FISCAL NOTE

Bill #:	HB617	**Title:**	Simplify and reduce Montana income taxes
Primary Sponsor:	Joe Balyeat	**Status:**	House 3rd Reading

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Sponsor signature Date Chuck Swysgood, Budget Director Date

Fiscal Summary

	FY2002 Difference	**FY2003 Difference**
Expenditures:		
General Fund	$0	$89,697
Net Impact on General Fund Balance:	**$0**	**$(89,697)**

Yes	**No**		**Yes**	**No**	
	X	Significant Local Gov. Impact		X	Technical Concerns
	X	Included in the Executive Budget	X		Significant Long-Term Impacts
	X	Dedicated Revenue Form Attached		X	Family Impact Form Attached

Fiscal Analysis

ASSUMPTIONS:

1. This bill is effective January 1, 2002 and applies to tax years beginning after December 31, 2002 (TY2003). There is no revenue impact from this proposal in fiscal year 2002 or fiscal year 2003.
2. The Department of Revenue shall not revise withholding tax tables in anticipation of this bill meeting the contingency language in the bill.
3. There would be additional administrative operating expenses totaling $89,697 in fiscal 2003 to provide for programming and tax form changes.

FISCAL IMPACT:	FY2002 Difference	FY2003 Difference
Expenditures:		
Personal Services	$0	$17,064
Operating Expenses	$0	$66,788
Equipment	$0	$5,845
TOTAL	$0	$89,697

Funding:		
General Fund (01)	$0	$89,697
Revenues:		
General Fund (01)	$0	$0
Net Impact to Fund Balance (Revenue minus Expenditure):		
General Fund (01)	$0	($89,697)

LONG-RANGE IMPACTS:
This bill becomes effective only if contingency language in the bill is satisfied. Contingency language provides that this act is effective January 1, 2002 *"only if the unreserved fund balance for the general fund as of June 30, 2001, as reported in accordance with generally accepted accounting principles and as published in the audited state financial statements as of June 30, 2001, exceeds the amount of $82.5 million by at least $10 million."* In the event this contingency occurs, the following impacts would occur:

Beginning with tax year 2003, this bill provides for a new, alternative method of determining individual income tax liability. Once a taxpayer elects to file using the alternative, the election is irrevocable for all subsequent tax years. The central elements of the alternative approach are that the taxpayer would no longer be able to deduct federal income taxes paid during the tax year, but would be allowed to use an alternative tax rate table with top marginal rates below those in the current law rate table.

Income Exclusions and Tax Credits – Alternative Method
In addition to the deduction for federal income taxes, the following current law exclusions or deductions of income also would not be allowed for those taxpayers *choosing* to use the alternative method of calculating their tax:
1) unemployment compensation;
2) elderly interest exclusion;
3) contributions to a medical savings account;
4) contributions to a first-time homebuyer's account;
5) contributions to a family education savings account;
6) certain retirement disability benefits provided for at 15-30-111(6);
7) the deduction for expenditures for recycled materials provided for under 15-32-601; and
8) the deduction associated with land sales to a beginning farmer under 80-12-211.

Further, taxpayers choosing to use the alternative method of calculating their tax would not be eligible for the following current law tax credits:
1) elderly care credit;
2) employer's disability insurance credit;
3) investment credit (carryover);
4) alternative fuels credit;
5) employer dependent care assistance credit;
6) rural physician credit;
7) geothermal energy credit;
8) wind energy credit;
9) recycling credit;
10) infrastructure user's fee credit; and

11) Montana capital company credit.

These credits are forecast to total $833,000 for all taxpayers in fiscal year 2003. The amount of credit not taken by just those taxpayers who would opt to file using the alternative method provided for in this bill would be significantly less than this amount.

Alternative Tax Rate Table

The alternative tax rate table that is provided for in this bill was designed to provide for an across-the-board reduction in tax liability of 5%, after eliminating the deduction for federal income taxes and the other exclusions and deductions of income listed above. This resulted in a tax rate table with a top marginal tax rate of 7.7% beginning with tax year 2003.

Transitional Income Item

The fiscal impacts show here assume that for tax year 2003 taxpayers would be required to continue to include in income any refund of federal income taxes that was used to reduce Montana income tax liability in a prior year.

Taxpayer Choice

The fiscal impacts shown here also assume that taxpayers will have perfect knowledge of their tax liability under both methods of calculating their tax that would be available to them, and will choose that method that results in a smaller liability, regardless of how different the two liabilities are.

Fiscal Impact

A simulation program was developed to provide the impact of the provisions of this bill using the population of tax year 1999 individual income tax returns. That analysis, based on the assumptions discussed above, shows that tax year 2003 liability would be reduced by $35.838 million for full-year residents; there would be a corresponding reduction in revenue to the state general fund in fiscal year 2004. In tax year 2004, liabilities would be reduced by approximately $42.379 million; with a corresponding reduction in revenue to the state general fund in fiscal 2005.

Future Tax Years

A further feature of this bill includes a trigger mechanism which provides for an additional 3% reduction in the tax rates used in the alternative tax rate table beginning as soon as tax year 2007 if growth in Montana wage and salary income is at least 8.8% greater than the third year immediately preceding the last full year for which data is available. It is estimated that if this were to take effect in tax year 2007, tax liabilities would be reduced by $51 million for that tax year.