Revenue Estimate Recommendations
Special Session December 2005

Fiscal Years 2006 and 2007

Prepared by the

Legislative Fiscal Division

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Legislative Fiscal Division

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INTRODUCTION

In accordance with the provisions of Section 5-12-302, MCA, this report provides the Revenue and Transportation Interim Committee (RTIC) with Legislative Fiscal Division (LFD) recommendations of revised general fund revenue estimates for fiscal years 2006 and 2007. It should be noted that the accompanying recommendations are based on current federal and state laws and do not include estimates for revenues due to litigation or any other pending legal issues. This position is consistent with past recommendations to the RTIC.

At the September 30, 2005 meeting, the RITC directed LFD staff to provide revised general fund revenue estimate recommendations to the committee in anticipation of a special legislative session. Since a majority of the difference between fiscal 2005 actual collections and HJR 2 revenue estimates (adjusted for legislation) was due to individual income and corporation income taxes, and to some degree, oil and natural gas production taxes, the committee directed staff to limit their review and potential adjustments to only the economic assumptions and the associated revenue estimates for these three sources. As had been done in the past, the committee also directed LFD staff to calculate the associated impact on US mineral royalty and common school interest and income revenues provided an adjustment was adopted for oil and natural gas price and production levels. The one exception to the above direction was for property tax. Because the committee felt taxable values of property classes were essential to the development of a new public school funding formula, it directed staff to review property tax taxable value assumptions. Even though the Quality Schools Interim Committee did not recommend school funding legislation for the special legislative session, staff has provided updated property tax estimates based on known taxable values for tax year 2005 (fiscal 2006). All other revenue sources remain as contained in HJR 2 as amended by the 59th Legislature.

In addition, Chairman Elliott, requested that staff of the LFD and the Executive (OBPP) work together to identify and explain significant differences prior to the RTIC meeting. Not only was this goal accomplished, but also the revenue estimate recommendations contained in this document reflect agreement between LFD and OBPP staff. This agreement was achieved by each office working independently combined with a series of work sessions to discuss relevant and significant differences. Since all of these differences were resolved, both offices could agree with the recommendations contained in this report.

Discussion of 2005 Revenues

When the legislature adjourned the 59th Legislative Session, fiscal 2005 revenue collections, as contained HJR 2 as adjusted for legislation, were expected to be $1,397.6 million. When the dust cleared at the end of fiscal 2005, actual collections were $1,530.9 million or $133.4 million more than anticipated. The majority of the unanticipated increase was from two revenue sources – individual and corporation income tax ($123.4 million).

Individual income tax collections for fiscal 2005 were $91.5 million above estimates contained in HJR 2 as adjusted for enacted legislation. This amount represents a 16.7 percent increase above fiscal 2004 collections. The 59th Legislature assumed the growth rate to be 1.6 percent above the fiscal 2004 amount. The following explains the reasons for the increase in fiscal 2005 collections. The figure above shows the accounting details of individual income tax collections for fiscal 2005 compared to fiscal 2004. Withholding taxes, which are an indicator of wage growth, grew by 5.3 percent, this was lower than the growth in wage and salary income seen from the 2004 tax return data of 5.8 percent.

Individual Income Tax Comparison

Revenue Code & Description	Actual Fiscal 2004	Actual Fiscal 2005	Difference	Percent Change
510101 Withholding Tax	474,851,498.28	501,230,798.36	26,379,300.08	5.26%
510102 Estimated Tax	152,143,812.91	199,884,808.59	47,740,995.68	23.88%
510103 Current Year I/T	103,283,893.97	134,284,266.54	31,000,372.57	23.09%
510105 Income Tax - Audit Collections	29,922,459.00	37,240,150.93	7,317,691.93	19.65%
510106 Income Tax Refunds	(154,853,243.51)	(166,405,444.62)	(11,552,201.11)	6.94%
Totals	$605,348,420.65	$706,234,579.80	$100,886,159.15	16.67%
Percent of Actual/Estimated	100.00%	114.88%		

The figure on the previous page, also shows that estimated and current year payments are above the previous year's amount by 23.9 percent and 23.1 percent, respectively. As shown in figure below, three non-wage income components (dividends, capital gains, rents/royalties/partnership incomes) for tax year 2004 were higher than anticipated in HJR 2. All the remaining components of income, when combined, were very close to the estimated amounts contained in HJR 2.

Individual Income Tax
Income Components Comparison (In Millions)

Income Components	Tax Year 2004 Estimated	Tax Year 2004 Actual	Difference	Percent Difference
Dividend Income	332.987	379.386	46.399	12.23%
Net Capital Gain	790.913	1,193.177	402.264	33.71%
Rent, Royalty, Partnership	1,123.657	1,283.271	159.614	12.44%
All Other Income	12,858.049	12,877.313	19.264	0.15%
Totals	15,105.606	15,733.147	627.541	3.99%

Senate bill 407, enacted by the 58th Legislature, changed the tax structure for individual income taxpayers. In the aggregate, this legislation was expected to reduce individual income tax collections in fiscal 2005 and subsequent years. Since this legislation was effective January 1, 2005, it was unclear whether taxpayers would adjust their estimated payments during the last six months of fiscal 2005. For example, if a taxpayer liability decreased under SB 407 but the taxpayer continued to submit estimated payments at the old rate, tax collections for fiscal 2005 would be overstated. This would result in a refund being claimed in fiscal 2006. Discussions with accounting firms indicated this occurred.

And finally, audit collections in fiscal 2005 were $37.2 million or $11.7 million more than anticipated in HJR 2.

Corporation income tax revenues in fiscal 2005 were $98.2 million, $31.9 million or 48.1 percent greater than projected in HJR 2 as adjusted for enacted legislation. Two known factors played a critical role in the increased corporation tax revenues. First, the fiscal 2005 estimate assumed $8.4 million of unusual refunds would be issued. Based on discussions with the Department of Revenue (DOR), these refunds have not occurred but are expected to be issued within the 2007 biennium. Second, the HJR 2 estimate included anticipated audit collections of $3.0 million. Actual audit receipts were about $10.6 million. According to the DOR, there were no unusually large audits in fiscal 2005. Another factor that has positively influenced corporation taxes is the improvement in the national economy since "9/11" and the 2002 recession. The increase in corporate profits at the national level has been significant and it is clear that Montana has benefited from this improvement.

The figure on the following page shows the fiscal 2005 revenue estimates for the general fund account as adopted in HJR 2 during the 2005 legislative session as adjusted for enacted legislation. The adjacent columns in the table show actual collections, the amount collections were over or (under) the estimate, the percent difference, and the contribution percent. The contribution percent signifies the importance of each revenue component to the general fund account. For example, individual income taxes were 46.2 percent of the total general fund collections while wine taxes accounted for only 0.10 percent during fiscal 2005. This column of information shows that about 70.7 percent of general fund revenue collections in fiscal 2005 came from individual (46.2%), property (10.9%), vehicle (7.2%), and corporate (6.4%) taxes.

General Fund Receipts By Major Component
Fiscal 2005

Revenue Category	Estimated 2005 Receipts *	Actual 2005 Receipts	Over(Under) Estimate	Percent Difference	Contribution Percent
GF0100 Drivers License Fee	$2,958,000	$3,373,220	$415,220	14.04%	0.22%
GF0200 Insurance Tax	59,272,000	57,308,425	(1,963,575)	-3.31%	3.75%
GF0300 Investment Licenses	4,464,000	5,192,327	728,327	16.32%	0.34%
GF0400 Vehicle License Fee	80,360,000	80,132,416	(227,584)	-0.28%	5.24%
GF0500 Vehicle Registration Fee	31,730,000	30,639,380	(1,090,620)	-3.44%	2.00%
GF0600 Nursing Facilities Fee	5,855,000	5,913,086	58,086	0.99%	0.39%
GF0700 Beer Tax	2,933,000	2,936,880	3,880	0.13%	0.19%
GF0800 Cigarette Tax	34,608,000	35,116,847	508,847	1.47%	2.30%
GF0900 Coal Severance Tax	9,105,000	10,311,856	1,206,856	13.25%	0.67%
GF1000 Corporation Tax	66,332,000	98,213,717	31,881,717	48.06%	6.42%
GF1100 Electrical Energy Tax	4,295,000	4,074,409	(220,591)	-5.14%	0.27%
GF1150 Wholesale Energy Trans Tax	3,485,000	3,370,263	(114,737)	-3.29%	0.22%
GF1200 Railroad Car Tax	1,585,000	1,604,005	19,005	1.20%	0.10%
GF1300 Individual Income Tax	614,736,000	706,234,580	91,498,580	14.88%	46.19%
GF1400 Inheritance Tax	3,701,000	4,190,613	489,613	13.23%	0.27%
GF1500 Metal Mines Tax	4,483,000	5,264,276	781,276	17.43%	0.34%
GF1700 Oil Severance Tax	58,206,000	62,625,939	4,419,939	7.59%	4.10%
GF1800 Public Contractor's Tax	1,748,000	1,410,831	(337,169)	-19.29%	0.09%
GF1850 Rental Car Sales Tax	2,593,000	2,565,554	(27,446)	-1.06%	0.17%
GFXXX Property Tax	169,370,000	167,270,350	(2,099,650)	-1.24%	10.94%
GF2150 Lodging Facilities Sales Tax	10,113,000	10,200,914	87,914	0.87%	0.67%
GF2200 Telephone Tax	0	31,657	31,657		0.00%
GF2250 Retail Telecom Excise Tax	21,307,000	21,144,420	(162,580)	-0.76%	1.38%
GF2300 Tobacco Tax	3,677,000	4,024,017	347,017	9.44%	0.26%
GF2400 Video Gaming Tax	52,932,000	53,361,007	429,007	0.81%	3.49%
GF2500 Wine Tax	1,436,000	1,502,601	66,601	4.64%	0.10%
GF2600 Institution Reimbursements	16,082,000	12,508,688	(3,573,312)	-22.22%	0.82%
GF2650 Highway Patrol Fines	4,104,000	4,292,730	188,730	4.60%	0.28%
GF2700 TCA Interest Earnings	9,174,000	10,046,531	872,531	9.51%	0.66%
GF2900 Liquor Excise Tax	11,125,000	11,468,432	343,432	3.09%	0.75%
GF3000 Liquor Profits	6,608,000	6,650,000	42,000	0.64%	0.43%
GF3100 Coal Trust Interest Earnings	33,892,000	36,751,940	2,859,940	8.44%	2.40%
GF3300 Lottery Profits	7,273,000	6,222,555	(1,050,445)	-14.44%	0.41%
GF3450 Tobacco Settlement	2,871,000	2,977,777	106,777	3.72%	0.19%
GF3500 U.S. Mineral Leasing	26,878,000	27,293,725	415,725	1.55%	1.79%
GF3600 Other Revenue	28,304,000	34,722,736	6,418,736	22.68%	2.27%
Total Current Year Revenue	$1,397,595,000	$1,530,948,704	$133,353,704	9.54%	100.14%
Prior Year Adjustments	0	(2,105,948)	(2,105,948)		-0.14%
Residual Equity Transfers	0	0	0		0.00%
Total Revenue	$1,397,595,000	$1,528,842,756	$131,247,756	9.39%	100.00%

* House Joint Resolution 2 estimates as adjusted for enacted legislation.

At the bottom of the figure shown above, prior year adjustments and residual equity transfers are shown, providing a complete picture of the total revenue flow in the account.

The figure on the next page shows the revised revenue estimate recommendations for fiscal 2006 and 2007 for the general fund account. Information provided includes the HJR 2 plus legislation estimate, the revised recommendations, and the difference for each year of the 2007 biennium. As shown in the figure, staff is recommending the general fund estimates be increased by $121.7 million in fiscal 2006 and $131.3 million in fiscal 2007 for a biennial adjustment of $253.0 million.

Common school interest and income estimates, which are non-general fund revenues, are recommended to be adjusted by $9.9 million in fiscal 2006 and $8.0 million in fiscal 2007 for a biennial increase of $17.9 million.

House Joint Resolution 2 Plus Legislation Impacts
General Fund Revenue Estimates
In Millions

			Fiscal 2006			**Fiscal 2007**			**2006-2007 Biennium**		
Source of Revenue	Percent Biennium	HJR 2 Plus Legislation	Spec. Sess. Recommend.	Change	HJR 2 Plus Legislation	Spec. Sess. Recommend.	Change	HJR 2 Plus Legislation	Spec. Sess. Recommend.	Change	Cumulative % of Total
1 Individual Income Tax	44.29%	607.178	677.815	70.637	630.060	712.611	82.551	1,237.238	1,390.426	153.188	44.29%
2 Property Tax	11.44%	173.804	176.391	2.587	180.062	182.900	2.838	353.866	359.291	5.425	55.73%
3 Oil & Natural Gas Production Tax	6.11%	61.192	99.410	38.218	64.958	92.554	27.596	126.150	191.964	65.814	61.84%
4 Corporation Income Tax	6.01%	81.148	91.427	10.279	78.997	97.281	18.284	160.145	188.708	28.563	67.85%
5 Vehicle Tax	5.17%	80.140	80.140	-	82.050	82.050	-	162.190	162.190	-	73.02%
6 Insurance Tax & License Fees	4.02%	61.580	61.580	-	64.637	64.637	-	126.217	126.217	-	77.04%
7 Video Gambling Tax	3.58%	55.031	55.031	-	57.509	57.509	-	112.540	112.540	-	80.62%
8 Motor Vehicle Fee	2.29%	35.029	35.029	-	36.960	36.960	-	71.989	71.989	-	82.92%
9 Cigarette Tax	2.07%	33.069	33.069	-	31.790	31.790	-	64.859	64.859	-	84.98%
10 Coal Trust Interest	2.05%	32.211	32.211	-	32.290	32.290	-	64.501	64.501	-	87.04%
11 All Other Revenue	1.82%	27.389	27.389	-	29.601	29.601	-	56.990	56.990	-	88.85%
12 US Mineral Royalty	1.74%	26.712	26.712	-	27.962	27.962	-	54.674	54.674	-	90.59%
13 Telecommunications Excise Tax	1.40%	21.700	21.700	-	22.101	22.101	-	43.801	43.801	-	91.99%
14 Public Institution Reimbursements	0.96%	15.127	15.127	-	15.049	15.049	-	30.176	30.176	-	92.95%
15 Treasury Cash Account Interest	0.87%	13.102	13.102	-	14.367	14.367	-	27.469	27.469	-	93.82%
16 Liquor Excise & License Tax	0.75%	11.535	11.535	-	11.959	11.959	-	23.494	23.494	-	94.57%
17 Lodging Facility Use Tax	0.70%	10.715	10.715	-	11.419	11.419	-	22.134	22.134	-	95.28%
18 Coal Severance Tax	0.54%	8.466	8.466	-	8.644	8.644	-	17.110	17.110	-	95.82%
19 Lottery Profits	0.50%	7.844	7.844	-	7.839	7.839	-	15.683	15.683	-	96.32%
20 Liquor Profits	0.44%	6.786	6.786	-	7.017	7.017	-	13.803	13.803	-	96.76%
21 Nursing Facilities Fee	0.37%	5.851	5.851	-	5.824	5.824	-	11.675	11.675	-	97.13%
22 Metalliferous Mines Tax	0.34%	5.236	5.236	-	5.438	5.438	-	10.674	10.674	-	97.47%
23 Highway Patrol Fines	0.33%	5.042	5.042	-	5.324	5.324	-	10.366	10.366	-	97.80%
24 Investment License Fee	0.30%	4.598	4.598	-	4.736	4.736	-	9.334	9.334	-	98.10%
25 Electrical Energy Tax	0.27%	4.276	4.276	-	4.270	4.270	-	8.546	8.546	-	98.37%
26 Tobacco Tax	0.24%	3.779	3.779	-	3.847	3.847	-	7.626	7.626	-	98.62%
27 Wholesale Energy Tax	0.23%	3.520	3.520	-	3.555	3.555	-	7.075	7.075	-	98.84%
28 Beer Tax	0.19%	2.986	2.986	-	3.039	3.039	-	6.025	6.025	-	99.03%
29 Driver's License Fee	0.18%	2.784	2.784	-	2.792	2.792	-	5.576	5.576	-	99.21%
30 Public Contractors Tax	0.18%	3.030	3.030	-	2.522	2.522	-	5.552	5.552	-	99.39%
31 Rental Car Sales Tax	0.18%	2.704	2.704	-	2.820	2.820	-	5.524	5.524	-	99.56%
32 Tobacco Settlement	0.15%	2.319	2.319	-	2.309	2.309	-	4.628	4.628	-	99.71%
33 Railroad Car Tax	0.10%	1.574	1.574	-	1.562	1.562	-	3.136	3.136	-	99.81%
34 Wine Tax	0.10%	1.487	1.487	-	1.538	1.538	-	3.025	3.025	-	99.91%
35 Estate Tax	0.09%	1.950	1.950	-	0.939	0.939	-	2.889	2.889	-	100.00%
Total General Fund	100.00%	$1,420.894	$1,542.615	$121.721	$1,465.786	$1,597.055	$131.269	$2,886.680	$3,139.670	$252.990	100.00%
Common School Interest & Income		$57.149	$67.013	$9.864	$56.233	$64.225	$7.992	$113.382	$131.238	$17.856	

How to Use This Report

The following section of this report contains revenue estimate recommendations for five revenue sources:

1. Corporation Income Tax
2. Individual Income Tax
3. Oil and Natural Gas Production Tax
4. Property Tax
5. Common Schools Interest & Income

A profile for each of the above revenue sources contains 10 categories of information. These categories and a short description of each follow:

Revenue Description: A brief description of the source is provided including the origin of the revenue and, in the case of taxes and fees, the item that is taxed.

Applicable Tax Rate(s): This section provides an explanation of the tax rate or license fee, more detail on the items that are taxed, and other information such as exemptions, minimums, initial versus annual fees, etc.

Distribution: This section shows how the revenue is distributed. In cases where uses or entities other than general fund receive a portion of the revenue, percentage distribution or the dollar amount is shown for each recipient.

Collection Frequency: Timing of the revenue deposited in the state treasury may affect the revenue estimate. Most revenue is usually received on a quarterly or monthly basis.

Statutory Reference: These are the citations from the Montana Code Annotated (MCA) applicable to the revenue source and include citations for the tax rate, the distribution, and when the tax is due.

Additional Information Since Adjournment: A general description of changes that have impacted the specific revenue source since the 59th Legislature adjourned.

Revenue Projection: This section consists of a graph and accompanying data table. The line graph shows the amount of actual collections and the projected amounts for fiscal years 2006 and 2007. Total collections are depicted by a dark line while general fund collections are shown by a lighter line. The data table contains historic information about this data source since 1983 including: 1) actual total collections; 2) actual general fund collections; 3) projected total and general fund amounts for fiscal 2006 and 2007; and 4) the yearly percentage change in general fund.

HJR 2 Comparison: This section includes a table that shows the HJR 2 revenue estimate, the LFD revenue estimate recommendations, and the difference between the two estimates for fiscal 2006, 2007 and a biennium total.

Discussion by Revenue Source

Corporation Income Tax

Revenue Description:

The corporation income tax is a license fee levied against a corporation's net income earned in Montana. The corporation income tax is imposed on corporations that, for reasons of jurisdiction, are not taxable under a license tax. Factors that affect corporation license tax receipts include tax credits and the audit efforts by the Department of Revenue. As with individual income tax, all forecasts are adjusted for allowable credits.

Applicable Tax Rate(s):

The tax rate is 6.75%, except for corporations making a "water's edge" election (see 15-31-322, MCA), who pay a 7.0% tax on their net income.

Distribution:

Prior to the enactment of SB 442 by the 2005 legislature, the Department of Revenue could distribute up to 0.45% of this general fund revenue source as an administrative assessment to a state special revenue account to pay debt service on the loan used to fund a POINTS replacement computer system (enacted in Senate Bill 271 by the 2003 legislature). SB 442 eliminated this provision. Beginning fiscal 2006, all corporation tax revenue is distributed to the general fund.

Collection Frequency:

Monthly, Quarterly, and Annually

Statutory Reference:

Tax Rate (MCA) – 15-31-121,
Tax Distribution (MCA) – 15-31-121, 15-1-501(1)
Date Due – by the 15th day of the fifth month following the close of the corporate fiscal year (15-31-111, 15-31-502).
Estimated taxes due April 15th, June 15th, September 15th, and December 15th (15-31-502).

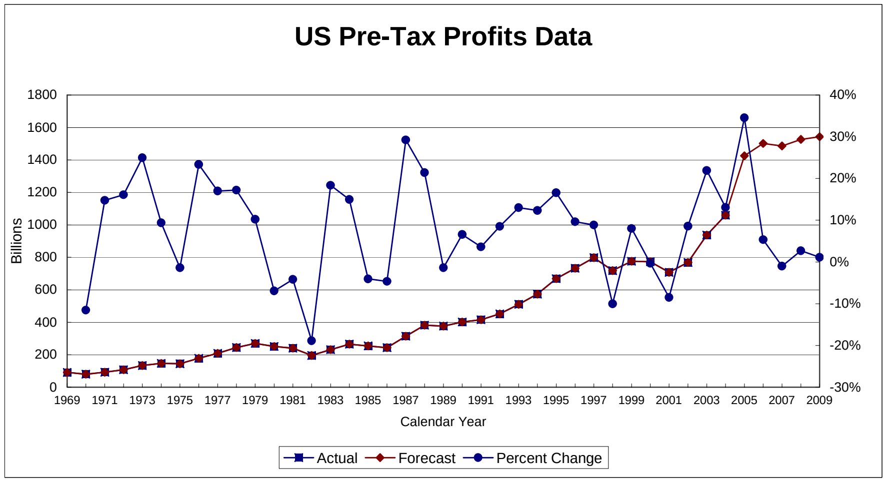
Additional Information Since Adjournment:

The corporation tax estimates are recommended to increase by $28.6 million, or 17.8 percent, over the HJR 2 estimates for the 2007 biennium. Since the last legislative session, new data has shown higher corporation tax collections. An additional year of data from both the state accounting, budgeting, and human resource system (SABHRS) and return data from the Department of Revenue (DOR) shows a dramatic increase in collections for this source. The recommendations are $91.4 million in fiscal year 2006 and $97.3 million in fiscal year 2007.

Total corporation tax collections are expected to increase to $99.8 million in fiscal year 2006, but a carry-over of $8.4 million in unusual refunds is anticipated to reduce the total collections. The refunds did not occur in the 2005 biennium as assumed in the previous projection, and the DOR believes they may be issued in fiscal year 2006. Before the refund adjustment, collections from corporation license tax are expected to increase 1.6 percent over actual fiscal year 2005 collections of $98.2 million. Collections for fiscal year 2007 are then expected to decrease by 2.5 percent.

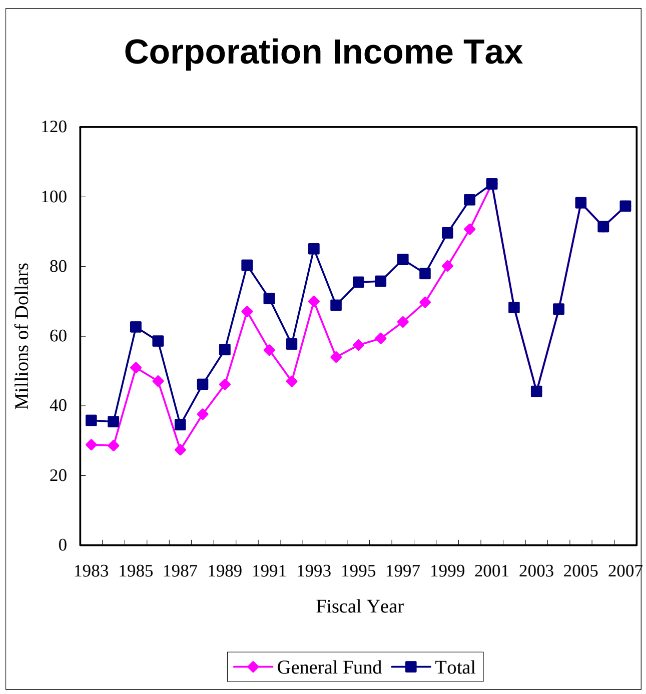
The DOR provides the estimates for corporation license tax audit collections. The recommendation for the 2007 biennium is $7.0 million, $3.5 million each fiscal year. In the 2005 biennium, actual audit collections, consisting of audit payments and interest and penalty payments, equaled $28.8 million ($14.2 million in fiscal 2004 and $10.6 million in fiscal 2005). The DOR estimates were used to create the recommendation, however the estimates are significantly understated when considering past collections. Additionally, the high audit collections in the 2005 biennium combined with the conservative estimates, distort the projected trend and make total growth appear lower than actually anticipated.

U.S. pre-tax corporation profits, as provided in the November 2005 Global Insight publication, are used in the development of the corporation license tax estimate. Consequently, the trend associated with the corporation license tax estimate is similar to the trend presented in the pre-tax profits series. As seen in the figure to the right, profits increased by almost 35.0 percent in calendar year 2005. In calendar year 2006 and 2007, growth slows significantly to 5.4 percent and negative 1.0 percent respectively.



Revenue Projection:

	Fiscal Year	Total Collections Millions	General Fund Collections Millions	GF Percent Change
A	1983	35.830832	28.832742	Not App.
A	1984	35.396240	28.573417	-0.90%
A	1985	62.609205	50.976990	78.41%
A	1986	58.584784	47.121070	-7.56%
A	1987	34.566361	27.371125	-41.91%
A	1988	46.200104	37.584806	37.32%
A	1989	56.139749	46.152627	22.80%
A	1990	80.315504	67.087905	45.36%
A	1991	70.784279	56.006784	-16.52%
A	1992	57.682672	47.027797	-16.03%
A	1993	85.054483	70.003987	48.86%
A	1994	68.871909	53.996713	-22.87%
A	1995	75.519940	57.425136	6.35%
A	1996	75.761891	59.336677	3.33%
A	1997	81.999138	64.078549	7.99%
A	1998	77.928498	69.724680	8.81%
A	1999	89.624560	80.142416	14.94%
A	2000	99.088867	90.682672	13.15%
A	2001	103.670487	103.670487	14.32%
A	2002	68.173253	68.173253	-34.24%
A	2003	44.137518	44.137518	-35.26%
A	2004	67.722940	67.722940	53.44%
A	2005	98.213717	98.213717	45.02%
F	2006	91.427000	91.427000	-6.91%
F	2007	97.281000	97.281000	6.40%



HJR2 Comparison:

Revised HJR 2 General Fund Revenue Estimates (In Millions)										
	Actual	HJR 2			LFD Recommendations			Difference		
Revenue Source	Fiscal 2005	Fiscal 2006	Fiscal 2007	Biennium	Fiscal 2006	Fiscal 2007	Biennium	Fiscal 2006	Fiscal 2007	Biennium
Corporation Tax	$98.214	$81.148	$78.997	$160.145	$91.427	$97.281	$188.708	$10.279	$18.284	$28.563

Individual Income Tax

Revenue Description:

The tax is levied against taxable income, which is defined as Montana personal income adjusted for exemptions and deductions. Once tax liability is determined, the amount of tax due is computed by subtracting allowable credits.

Applicable Tax Rate(s):

Tax rates vary from 1.0% to 6.9%, depending on the level of taxable income. Tax brackets, personal exemption amounts, and the standard deduction are adjusted by the rate of inflation in each year. SB 407, enacted by the 2003 legislature, created a new capital gains income tax credit. As a result, the tax rate on capital gains income is less than the tax rate on ordinary income by 1 percent in tax years 2005 and 2006, and by 2 percent in tax year 2007 and beyond.

Distribution:

Prior to the enactment of SB 442 by the 2005 legislation, beginning fiscal 2004 through fiscal 2011, the Department of Revenue could distribute up to 0.45% of this general fund revenue source as an administrative assessment to a state special revenue account to pay debt service on the loan used to fund a POINTS replacement computer system (enacted in Senate Bill 271 by the 2003 legislature). SB 442 eliminated this provision. All proceeds are deposited into the general fund.

Collection Frequency:

Withholding taxes are collected monthly, bi-weekly, and weekly, and estimated taxes are collected quarterly.

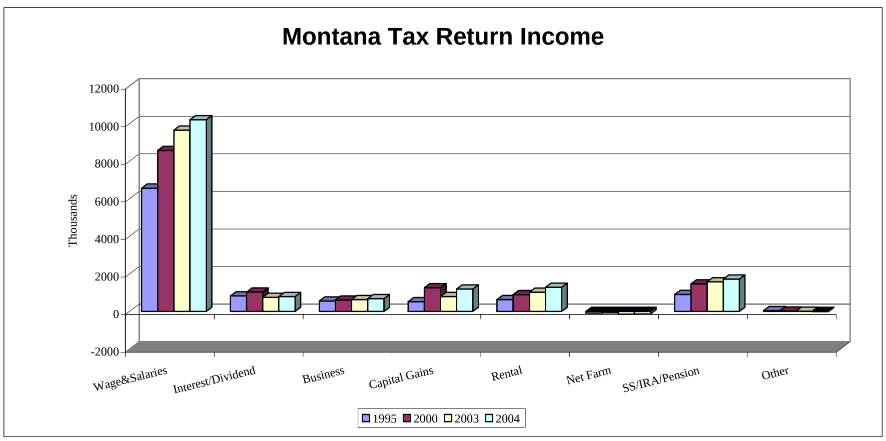
Statutory Reference:

Tax Rate (MCA) – 15-30-103
Tax Distribution (MCA) – 15-1-501(1)
Date Due – 15th day of the fourth month of the filer's fiscal year (15-30-144). Withholding taxes due monthly, quarterly, or on an accelerated schedule depending on income (15-30-204). Estimated taxes due on the 15th day of the 4th, 6th, and 9th month and the month following the close of the tax year.

Additional Information Since Adjournment:

The recommendation for individual income taxes is an increase of $153.2 million, or 12.4 percent, over the HJR 2 estimates for the 2007 biennium. Unexpectedly high collections in fiscal year 2005, an additional year of tax return data, coupled with new data from the Global Insight forecasting service were used to develop the recommendation for an upward adjustment to the individual income tax projection. Recommendations for the biennium include $677.8 million in fiscal 2006 and $712.6 in fiscal 2007.

Return data for the 2004 tax year became available in November. The figure to the right depicts the income category results of this data and compares it to data from tax years 1999, 2000, and 2003. As seen in this figure, most income sources experienced growth over tax year 2003. While growth in wages and salaries was expected, growth in dividends, capital gains, and rents and royalties was greater than anticipated.

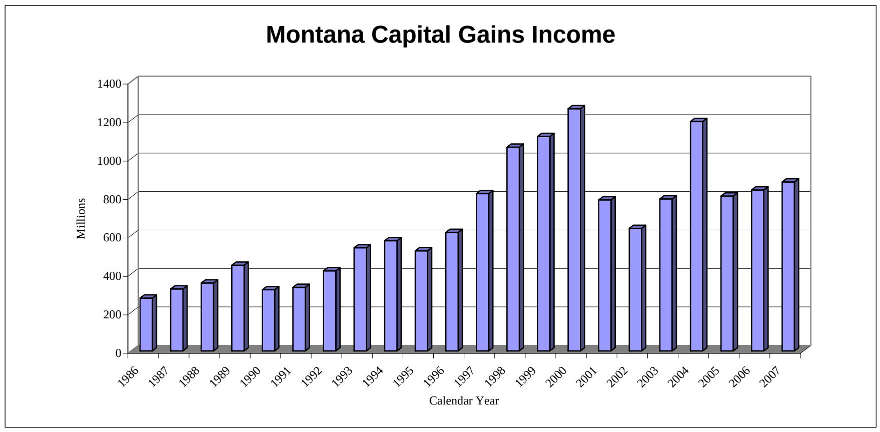


New information was used in the development of the individual income tax recommendations. Several modifications were made to the assumptions used in HJR 2. The economic assumptions used to produce the recommendation include:

1. Wage and salary income: increased by 5.8 percent in tax year 2004. HJR 2 assumed growth of 4.5 percent in tax years 2005 through 2007. While the assumption for 2004 was accurate, information provided by Global Insight shows wages and salaries growing at a rate of 8.4 percent in tax year 2005, 5.7 percent in tax year 2006, and 4.8 percent in tax year 2007.

2. Dividend income: increased by 27.6 percent in tax year 2004. Growth for tax year 2004 was estimated to be 12.0 percent. The assumption is that growth in this income source is the result of federal tax changes that reduced the tax on dividend income to 15.0 percent through tax year 2009. While a similar spurt of growth is not anticipated in future years, increased dividend income is expected during the period of preferential tax treatment. As a result, HJR 2 growth rates were not changed, but they are applied to the higher base of tax year 2004.

3. Capital gains income: increased by 50.9 percent in tax year 2004. As apparent in the figure to the right, income from capital gains nears the magnitude seen in the late 1990's. No growth had been assumed in tax year 2004 in HJR 2. Capital gains income includes the gains incurred from the sales of many forms of capital including land and equity investments. The tax return data provided by the DOR is provided in aggregate by taxpayer and does not segregate the sources of the gains. Regardless, it is assumed the significant increase of capital gains in the 2004 tax year results from individuals who have taken advantage of the new federal preferential tax treatment. Such significant increases are not expected to continue in future tax years. As a result, the recommendation uses the 2004 tax year as a base and assumes a return to the long-term trend line into the future.



4. Rents and royalty income: increased by 25.8 percent in tax year 2004. The growth assumption for this source of income was 10.2 percent for the 2004 tax year. As in the case of capital gains data, this category includes three sources of income: rents, partnership, and royalty income. The income data is provided as an aggregate figure. There is no method for determining whether rental, partnership, or royalty income is responsible for the significant increase. However, the dramatic increase in oil and natural gas production in the state suggests that the increase can be attributed to royalty income. As long as oil and gas production remain at current levels, the assumption is that rent and royalties income will also be strong. Accordingly, HJR 2 growth rates were not changed but they are applied to the higher base of tax year 2004.

In addition to modifying these growth rates, the recommendation includes changes to the population adjustment factor and the non-resident filers multiplier. These factors were adjusted slightly to agree with new data provided through Global Insight.

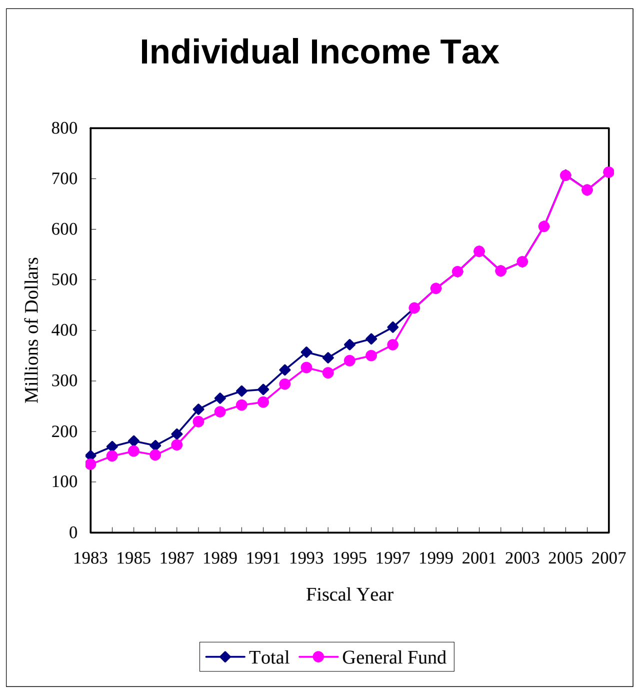
The DOR provides the estimates for individual income tax audit collections. The recommendation for the 2007 biennium is $45.0 million. In the 2005 biennium, actual audit collections, consisting of audit payments and interest and penalty payments, equaled $67.1 million ($29.9 million in fiscal 2004 and $37.2 million in fiscal 2005). The DOR estimates were used to create the recommendation, however the estimates are significantly understated when considering past collections. Additionally, the high audit collections in the 2005 biennium combined with the conservative estimates, distort the projected trend and make total growth appear lower than actually anticipated.

Estimated refunds for the 2005 tax year are expected to be higher than assumed in HJR 2 as a result of two factors related to the enactment of SB 407. The legislation became effective at the beginning of the 2005 tax year. In aggregate, this legislation was expected to reduce individual income tax collections in fiscal 2005 and subsequent years. First, the DOR distributed new withholding tables to the employers at the beginning of the 2005 tax year, followed by a revised tax table at a later date. There is still uncertainty when the new withholding tables, were implemented by employers in tax year 2005. Consequently, failure to use the new tables may result in additional refunds in fiscal 2006. Next, discussions with accounting firms indicate that some taxpayers were advised to make estimated payments, unadjusted for the impact of SB 407. Such actions would mean that taxpayers were paying taxes at too high a rate. This action would also result in additional refunds in fiscal 2006. The refund impacts of both situations is included in the recommendation.

Collectively, these changes produce a recommendation of $677.8 million in fiscal year 2006. This is an increase of 11.6 percent from the HJR 2 estimate. In fiscal year 2007, the recommendation is $712.6 million. The estimate is 13.1 percent greater than the HJR 2 estimate.

Revenue Projection:

	Fiscal Year	Total Collections Millions	General Fund Collections Millions	GF Percent Change
A	1983	151.800311	135.102282	Not App.
A	1984	170.346345	151.608247	12.22%
A	1985	181.057157	161.140870	6.29%
A	1986	172.216130	153.272356	-4.88%
A	1987	194.676947	173.262483	13.04%
A	1988	243.768721	219.241292	26.54%
A	1989	265.539814	238.963596	9.00%
A	1990	279.642960	252.230465	5.55%
A	1991	282.960086	258.216424	2.37%
A	1992	321.538093	293.564151	13.69%
A	1993	356.986934	326.187735	11.11%
A	1994	345.643403	315.677433	-3.22%
A	1995	371.902909	339.939156	7.69%
A	1996	383.091612	350.161013	3.01%
A	1997	406.275740	371.275410	6.03%
A	1998	444.160729	444.160729	19.63%
A	1999	483.031571	483.031571	8.75%
A	2000	516.261912	516.261912	6.88%
A	2001	556.014554	556.014554	7.70%
A	2002	517.567691	517.567691	-6.91%
A	2003	535.830664	535.830664	3.53%
A	2004	605.582309	605.348420	12.97%
A	2005	707.343334	706.234580	16.67%
F	2006	677.815000	677.815000	-4.02%
F	2007	712.611000	712.611000	5.13%



HJR2 Comparison:

Revised HJR 2 General Fund Revenue Estimates (In Millions)										
	Actual	HJR 2			LFD Recommendations			Difference		
Revenue Source	Fiscal 2005	Fiscal 2006	Fiscal 2007	Biennium	Fiscal 2006	Fiscal 2007	Biennium	Fiscal 2006	Fiscal 2007	Biennium
Individual Income Tax	$706.235	$607.178	$630.060	$1,237.238	$677.815	$712.611	$1,390.426	$70.637	$82.551	$153.188

Oil and Natural Gas Production Tax

Revenue Description:

The oil and natural gas production tax is imposed on the production of petroleum and natural gas in the state. Gross taxable value of oil and natural gas production is based on the type of well and type of production.

Applicable Tax Rate(s):

The oil and natural gas production tax has numerous tax rates depending on several factors. These factors include whether the oil or gas is produced from a stripper well, a stripper incentive well, from a well initially drilled before 1999 or after, from a well newly drilled within the last year or 18 months, and whether the interest being taxed is the working interest or the royalty interest. The Board of Oil and Gas Conservation imposes an additional privilege and license (P & L) tax on all oil and natural gas tax rates. For the 2007 biennium, the P&L tax rate is 0.26 percent. HB 758 (enacted by the 2005 legislature) allows an additional tax rate of 0.04 percent to generate revenue for local impacts for local governments. The two taxes may not exceed 0.3 percent. HB 535 (enacted by the 2005 legislature) created out of the "stripper well exemption" category a new tax category called "stripper well bonus" which is defined as production from a stripper well that produces three barrels a day or less. The figure to the right shows tax rate percentages for each type of pre-1999 oil and post-1999 oil, excluding the P & L tax and the new Local Impact tax. The quarterly tax rates on stripper production and on incremental production are lower than that for regular production unless the price of West Texas Intermediate averages above $30 for the quarter. Similarly, the quarterly tax rate for stripper well exemption production (1-3 barrels a day) is lower than that for regular production unless the price of West Texas Intermediate averages above $38 for the quarter.

Oil and Natural Gas Production Tax Rates *

Oil Production	Tax Rates
Working Interests	
Pre 99 after 12 Months (Regular)	12.50%
Post 99 First 12 Months (New)	0.50%
Post 99 after 12 months (Regular)	9.00%
Stripper 4-10 barrels per day	5.50%
Stripper 11-15 barrels per day	9.00%
Stripper Well Exemption (1-3 barrels per day)	0.50%
Pre99 Horizontal after 18 months	12.50%
Post 99 Horizontal first 18 months	0.50%
Post 99 Horizontal after 18 months	9.00%
Incremental - secondary	8.50%
Incremental - tertiary	5.80%
Pre99 Horizontal Recomp - after 18 months	12.50%
Post99 Horizontal Recomp - first 18 months	5.50%
Post99 Horizontal Recomp - after 18 months	9.00%
Royalty Interests	14.80%
Natural Gas Production	
Working Interests	
Pre-99 after 12 months	14.80%
Post 99 first 12 months	0.50%
Post 99 after 12 months	9.00%
Pre 99 stripper wells	11.00%
Horizontal first 18 months	0.50%
Horizontal after 18 months	9.00%
Royalty Interests	14.80%

If the West Texas price of oil exceeds $30/bbl in a quarter, the rates for stripper

* Excluding the P & L and Local Impact tax rates

Distribution:

Once the oil and natural gas production taxes have been collected, the revenue is first distributed based on the amounts collected from the P & L and Local Impact taxes. The amounts from the P & L tax are distributed to the: 1) Board of Oil and Gas Conservation; and 2) the Legislative Services Division - $50,000 only in the 2007 biennium. The amounts from the Local Impact tax are distributed to the oil, gas, and coal natural resource state special revenue account. The amounts received by the Board and the oil, gas, and coal natural resource account vary based on a sliding scale based on the P & L tax set by the Board. Counties producing oil receive the next share of the total revenue with each county having its own distribution percentage of total revenue, including the revenue generated by the P & L and Local Impact taxes. The remainder of the revenue is distributed to other state accounts in the following manner:

Fiscal 2004 though Fiscal 2011

- Coal bed methane account – 1.23%
- Reclamation and development account – 2.95%
- Orphan share account – 2.95%
- University system 6 mill levy account – 2.65%
- General fund – the remainder (90.22%)

The distributions of county shares and the amount of oil and natural gas production tax revenue deposited in the oil, gas, and coal natural resource account are statutorily appropriated and are based on the statutorily set percentages for each county.

Collection Frequency:

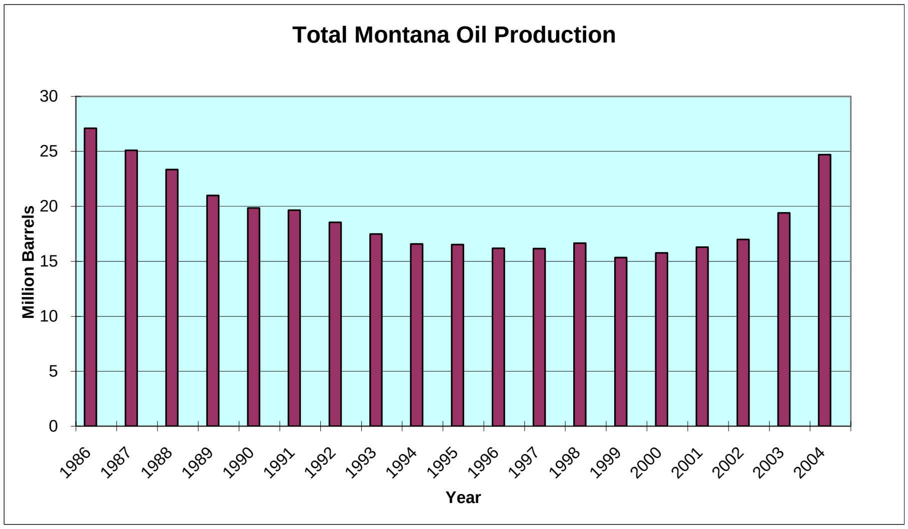
Quarterly: The oil and natural gas production tax is due 60 days after the end of the production quarter.

Statutory Reference:

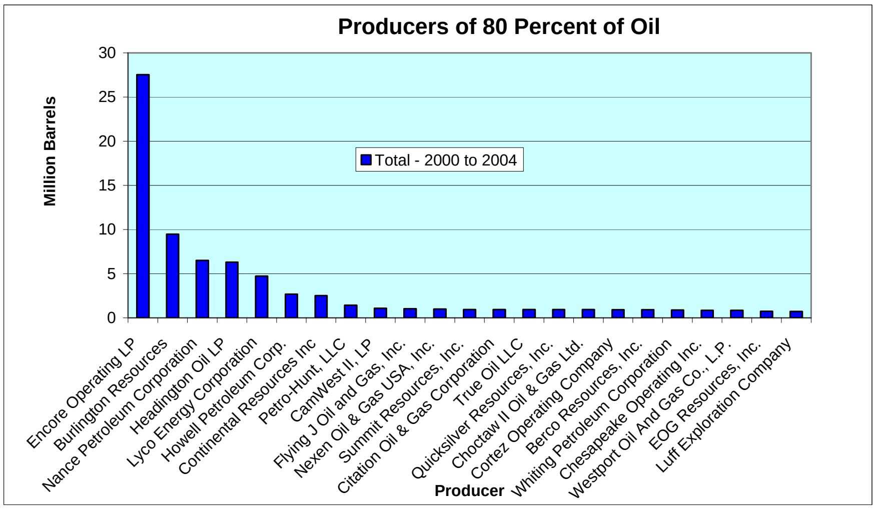
Tax Rate (MCA) – 15-36-30. Privilege and license tax – 82-11-131, Administrative Rules 36.72.1242
Tax Distribution (MCA)– 15-36-331(4), 15-36-332(2&3) (to taxing units)
Date Due – within 60 days after the end of the calendar quarter (15-36-311(1))

Additional Information Since Adjournment:

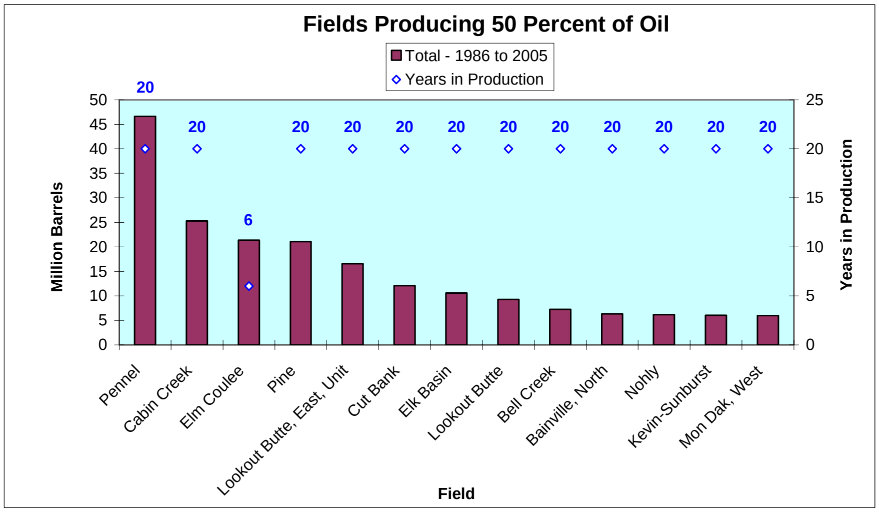
The recommendations for the oil and natural gas estimates are for an increase of $38.2 million in fiscal 2006 and $27.6 million in fiscal 2007 for a total of $65.8 million above HJR 2 estimates for the 2007 biennium. The oil estimates were based on assumptions of 34.9 million barrels at $57.79/per barrel in fiscal 2006, and 35.5 million barrels at $50.49/per barrel in fiscal 2007. The natural gas estimates were based on assumptions of 102.2 million MCF at $8.35/per MCF in fiscal 2006, and 101.1 million MCF at $8.10/per MCF in fiscal 2007.



The oil industry in Montana has been undergoing major changes. Improved techniques have allowed new fields to be developed and old fields to be more productive. The figures on this page show various aspects of this industry. Data from the Board of Oil and Gas Conservation enabled an isolation of production for each field. Analysis of the field data indicated that the majority of increased production is from the relatively new Elm Coulee field in Richland County. Production from fields other than Elm Coulee grew an average of 2.2 percent for the past five years, indicating that most of the increase in production is from the Elm Coulee field. Industry personnel state that although this field has yet to be fully defined, it probably is nearing that stage. When this occurs, fewer new wells will be spudded (drilling initiated).

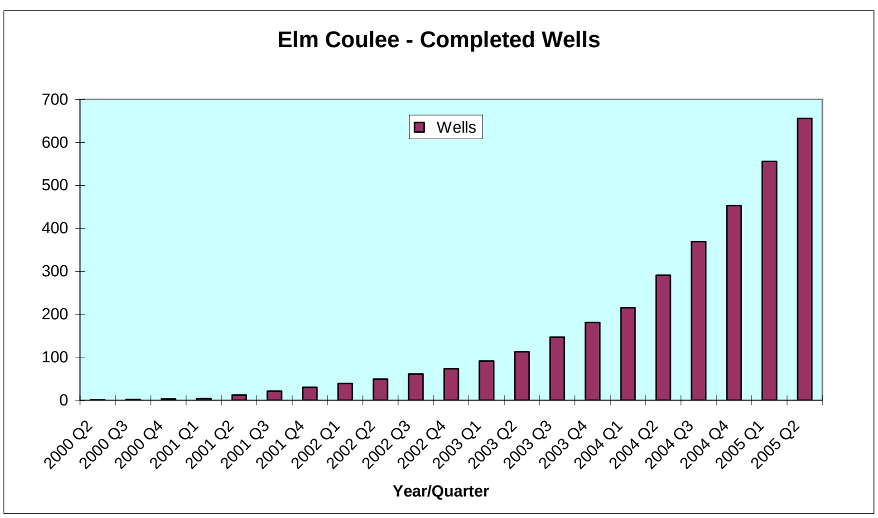


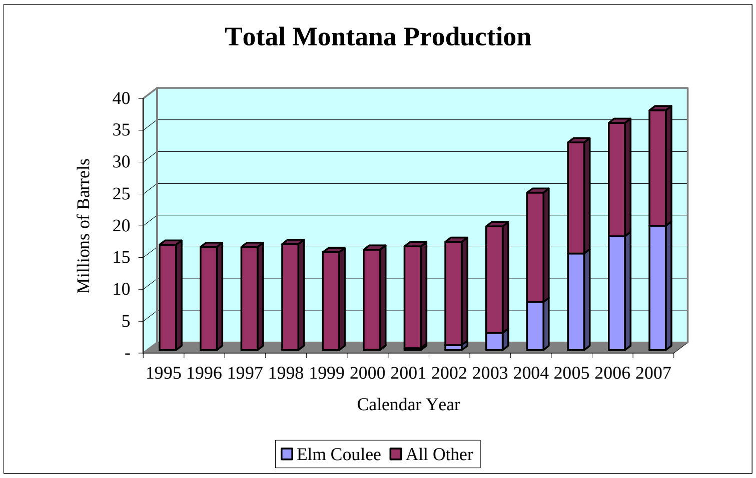
Existing wells will then follow a production decline curve unique to the characteristics of the field. Fields tapped through horizontal drilling, such as Elm Coulee, tend to be depleted more rapidly than those tapped vertically. The importance of Elm Coulee is shown in the figure below. The figure shows that even though the field has been in production for only six of the last 20 years, it ranks third in total production out of the major fields that have been producing for the entire 20 years. The Elm Coulee field first began production in 2000. From that time through August 2005, 197 wells had been completed and 48 wells have been spudded. Future production from completed wells can be estimated by developing a normalized production decline curve from the producing wells.



In doing so, the difficulty of having different starting time for each well can be eliminated by averaging each well's production from a common time point. The result is a curve that represents the average production of wells in the Elm Coulee field by month of production. Knowing monthly production from each well and the date it was placed into production are essential for estimating oil tax revenue because tax rates vary based on the length of time a well has been in production.

Production from future wells can be estimated by applying the production curve coefficients to an estimate of future spudded wells. The figure below shows the history of completed wells since the beginning of this field.



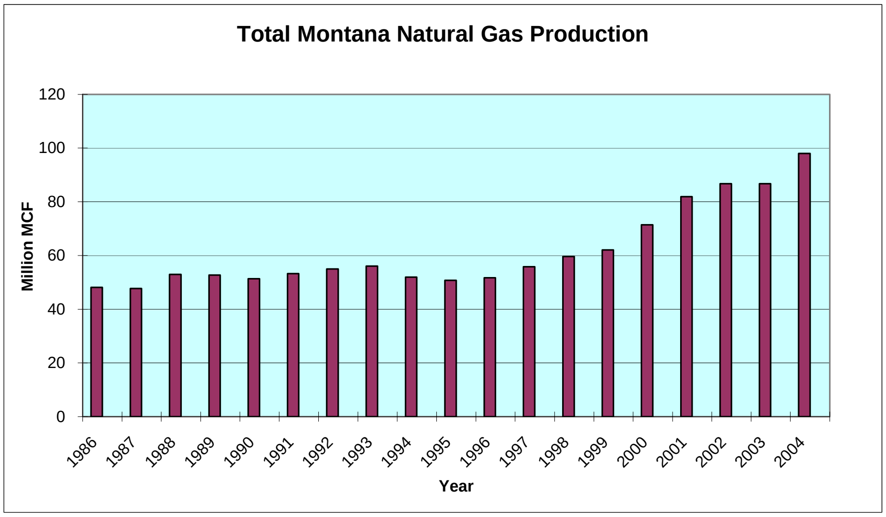


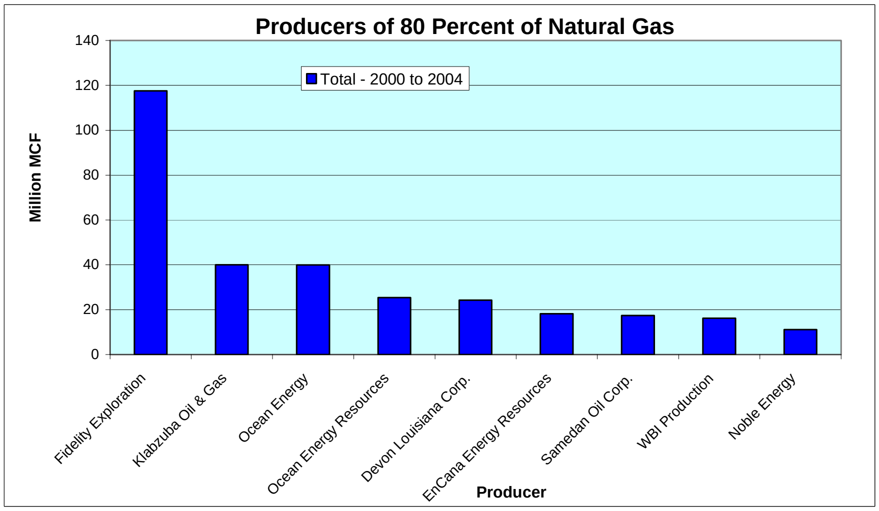
The importance this one field plays in the oil production tax estimate for the 2007 biennium is seen in the figure to the left. For this biennium it is estimated that, 51 percent of total statewide production comes from Elm Coulee.

In determining a price estimate for oil, Global Insight's future forecasts of West Texas Intermediate crude were used. In general, the price of WTI oil is expected to decrease from \$63/barrel to \$50/barrel during the 2007 biennium. Because the price received from Montana oil is normally lower than the quoted price for WTI, an adjustment to the WTI price was applied based on historical comparisons between the two prices.

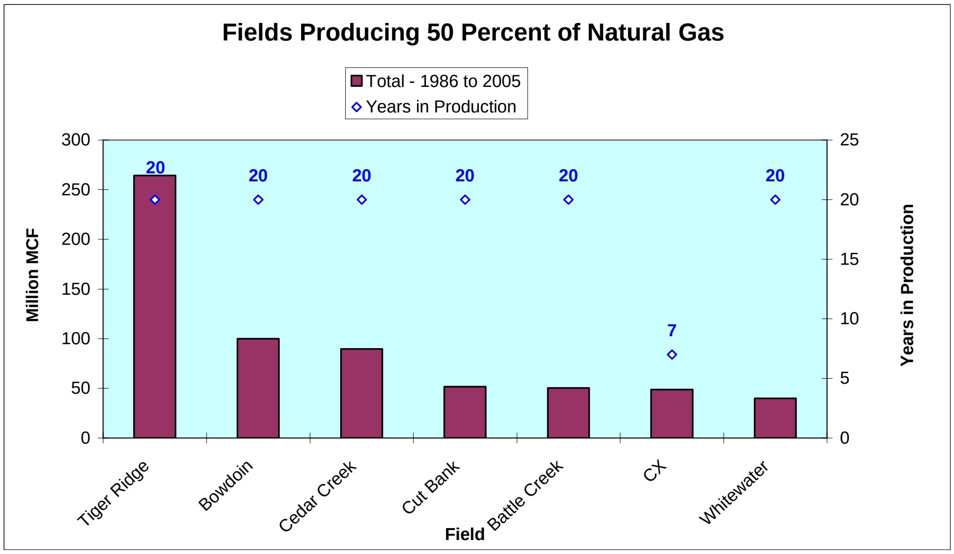
Natural Gas

The natural gas industry in Montana has also been undergoing major changes. Improved techniques have allowed new fields to be developed and old fields to be more productive. The figures on this page show various aspects of this industry. Data from the Board of Oil and Gas Conservation indicate that the majority of increased production is from the relatively new CX field in Big Horn County and the Elm Coulee field in Richland County. Other fields that exhibit increasing production are the Bowdoin and Cedar Creek fields, the second and third largest producing fields, respectively. Since its peak production in 1999,





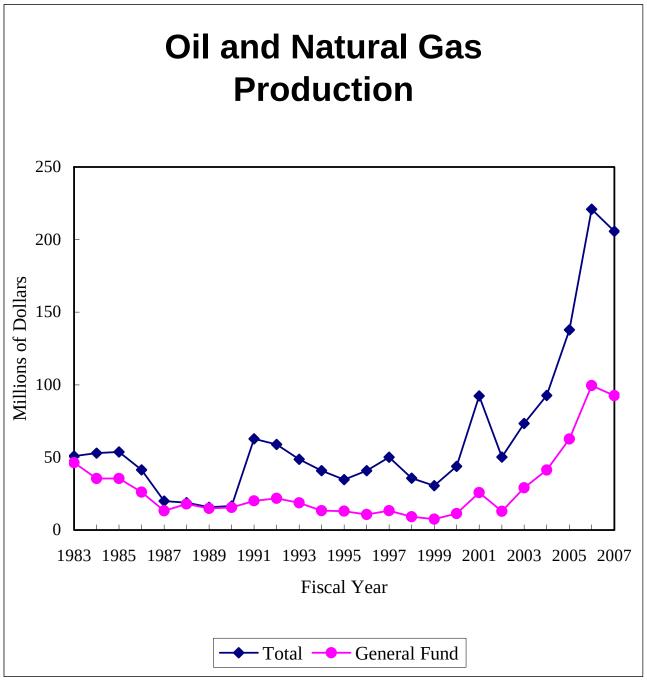
production from Tiger Ridge, the largest producing field, has declined. By excluding production from fields with increasing production, it was found that production from the remaining fields has been decreasing since 2001. Of the fields with increasing production, most is coming from the CX and Elm Coulee fields. The importance of the CX field is shown in the figure on the following page. The figure shows that even though the CX field has been in production for only seven of the last 20 years, in ranks sixth in total production out of the major fields that have been producing for the entire 20 years. A similar analysis to that used for oil can also be used for natural gas. The CX field began production in April 1999 and in 2004 produced 12.3 million MCF. From that time through August 2005, 543 wells have been completed, 95 of which were completed in 2005. In 2005, 25 wells have been spudded. The Elm Coulee field began production in 2000 and in 2004 produced 5.7 million MCF. As with oil, the development of a normalized production curve from individual wells eliminates the difficulty of having different starting time for each well by averaging each well's production from a common point in time. The result is a curve that represents the average production of wells in the CX field by month of production.



Global Insight does not provide future estimates of natural gas prices. In determining a price estimate for natural gas, Henry Hub spot market future forecasts were used. In general, the price is expected to decrease to $9.19/MCF at the end of the 2007 biennium. Because the price received from Montana natural gas is normally lower than the national price for natural gas, an adjustment was applied based on historical comparisons between the two prices.

Revenue Projection:

	Fiscal Year	Total Collections Millions	General Fund Collections Millions	GF Percent Change
A	1983	50.873263	46.313019	Not App.
A	1984	52.977130	35.484010	-23.38%
A	1985	53.667357	35.472434	-0.03%
A	1986	41.441086	26.043170	-26.58%
A	1987	19.904239	13.254877	-49.10%
A	1988	18.913097	17.975582	35.61%
A	1989	15.748241	14.959251	-16.78%
A	1990	16.486405	15.567426	4.07%
A	1991	62.879742	20.163269	29.52%
A	1992	58.892324	21.822893	8.23%
A	1993	48.650604	18.676586	-14.42%
A	1994	40.871318	13.403408	-28.23%
A	1995	34.704332	12.963887	-3.28%
A	1996	40.826475	10.665986	-17.73%
A	1997	50.150068	13.283093	24.54%
A	1998	35.709042	9.120152	-31.34%
A	1999	30.446634	7.505617	-17.70%
A	2000	43.772950	11.362741	51.39%
A	2001	92.395790	25.791723	126.99%
A	2002	50.303610	12.902439	-49.97%
A	2003	73.389376	29.086038	125.43%
A	2004	92.676048	41.323718	42.07%
A	2005	137.754330	62.625939	51.55%
F	2006	220.851727	99.410000	58.74%
F	2007	205.620267	92.554000	-6.90%



HJR2 Comparison:

Revised HJR 2 General Fund Revenue Estimates (In Millions)										
	Actual	HJR 2			LFD Recommendations			Difference		
Revenue Source	Fiscal 2005	Fiscal 2006	Fiscal 2007	Biennium	Fiscal 2006	Fiscal 2007	Biennium	Fiscal 2006	Fiscal 2007	Biennium
Oil Severance Tax	$62.626	$61.192	$64.958	$126.150	$99.410	$92.554	$191.964	$38.218	$27.596	$65.814

Property Tax

Revenue Description:

Montana law requires counties to levy a county equalization levy of 55 mills, a state equalization levy of 40 mills and 6 mills for the university system against all taxable value in each county. A mill levy of 1.5 mills is also applied against all property in the five counties with a vo-tech college. Taxable value is defined as the market value of statutorily defined property times a statutory tax rate. Property valued at market value includes personal property, utility property, railroad and airline property, and mineral net and gross proceeds. The assessed value of residential and commercial real estate is the market value phased in over the reappraisal cycle. Agricultural land and timberland are valued on a productivity basis and their values are also phased in over the reappraisal cycle. Beginning January 1, 2003, livestock is no longer taxed.

Beginning January 1, 2003, residential and commercial property as well as agricultural land and timberland reflect the impact of a new reappraisal on market values. The current reappraisal cycle is 6 years, during which increases in property values will be phased in by 1/6th per year. Property that declines in value will be assessed immediately at its new reappraised value. The impact of reappraisal on assessed values increased the market value of the average residence by 20.2 percent. The equivalent increases for commercial property were 18.5 percent and for agricultural land by 15.3 percent.

The 2003 legislature passed a reappraisal mitigation bill - SB 461 (see below). Beginning in tax year 2003, reappraisal values were phased in over the next six years. The new tax rates and the new homestead and comstead exemptions are shown in the accompanying table:

SB 461 Tax Rates and Exemption Percentages for Class 4 Residential and Commercial Property

Fiscal Year	Tax Rate	Class 4 Residential Exemption	Class 3 Multi Family Housing Exemption	Class 4 Commercial Exemption
2003 (prior law)	3.46%	31.0%	31.0%	13.0%
2004	3.40%	31.0%	31.0%	13.0%
2005	3.30%	31.4%	31.4%	13.3%
2006	3.22%	32.0%	32.0%	13.8%
2007	3.14%	32.6%	32.6%	14.2%
2008	3.07%	33.2%	33.2%	14.6%
2009	3.01%	34.0%	34.0%	15.0%

In addition to the tax on property, this revenue component includes collections from "non-levy" sources that are distributed on the basis of mills levied by taxing jurisdictions. These non-levy sources include the state share of coal gross proceeds taxes, federal forest revenues, and other smaller revenue sources.

This source also includes the state's share of protested taxes paid by centrally assessed companies. Should the state fail in it defense of the taxation of these companies, the protested taxes must be returned to the taxpayer. With the enactment of Senate Bill 87 by the 2005 legislature, one-half of protested taxes from the states 95 mills is deposited to the general fund and one-half is deposited to a fiduciary fund.

Applicable Tax Rate(s):

Each property class has its own tax rate that is applied to assessed value to produce a taxable value. For every $1,000 in taxable value, each mills generates $1 in state property taxes.

Distribution:

Most property tax receipts are deposited into the general fund. There are two exceptions: 1) revenue associated with the 6-mill university levy is deposited to the state special revenue fund; and 2) half of the revenue paid under protest for centrally assessed property is deposited in a fiduciary fund.

Collection Frequency:

Monthly with significant state deposits in December and June.

Statutory Reference:

Tax Rate (MCA) – 20-9-331(1), 20-9-333(1)
Tax Distribution (MCA) - 20-9-331(1), 20-9-333(1)
Date Due – one-half of taxes due November 30th and one-half due May 31st (15-16-102(1)), county treasurers must remit to the Department of Revenue within the first 20 days of each month money received in the previous month (15-1-504(1))

Additional Information Since Adjournment:

Property tax revenue for the 2007 biennium is recommended to increase by $5.4 million or 1.5 percent over the HJR 2 revenue estimate. Since the last legislative session, taxable values for tax year 2005 (fiscal 2006) have become known and can be used to recalculate estimated property taxes for the biennium (see the table below).

Property Taxable Values

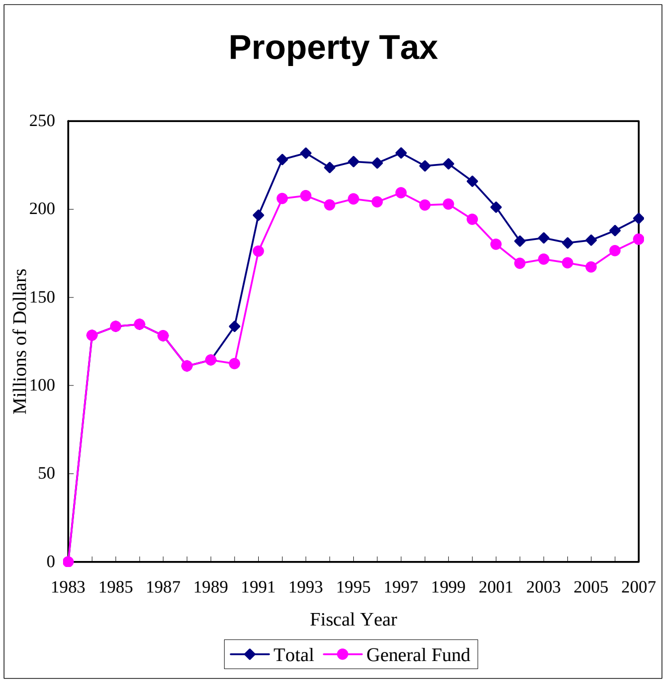
Tax Class	Name	TY 2005	FY 2006	FY 2007
Class 1	Net Proceeds	$2,694,216	$2,694,216	$2,694,216
Class 2	Gross Proceeds	13,045,195	13,045,195	13,045,195
Class 3	Ag Land	140,988,242	140,988,242	140,847,254
Class 4	Real Property	1,129,794,467	1,129,794,467	1,174,986,246
Class 5	Co-ops	34,611,220	34,611,220	34,611,220
Class 7	Independent Telephone	953,438	953,438	953,438
Class 8	Personal Property	123,054,946	124,972,142	130,096,000
Class 9	Utilities	238,766,675	238,766,675	238,527,908
Class 10	Timber Land	6,793,765	6,793,765	6,793,762
Class 12	RR & Airlines	44,267,220	44,267,220	43,580,253
Class 13	Electric, TelCom	122,845,989	122,845,989	122,845,989
Class 14	Wind Generation	0	0	6,412,500
Total		$1,857,815,373	$1,859,732,569	$1,915,393,981

There are three notable changes to the property tax revenue estimate:

1. Actual tax year 2005 (fiscal 2006) statewide taxable value increased over the prior year by 4.4 percent, whereas the HJR2 revenue estimate projected a 2.5 percent increase.
2. The growth changes in tax year 2005 and new information warrant adjusting the estimated tax year 2006 (fiscal 2007) growth rates for class 8, business equipment from 2.9 percent to 4.1 percent; and class 13, telecommunication and electric generation property from -1.6 percent growth to 0 percnet, or no change in taxable value.
3. Protested property taxes (net of settled cases) are estimated to be $2.4 million higher each year of the biennium than the SB 87 estimate. Fifty percent of this amount is removed from the general fund, so this is an offset of $1.2 million a year.

Revenue Projection:

	Fiscal Year	Total Collections Millions	General Fund Collections Millions	GF Percent Change
A	1983	0.000000	0.000000	Not App.
A	1984	128.445172	128.445172	Not App.
A	1985	133.608178	133.608178	4.02%
A	1986	134.707251	134.707251	0.82%
A	1987	128.225413	128.225413	-4.81%
A	1988	111.111138	111.111138	-13.35%
A	1989	114.444609	114.444609	3.00%
A	1990	133.619694	112.374543	-1.81%
A	1991	196.551532	176.154583	56.76%
A	1992	228.220531	206.138029	17.02%
A	1993	231.757476	207.646372	0.73%
A	1994	223.577122	202.381945	-2.54%
A	1995	226.944990	205.842671	1.71%
A	1996	226.234755	204.082588	-0.86%
A	1997	231.943080	209.284365	2.55%
A	1998	224.562154	202.350380	-3.31%
A	1999	225.681256	202.774979	0.21%
A	2000	215.866432	194.196158	-4.23%
A	2001	201.103545	180.050247	-7.28%
A	2002	181.923409	169.339388	-5.95%
A	2003	183.690786	171.679862	1.38%
A	2004	180.905286	169.530994	-1.25%
A	2005	182.394383	167.270350	-1.33%
F	2006	187.902000	176.391000	5.45%
F	2007	194.733000	182.900000	3.69%



HJR2 Comparison:

Revised HJR 2 General Fund Revenue Estimates (In Millions)										
	Actual	HJR 2			LFD Recommendations			Difference		
Revenue Source	Fiscal 2005	Fiscal 2006	Fiscal 2007	Biennium	Fiscal 2006	Fiscal 2007	Biennium	Fiscal 2006	Fiscal 2007	Biennium
Property Tax	$167.270	$173.804	$180.062	$353.866	$176.391	$182.900	$359.291	$2.587	$2.838	$5.425

Common School Interest and Income

Revenue Description:

Lands granted by the federal government to the state for the benefit of public schools generate income. The common school trust is actually part of the trust and legacy trust fund that includes nine other trusts. Prior to fiscal 1996, interest and income from the common school trust was deposited in the state equalization account. Beginning in fiscal 1996, this interest and income was deposited in the general fund, as mandated by SB 83, passed by the 1995 legislature. Beginning fiscal 2003, House Bill 7 from the August 2002 special legislative session changed the deposit to the state special revenue guarantee account and statutorily appropriated the money for schools. The estimates show the amount of revenue deposited to the guarantee account and are net of amounts diverted (of mineral royalties, timber sale revenue, and income) for DNRC administration costs. Included is timber revenue for school technology and the amounts of mineral royalty revenue that is required to pay interest and principal on the SB 495 loan. These items are explained below.

Common school lands produce two kinds of revenue: 1) distributable income such as interest earnings, agricultural rents or crop shares, and timber sale revenue; and 2) permanent income that is returned to the trust such as income from the sale of minerals (see the effects of Senate Bill 495 from the 2003 legislative session below), land, and easements. Excluding the amount of timber sale revenue diverted for DNRC administration and school technology and after a 3.0 percent deduction of the revenue for use by the Department of Natural Resources and Conservation (DNRC), 95 percent of distributable revenue is available to fund schools and, due to Senate Bill 48 (discussed below), the remaining 5.0 percent is available to fund the Trust Land Management Division of DNRC. The 3.0 percent allocation to DNRC is used for resource development purposes. Timber revenue is allocated: 1) first to DNRC to fund a portion of its timber program based on the amount appropriated by the legislature (the remaining portion is funded with timber sale revenue from the capital land grant and other land trusts that generate timber revenue); 2) the amount received from production over 18 million board feet is deposited into the state special revenue fund for school technology equipment and training and is statutorily appropriated to OPI (House Bill 41 enacted by the 2001 legislature and House Bill 7 from the August 2002 special legislative session); and 3) any remainder for the support of public schools.

Senate Bill 48, passed by the 1999 legislature, provides for the diversion of the following funds for the purpose of funding the Trust Land Management Division in the DNRC: 1) mineral royalties; 2) revenues from the sale of easements; and 3) 5.0 percent of interest and income previously credited to the common school trust. The amount of the money diverted from the common school trust reduces the growth of the trust fund balance and, hence, reduces the amount of distributable interest earnings.

As of October 1, 1995, all fixed-income investments held by the state's major trust funds (which include the trust and legacy fund of which the common school trust is a part), were transferred to a newly-created Trust Fund Bond Pool (TFBP). The majority of common school trust funds are invested as part of the TFBP. Some funds, however, are invested on a short-term basis in the state's Short Term Investment Pool (STIP). The state Constitution prohibits the investment of common school trust funds in common stock. Interest income is distributed 95 percent to the guarantee account and 5 percent is available for DNRC administration with the remainder deposited to the trust.

Senate Bill 495 (enacted by the 2001 legislature) authorized DNRC to purchase the mineral production rights (with a loan from the coal severance trust) from the common school trust. The department subsequently purchased $138.9 million of future mineral royalties (over an approximate 30-year period) from the school trust for $46.4 million. Since these royalties will no longer be deposited to the trust, interest earnings from the trust corpus are lessened. However, additional interest earnings are generated from the proceeds of the sale, but it is estimated that interest losses will exceed interest gains after fiscal 2012. It is estimated that the trust balance will be $94.7 million less after the 30-year period. For further information and analysis on Senate Bill 495 contact the Legislative Fiscal Division for a copy of the two-part report: "Senate Bill 495-Implementation, Impacts and Implications".

<u>Applicable Tax Rate(s): N/A</u>

<u>Distribution:</u>

As described above, interest and income from common school lands (including a portion of timber sales and after amounts diverted for DNRC administration) are distributed 95.0 percent to the state special revenue guarantee account and is statutorily appropriated for schools. The remaining 5.0 percent is available to fund the Trust Land Management Division with the remainder deposited to the trust fund. The amounts deposited to the guarantee account are shown in this revenue source.

<u>Collection Frequency:</u>

Revenue is received monthly, however, distribution to the state special revenue fund takes place three times per year.

<u>Statutory Reference:</u>

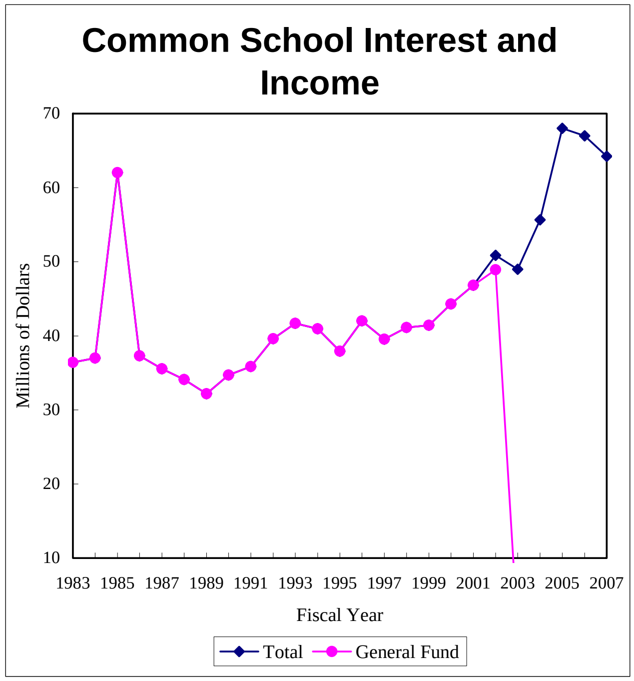
Tax Rate – NA
Distribution (MCA) – Montana Constitution Article X, Section 5; 20-9-342 (school technology); 20-9-622 (guarantee account)
Other (MCA) – DNRC trust land administration diversion (77-1-109)
DNRC timber sale program diversion (77-1-613)
DNRC land bank administration diversion (77-2-362)
DNRC resource development diversion (77-1-607)
Enabling Act, Section 10
Date Due - the last business day of February following the calendar year in which the money was received (20-9-342).

<u>Additional Information Since Adjournment:</u>

Although the committee directed staff to limit their review and potential adjustments to only income taxes, corporation income taxes, and oil and natural gas production taxes, it did request staff to calculate the associated impact on common school interest and income revenues if adjustments were adopted for oil and natural gas price and production levels.

Revenue Projection:

	Fiscal Year	Total Collections Millions	General Fund Collections Millions	GF Percent Change
A	1983	36.398297	36.398297	Not App.
A	1984	36.982835	36.982835	1.61%
A	1985	62.050661	62.050661	67.78%
A	1986	37.301053	37.301053	-39.89%
A	1987	35.529619	35.529619	-4.75%
A	1988	34.078544	34.078544	-4.08%
A	1989	32.165382	32.165382	-5.61%
A	1990	34.706901	34.706901	7.90%
A	1991	35.865505	35.865505	3.34%
A	1992	39.616168	39.616168	10.46%
A	1993	41.673746	41.673746	5.19%
A	1994	40.943551	40.943551	-1.75%
A	1995	37.904099	37.904099	-7.42%
A	1996	42.031801	42.031801	10.89%
A	1997	39.538792	39.538792	-5.93%
A	1998	41.129779	41.129779	4.02%
A	1999	41.432733	41.432733	0.74%
A	2000	44.296034	44.296034	6.91%
A	2001	46.845895	46.845895	5.76%
A	2002	50.875186	48.937673	4.47%
A	2003	48.977342	0.000000	-100.00%
A	2004	55.663022	0.000000	Not App.
A	2005	68.035764	0.000000	Not App.
F	2006	67.010000	0.000000	Not App.
F	2007	64.218000	0.000000	Not App.



HJR2 Comparison:

Revised HJR 2 Non-general Fund Revenue Estimates (In Millions)										
	Actual	HJR 2			LFD Recommendations			Difference		
Revenue Source	Fiscal 2005	Fiscal 2006	Fiscal 2007	Biennium	Fiscal 2006	Fiscal 2007	Biennium	Fiscal 2006	Fiscal 2007	Biennium
Common School I & I	$68.036	$57.146	$56.233	$113.379	$67.013	$64.225	$131.238	$9.867	$7.992	$17.859