRIS. Mr. Hoffman provided a report that shows what has been occurring with the IRIS project. (Exhibit 8) Another contract has been signed to continue with the project. The contract was for an additional $7 million with a loan secured from the Board of Investments. The corporation tax will be added in January 2005 and individual income tax will be added in September 2005.

Jeff Martin, Research Analyst, LSD, discussed assigning sponsors for the committee bills voted on at the last meeting. It was decided that it would be postponed until the meeting after the election. He also asked the committee to request a committee bill be drafted for the revenue estimating resolution.

MOTION: Rep. Devlin moved to request that the Revenue and Transportation Committee request a committee bill for the revenue estimating resolution. **VOTE:** Motion passed.

(Tape 3; Side B)

Use of recycled glass in road base and in other local markets

Brian Spangler, Department of Environmental Quality, provided several handouts: 1) Mobile Glass Pulverizer and Local Markets; 2) The Economic and Ecological Impacts of Recycling in Montana; 3) Glass Cullet Use for Soil-Aggregate Base Course; and 4) a sample of glass cullet. (Exhibits 9, 10, 11 and 12) Mr. Spangler said the system is able to pulverize all types of glass containers with no need to sort colors or remove labels. The system produces a rounded glass particle (non-fractured edge) and is less than 3/8" in size and processes 3-5 tons per hour. Estimated annual operating cost is $50,000.

Discussion of Montana Department of Transportation legislation

- **signs on secondary roads (Committee bill)**

Dave Galt, Director, Montana Department of Transportation, provided a copy of statute on highway encroachments. (Exhibit 13) Mr. Galt said that the sign issue has become serious on county secondary roads. Rather than drafting legislation at this time, the department would like to do an inventory of the sign situation and present something to the 2005 Legislature. In the meantime, signs in the right of way will not be removed, but if a sign is in the clear zone it will be removed.

- **prohibition of open containers in motor vehicles**

Mr. Galt provided a bill draft for open container legislation (Exhibit 14)

Safety Report Update

Dave Galt, Director, Montana Department of Transportation, provided an updated list of traffic fatalities for June and July 2004. (Exhibit 15) According to the report, out of the 48 fatalities, alcohol was determined to be a factor in 19. The number of fatalities for this year is down 32 from this time last year.

Mr. Galt provided a list of the members of the safety committee (Exhibit 16) The safety committee had its first meeting and hired a consultant to help the department develop a comprehensive safety plan. The committee will meet again in December and the department will post developments on its website.

Highway Special Revenue Account

Jim Currie, Deputy Director, Montana Department of Transportation, handed out a draft of the budget request for highway state special revenue account for the 2007 biennium. (Exhibit 17) The document includes the budget for fiscal year 2005 and the budget request for fiscal years 2006 and 2007. Based on current information, the state special revenue fund account is solvent through fiscal year 2007. The department is assuming federal aid funding of $325 million in fiscal year 2006.

(Tape 4; Side A)

Status of federal funding for highways

Sandra Straehl, Montana Department of Transportation, said that approximately 90 percent of Montana's construction program is federal aid funded. The current extension on appropriations authorization expires on September 24, and Congress has withheld $1.8 billion. Congress has not decided whether the $1.8 billion will be distributed for earmarked projects or by formula. If it is distributed by formula, Montana would get about $17 million. A Department of Defense bill passed last month may distribute about $8 million. In 2005, the U.S. House of Representatives appropriated $34.6 billion and the Senate appropriated $34.9 billion. If the highway money is distributed by formula, Montana could expect $317 million. The distribution formula is in the reauthorization bill and may be subject to change.

Design-build contracting program

Dave Galt, Montana Department of Transportation, provided an outline of the MDT Design-Build program. (Exhibit 18) Mr. Galt said that an advisory group was formed and met before beginning the first project. The Motor Carrier Services facility in Wibaux, was awarded in August 2004. Project duration is 365 calendar days. The Lincoln road/I-15 interchange is a safety improvement project scheduled to begin in February 2005 and the Dupuyer south reconstruction project is tentative pending right-of-way acquisition. The department plans to have a report to the legislature in 2007.

Test results of using biodiesel fuel in state vehicle fleet

Chris Strong, Western Transportation Institute, handed out copies of his presentation on the Evaluation of Biodiesel Fuel: Field Test. (Exhibit 19) Mr. Strong said that HB 502 proposed that all diesel fuel used in state vehicles, contain 2 percent biodiesel. There was concern about the impact of biodiesel on engines and if there might be long-term effects that would be harmful. The department was directed to look into engine performance, cold weather product storage, emissions and the potential for engine damage. Phase I and II of the study typically showed minimal difference in engine performance; there was no significant engine damage; studies showed that cold weather was not a problem for biodiesel of B20 or less; studies also showed that biodiesel is environmentally beneficial. Currently there are no federal fuel tax implications and it appears that cost is the biggest barrier for widespread implementation. The next of step of the project is to review state policies; production and prices; develop policy alternatives and complete draft report by the end of September.

Update on Highway 2 environmental impact statement

Dave Galt, Montana Department of Transportation, handed out the MDT Change on Highway 2 Stance. (Exhibit 20) Mr. Galt said that all of the analysis done as part of the U.S. 2 Havre to Fort Belknap EIS clearly supports an improved two-lane alternative with passing lanes. The department studied all the alternatives, looked at the impacts, costs and justifications; and in keeping with the practices outlined in NEPA, recommend an improved two-lane design with passing lanes as a preferred alternative. The estimated cost of the improved two-lane with passing lanes is $73.4 million; the four-lane alternative is $106.8 million.

Mr. Galt provided a document on the Estimated Federal and State Resources Used. (Exhibit 21) This document shows estimated cost resulting from SB 3 (2001) not including EIS. In addition, the EIS has caused a delay which will cost the state an additional $3 million in federal-aid and state funds.

Representative Kaufmann asked if SB 3 needs to be repealed. Mr. Galt said it is a directive of the Legislature and the department may not be in compliance.

Tape 4; Side B

Not on the Agenda

Mr. Galt presented an update on the Montana Branch Line Study Phase II. (Exhibit 22) Based on rail line condition and traffic, the railroads in the study are considered at risk of being abandoned by class 1 railroad. On page 31 of the report is a summary of Financial, Marketing and Operational Analysis to keep the lines maintained in a class I fashion.

Legislation Request:

Mr. Galt said that overweight load carriers are allowed to purchase an annual permit. The permits are sold in weight increments of 5,000, 10,000, 15,000, 20,000, 25,000, 30,000, and 40,000. Some of the larger carriers requested a 35,000 pound weight permit. This would not change any of the processes in getting a permit, it would only add a different weight.

Public Comment

John Brenden, Scoby, commented on the delays and wetland mitigation and said that it needs to be rectified. He also expressed concern about abandoning railroads.

Other Business

The next meeting is November 15, 2004. There being no further business, the meeting adjourned at 3:15 p.m.