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MACo TAX, FINANCE AND BUDGET COMMITTEE

BRIEFING PAPER

RETAIL SALES TAX IN MONTANA AND RELATED PROPERTY TAX RELIEF MEASURES

(Revised February 21, 2005)

The Montana Association of Counties, having continued the study of Montana taxation, submits the following considerations and recommendations for tax reform for all Montanans. We make these recommendations and feel strongly that we must achieve significant reform in this regard in order to attain long-term economic stability. We would point out that we do not believe that the voters in 1993 foreclosed on the debate into the foreseeable future. Instead, we believe the voters simply said no to a proposal that did not meet their basic requirements for overall reform.

Based upon surveys conducted dating all the way back to 1993 and reconfirmed in focus groups and other polling efforts since, we are convinced that the voters will accept tax reform involving a general sales tax, if the following four points are taken into account. In addition, we think the social climate has changed significantly and as a result a legislative initiative would be acceptable. We further believe that the essential elements of any legislation must take into account the following:

- The proposal must be revenue neutral or better in terms of the aggregate tax bill for Montanans. It is reasonably estimated that eight to twelve percent of the sales tax revenues will come from tourists and can be considered as new revenue while achieving a neutral impact or better on Montana residents.

- The proposal must provide significant funding for education. This can be achieved by eliminating many of the current school and higher education levies and at the same time providing state funding to eighty percent of the base for school districts.

- The proposal must result in a significant reduction in property taxes.

- There must be mechanisms in place to insure that taxes do not simply creep back to the previous levels. This is achieved when one recognizes that Montanans have already constitutionally capped the sales tax at four percent. They, the voters, also need the assurance that property taxes, once eliminated by any proposal, could not be reinstated without a vote of the people. Remaining property taxes would be capped within an allowable growth mechanism as provided under current law.

- Any sales tax must be based on the principle of being very broad and general in application to all sales of goods and services. The exemptions would be limited primarily to non-prepared food, health services and prescription drugs. Such a broad based approach to a tax on goods and services takes out the traditional regressivity when only goods are taxed and taxing services results in progressivity when measured in terms of the impact on individuals in various income levels.

Any tax reform proposal should take into account the need to address the additional elements:

• preserving the income tax restructuring either within the existing brackets or possibly with a flat tax.

• the capital gains tax should be restructured.

• there should be a reduction or elimination of education funding from property taxes: specific to the 6 mill university levy, the 95 mill levied for education, the school retirement levies, the school transportation levies, and local levies below the base state funding at 80%.

• there should be a low income tax credit to offset the regressive effects of a sales tax on the low income end of the spectrum.

• there should be significant reduction in residential property taxes achieved through a homestead exemption in combination with the consideration of changing the classification ratio to 3%.

• there should be a like reduction in commercial property taxes through a comstead exemption and the reduction in the ratio.

• the business equipment taxes should be considered for possible elimination or the repeal of the trigger mechanism currently set forth in law.

• consideration of an increase in electrical energy generation taxes.

• overall simplification of the property tax system by establishing true market values on all property with consideration for a uniform classification ratio for all property.

• federal tax deductibility should be analyzed to determine the impact if the deductibility was eliminated for state tax purposes

• the issue needs to be evaluated related to the property tax reductions proposed for elimination versus retaining the tax and collecting it and rebating resident tax payers who have paid the tax.

OTHER ISSUES:

• The true elasticity of sales tax revenue can be demonstrated by looking at revenue projections associated with prior tax reform efforts.

In a study conducted in 1983, it was estimated that a 1% sales tax would generate $46,500,000.

A 1984 Tax Relief Proposal estimated revenues per 1% at $46,600,000.

The fiscal note on the proposal as introduced in 1985 estimated revenues at $45,900,000.

In 1993, the revenue estimate at 1% was $75,000,000.

In 1997, the revenue estimate at 1% was $100,000,000.

In 1999, the revenue estimate at 1% was $125,000,000.

In 2003, the revenue estimate at 1% is $146,000,000.

• Montana per capita income has increased significantly since 1984 and, as a result, taxes as a percentage of personal income have dropped considerably.

In 1984 the US average per capita income was $13,867 and Montana was raked 40th at $10,546. By 1994 the US average per capita income had grown to $21,698 and Montana was raked in comparison at 42% at $17,825. The latest figures for Montana have per capita income for 2001 at $23,963 and we are ranked at 47th. US figures are not available.

• Montana property tax values and taxes levied have changed significantly over the course of the past 27 years as illustrated below.

YEAR	TAXABLE VALUE	PROPERTY TAXES LEVIED
1975	$1,350,774,330	$266,742,900
1985	$2,370,133,344	$572,086,939
1988	$1,942,949,796	$526,706,810
1990	$1,573,360,769	$542,138,875
1995	$1,838,336,965	$739,361,193
2002	$1,718,653,223	$826,860,634
2003	$1,733,674,415	$882,713,901
2004	$1,779,939,986	$915,700,040

In conclusion, all of the economic indicators point to the problems within the current system and cry out for resolution. In order to reach the goal of a fair, equitable and balanced tax system the Montana Association of Counties will support and will endeavor to facilitate such legislation during the 2005 legislative session.