

# MONTANA TAXPAYER



MONTANA TAXPAYERS ASSOCIATION

HELENA, MONTANA

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## Upcoming Meetings

**Thursday, December 6 – [MONTAX ANNUAL MEETING](#)**

**Thursday, December 6 and Friday, December 7 – [Revenue & Transportation Committee](#)**, 8:00am, State Capitol

**Tuesday, December 11 and Wednesday December 12 – [Legislative Finance Committee](#)**, 8:00am, State Capitol

**Wednesday, December 12 – [MAR Notice No. 42-2-790](#)**, relating to alternative energy tax credits, 10:00am

**Thursday, December 13 and Friday, December 14 –** Education and Local Government

**Thursday, December 13 – DOR Rule Hearings**

[MAR Notice No. 42-2-783](#), relating to contractors gross receipts taxes 1:00pm

[MAR Notice No. 42-2-784](#), relating to qualified endowment, 1:30pm

[MAR Notice No. 42-2-785](#), relating to new and expanded industry, 2:00pm

[MAR Notice No. 42-2-787](#), relating to the capital gain credit, 2:30pm

[MAR Notice No. 42-2-791](#), relating to movie, television and related media tax credits 3:00pm

**Friday, December 14 – DOR rule hearings**

[MAR Notice No. 42-2-788](#), relating to estimated tax, 9:00am

[MAR Notice No. 42-2-789](#), relating to individual income taxes, 10:00am

**Monday, December 17 – DOR rule hearings**

[MAR Notice No. 42-2-786](#) relating to biodiesel and biolubricant tax credits, 10:00am

[MAR Notice No. 42-2-782](#), relating to property tax incentives for new investment, development research, and technology related to renewable energy, 1:00pm

## ***Understanding Property Tax Appeals and Protests***

Recent articles in Montana newspapers regarding property tax appeals and protests from large taxpayers would lead you to believe these protested taxes are inhibiting local governments' ability to provide essential public services. In most cases, this is simply not accurate.

Local governments are allowed to increase mill levies each year to generate the same amount of money generated the year before plus half the average rate of inflation over the past three years. Excluded from this calculation is any value associated with newly taxable value. Newly taxable value includes:

- (i) annexation of real property and improvements into a taxing unit;
- (ii) construction, expansion, or remodeling of improvements;
- (iii) transfer of property into a taxing unit;
- (iv) subdivision of real property; and
- (v) transfer of property from tax-exempt to taxable status.

This means that local governments can increase spending by the amount of the newly taxable value each year. Included in the definition of (ii) new construction is the increase in value of centrally assessed properties. These properties, unlike real property, are appraised annually rather than under the current six year reappraisal process. Taxpayers in these classes can be faced with fluctuating values year to year. This is frustrating to both the taxpayer and local governments. Predictability and stability are two important components of a good revenue system.

The examples on page 3 demonstrate how protested taxes might affect a local government's budget. These examples assume one taxpayer in the county with one year of newly taxable value. The taxpayer added no new property that first year. The newly taxable value is solely attributable to the increase in the valuation of the company from the prior year due to reappraisal.

The first example assumes no inflation. The local government had revenues of \$5 million in the prior year (line 1). The department of revenue certifies a total taxable value to the county in August of \$54 million. Of that, \$4 million is newly taxable value (or once again for this taxpayer the change in the value of the property from the prior year without any additions). The local government subtracts the newly taxable from the total taxable to determine the mill levy. The mill levy is allowed to float to generate as much money as the year before. The mill levy is calculated by dividing the revenues (line 3) by the net taxable value (line 6). The local government is then allowed to apply that mill levy times the newly taxable and count that as new revenue (lines 5 X 7 / 1000 – mills expressed as 1/10 of a cent). The local government's revenues are now \$5.4 million.

# Montana Taxpayer

Address all communications to:  
MONTANA TAXPAYERS ASSOCIATION

P.O. BOX 4909, HELENA, MT 59604

Telephone (406) 442-2130

FAX (406) 442-1230

Web Site - [www.montax.org](http://www.montax.org)

E-mail - [mwhitt@montax.org](mailto:mwhitt@montax.org)

[phyatt@montax.org](mailto:phyatt@montax.org)

Business Office: 506 North Lamborn



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But, if the taxpayer protests, this money must be set aside in a protest fund.

In year two, the local government begins the budget process at \$5.4 million in revenues. They must use this amount to determine the current year's mill levy even though the money is in protest. Since no new property has been added, there is no newly taxable value and the mill levy remains at 100 mills to generate the same amount of revenue from the prior year. Once again the taxpayer protests the \$400,000 as the disputed value has carried over from the prior year.

Assume the court finds in favor of the department of revenue's value at the end of year three. In year four, the local government's revenues would now be \$5.4 million. If the taxpayer wins, the county's revenues would go back to \$5 million in year four. Either way, the mills have stayed the same assuming no growth and no inflation.

Now look at example two. Here inflation is added to show that local governments' revenues grow even if there have been protested taxes. We begin in year one, with the same \$5 million in revenues. The government can grow the revenues by 1/2 the average rate of inflation over the past three years, so they can increase their property tax revenues by an additional \$75,000 (local governments have other sources of non-levy revenue in addition to property taxes). The inflation adds additional money to the revenues of the local government with or without the protest. Line 11 shows the additional money each year that is added with the inflation factor adjustment.

Once again, in this example if the valuation of the company as determined by the department of revenue is upheld, the local government now has access to the money in the protest fund. If the taxpayer is successful, the taxable value of the county decreases back to the \$50 million that it was in the first year. But, unlike the first example, the local government has been able to increase revenues through the use of the inflation factor.

Obviously these are two simple examples and assume all other things remain equal, but they illustrate how valuation increases for annually assessed properties are treated. Complications arise since budgets are set by local governments in late August prior to taxes being filed under protest in November by taxpayers. If local governments are unaware of a potential protest in year one, they could put future budgets in jeopardy if the revenues are not ultimately collected.

But if local governments are aware there is the potential for protests, although they have to use the department's actual certified numbers, they can also set these anticipated funds aside into a line item in their budget and simply do not spend it. They could keep rolling that amount forward from year to year until the protest is finally resolved. This way, the budget can still increase from other newly taxable property, the inflation factor and other local revenues.

Over the past few years more companies have protested their taxes due to significant valuation increases from year to year. Some taxpayers have seen increases in their values of nearly 30 percent in just a few short years. If these large valuation increases continue, there needs to be better communication between the department, local governments and the affected taxpayers to minimize negative budget impacts to local governments. Although minimal communication is already occurring by letter from the department to local governments, the actual implications and potential solutions regarding the protests are not clear.

Granted, long-drawn out appeals add a level of complexity and the potential curtailing of certain new expenditures. That is why our association joined with the Montana Treasurers Association and others in supporting legislation in both the 2005 and 2007 Legislative Sessions that would have put certain sidebars on the appeal process in an attempt to speed up the appeal process. Unfortunately, none of that legislation passed.

Protested taxes have a different effect on school budgets. We will explain this effect in a subsequent newsletter.

### ***Department of Revenue Rules***

The Department of Revenue has filed numerous bills over the past few weeks. Two of the rules have already been heard and comments were due on November 26.

<b>Sample County</b>	<b>Year 1</b>	<b>Year 2</b>	<b>Year 3</b>	<b>Value Upheld Year 4</b>	<b>Taxpayer Successful Year 4</b>
<b>1 Tax Revenue Prior Year</b>	<b>\$5,000,000</b>	<b>\$5,400,000</b>	<b>\$5,400,000</b>	<b>\$5,400,000</b>	<b>\$5,000,000</b>
2 No inflation					
3 Allowable Revenue Current Year	\$5,000,000	\$5,400,000	\$5,400,000	\$5,400,000	\$5,000,000
4 Total Taxable Value Current Year (as certified to the county by DOR)	\$54,000,000	\$54,000,000	\$54,000,000	\$54,000,000	\$50,000,000
5 Total taxable Value of Newly Taxable (as certified to the county by DOR)	\$4,000,000	\$0	\$0	\$0	\$0
6 Net Taxable Value (4 - 5)	\$50,000,000	\$54,000,000	\$54,000,000	\$54,000,000	\$50,000,000
7 Allowable Mill Levy – floating mill – (3 / 6)	100.000	100.000	100.000	100.000	100.000
8 Additional Revenues from Newly Taxable (5 x 7)	\$400,000	\$0	\$0	\$0	
<b>9 Total Tax Revenue Current Year (8 + 3)</b>	<b>\$5,400,000</b>	<b>\$5,400,000</b>	<b>\$5,400,000</b>	<b>\$5,400,000</b>	<b>\$5,000,000</b>
10 Assume 100 percent of newly taxable protested	\$400,000	\$400,000	\$400,000	\$0	\$0
<b>11 Total revenues available to the county for current year after protest (9 - 10)</b>	<b>\$5,000,000</b>	<b>\$5,000,000</b>	<b>\$5,000,000</b>	<b>\$5,400,000</b>	<b>\$5,000,000</b>
<b>Sample County</b>	<b>Year 1</b>	<b>Year 2</b>	<b>Year 3</b>	<b>Value Upheld Year 4</b>	<b>Taxpayer Successful Year 4</b>
<b>1 Tax Revenue Prior Year</b>	<b>\$5,000,000</b>	<b>\$5,481,000</b>	<b>\$5,563,215</b>	<b>\$5,646,663</b>	<b>\$5,306,818</b>
2 ½ Average Rate of Inflation past 3 years	1.50%	1.50%	1.50%	1.50%	1.50%
3 Allowable Revenue Current Year	\$5,075,000	\$5,563,215	\$5,646,663	\$5,731,363	\$5,386,420
4 Total Taxable Value Current Year (as certified to the county by DOR)	\$54,000,000	\$54,000,000	\$54,000,000	\$54,000,000	\$50,000,000
5 Total Taxable Value of Newly Taxable (as certified to the county by DOR)	\$4,000,000	\$0	\$0	\$0	\$0
6 Net Taxable Value (4 - 5)	\$50,000,000	\$54,000,000	\$54,000,000	\$54,000,000	\$50,000,000
7 Allowable Mill Levy – floating mill – (3 / 6)	101.500	103.023	104.568	106.136	107.728
8 Additional Revenues from Newly Taxable (5 x 7)	\$406,000	\$0	\$0	\$0	\$0
<b>9 Total Tax Revenue Current Year (8 + 3)</b>	<b>\$5,481,000</b>	<b>\$5,563,215</b>	<b>\$5,646,663</b>	<b>\$5,731,363</b>	<b>\$5,383,420</b>
10 Assume 100 percent of newly taxable protested	\$406,000	\$412,090	\$418,271	\$0	\$0
<b>11 Total revenues available to the county for current year after protest (9-10)</b>	<b>\$5,075,000</b>	<b>\$5,151,125</b>	<b>\$5,228,392</b>	<b>\$5,731,363</b>	<b>\$5,386,420</b>

**MAR Notice No. 42-2-779**, amendment of rules relating to telecommunications license and telecommunication excise tax as found in Chapter 31, Title 42, Administrative Rules of Montana. The department proposed an amendment to the rule changing the date to clarify that if the 113<sup>th</sup> Congress (rather than the 110<sup>th</sup> Congress) adjourns without reauthorizing the internet moratorium then it is considered “lifted.”

The Montana Taxpayers Association submitted comments that the rule was not necessary since the moratorium was extended seven years. We also contended Montana statute does not confer upon the

Department the ability to impose new taxes administratively on the internet. Such an action would only be possible if the Legislature grants such authority by passing legislation sometime in the future.

**MAR Notice No. 42-2-778**, adoption of new rules and amendment of rules relating to Mineral Royalty Backup Withholding as found in Chapter 17, Title 42, Administrative Rules of Montana. Comments were submitted by the Montana Society of CPAs and a private CPA to address two concerns:

- The requirement to attach the Federal K-1 to S-Corp, Partnership, Trust, and Estate returns will

cause any return claiming these credits to not be able to E-File. There will be no method available for prepares to send this information and for the DOR to “capture” the information. Similar problems will be with the requirement to attach the 1099-MISC to the return.

- Partnerships, trusts, estates, and S-corps should be exempt if all the proper paper work has been filed by all the partners agreeing to be taxed by Montana. If you have compliance in filing tax returns reporting this information, then you could ease the burden on trying to track this withheld tax. You already have the system in place for all out of state taxpayers that have not signed an agreement to have withholding for State income tax. I think that we need to make sure we do not place unfair burdens on the taxpayers that are complying to try to catch the small percentage that are not.

Similarly, how will withholding be handled with pass-through entities?

For example, if a Limited Liability Company has royalty income of \$25,000.00, the withholding on this would be \$1,500.00. Let's assume that there are 5 members. The 1099 would go to the LLC showing the royalty and the withholding. How do we get that withholding information to the members of the LLC?

Other upcoming rules are listed at the beginning of the newsletter. Please contact [mwhitt@montax.org](mailto:mwhitt@montax.org) or (406)442-2130 if you have any comments.

## **Revenue and Transportation Committee**

*(taken from The Interim newsletter)*

[http://www.leg.mt.gov/content/publications/interim\\_newsletter/Interim\\_07NOV.pdf](http://www.leg.mt.gov/content/publications/interim_newsletter/Interim_07NOV.pdf)

Committee meets in conjunction with Montana Taxpayers Association annual meeting ... The Revenue and Transportation Committee is meeting Dec. 6 and 7 in Helena. The committee is studying the conformity of state individual and corporation income tax laws with federal tax laws (HJR61). On Dec. 6, Harley Duncan, executive director of the Federation of Tax Administrators, will discuss the implications of state conformity with federal law. Tax practitioners and the Department of Revenue will also provide their insights.

Larry Swanson, director of the Center for the Rocky Mountain West, will discuss demographic trends in Montana. The committee wants to have an understanding of these trends as part of its SJR 31 study of school funding and property taxes. The discussion may also have pertinence for the HB 488 property reappraisal study.

The committee will recess before noon on Thursday to attend the Montana Taxpayers Association annual meeting.

Other Agenda topics...The committee will reconvene Friday morning, Dec. 7. Although the agenda has not been set for Friday, the committee will consider a number of topics. Lee Heiman, staff attorney, will discuss a legal memo regarding the “trigger” language in House Bill 9 that provides an income tax credit for a portion of state school equalization property taxes paid by residential property owners. There is a dispute on whether the trigger has been met. The committee will also review background information on the SJR 31 study. The Department of Revenue will provide an update on the development of rules for tax increment finance districts and the Department of Transportation will report on the highway revenue account.