Montana Department of Revenue

Dan Bucks
Director

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Governor

SENATE TAXATION
EXHIBIT NO. 3
DATE 2-2-05
BILL NO. NA

DATE: February 2, 2005

TO: Senator Jim Elliott, Chairman
Senate Taxation Committee

FROM: Larry Finch, Administrator
Tax Policy and Research

SUBJECT: Requests for Information

During the January 26, 2005 hearing on Senate Bill 48 members of the Senate Taxation Committee requested the following items of information:

Business Equipment Exemptions in Other States

Senator Essmann had requested information on business equipment exemptions being used in neighboring states for property tax purposes. We have contacted our neighboring states, and have found the following:

- Colorado – exempts first $2,500 of market value from taxation
- Arizona – exempts first $50,000 of market value, adjusted for inflation (current exemption is $57,000)
- Washington – exempts first $3,000 of market value for sole proprietorships run by heads of families who have dependents living with them
- Wyoming – no general exemption
- Idaho – no general exemption

Impact of Class 8 Tax Reduction on Corporation License Tax – Taxpayer Example

Senator Gillan requested that the Department provide an example of the impact of reducing Class 8 business equipment taxes on a corporation's income tax. This impact is shown on the first attachment to this memo labeled "Impact of Eliminating Business Equipment Taxes on Corporation XYZ Income Tax".

The attached example assumes the business has $2 million of taxable value in Class 8 business equipment. Under current law, property taxes on this equipment, at the statewide average mill levy applied to Class 8 property of 512 mills, total $1,024,000. The example shows the impact on Corporation XYZ if business equipment were to become completely exempt from property taxation.

As the attachment shows, for a profitable corporation (a corporation with positive net taxable income for both federal and state tax purposes) deductions decrease and taxable income increases by the amount of the change in property tax, or by $1,024,000. At the federal level, corporation income taxes increase by $348,160 (the federal marginal tax rate of 34% times the reduction in business equipment taxes); at the state level income taxes increase by $69,120 (the state marginal tax rate of 6.75% times the reduction in business equipment taxes). The combined federal/state increase in corporation income taxes is $417,280. This is about 41% of the property tax reduction.

Corporations that are not profitable would also have a reduced deduction for property taxes paid. This would act to decrease the amount of net operating loss that could be carried forward or backward for these corporations.

Change in Market Value of Business Equipment – TY1990 to TY2004

Representative Gillan also asked if we could provide how the total market value of Class 8 business equipment has changed over time. The last four attachments illustrate this change.

The first of these attachments shows the change in total market value of Class 8 business equipment from tax year 1990 through tax year 2004. The total market value is further disaggregated into sub-classes of property including ag implements, furniture and fixtures, mining and manufacturing machinery, etc.

In order to provide an "apples-to-apples" comparison over time, these figures are adjusted to remove items that are no longer in Class 8, such as motor vehicles which are no longer subject to property taxes.

Also shown on the left hand side of this chart is the taxable valuation rate applied to Class 8 business equipment over the period 1990-2004.

The second attachment is a chart of the growth in Class 8 market value over time. The chart shows how total market value has grown, and also how just the mining and manufacturing machinery component has grown, over the period 1990 to 2004.

These two categories are also shown with and without the impact of the AsiMi plant in Butte-Silver Bow County. Because the AsiMi plant contributes such a significant portion of total Class 8 equipment, growth with and without the plant is shown to provide a look

at growth, in general, across the state. Class 8 business equipment for the AsiMi plant first shows up in TY1998, two years before the Class 8 tax rate dropped from 6% to 3%.

The third attachment of this series shows the rate of growth in each year, with and without the AsiMi plant. Excluding AsiMi, from 1990 to 1995 the average growth rate was about 4.9%; from 1996 through 1999 the growth rate was about 3.1%; and for the period 2000 through 2004 the growth rate has averaged about 2.2%, notwithstanding the fact that during this period the federal government provided businesses with a 30% bonus depreciation for purchases of business equipment.

The fourth attachment of this series shows the actual dollar amount of market value added each year since 1990, with and without the AsiMi plant. Notable is the large addition to market value in 1998 because of the AsiMi plant coming on line. In 1998, AsiMi added $277 million in market value. Since that time, the AsiMi plant has accounted for 9 - 10% of total market value of all Class 8 business equipment.

In tax year 2004, the AsiMi Corporation appealed the valuation of their business equipment and subsequently received a greatly reduced market value for tax purposes for that year. That decision is largely responsible for the negative growth rate in tax year 2004 for *all* business equipment; but when AsiMi is excluded the chart shows a positive growth rate for all other business equipment.

Attachment 1

Impact of Eliminatinag Business Equipment Taxes on Corporation XYZ Income Tax

Montana Business Equipment Taxes	
Taxable Value of Business Equipment @ 3% Rate:	$ 2,000,000
Statewide Average Mill Levy Applied to Class 8 Property:	512
Change in Taxes (Business Equipment Fully Exempt):	**$ (1,024,000)**

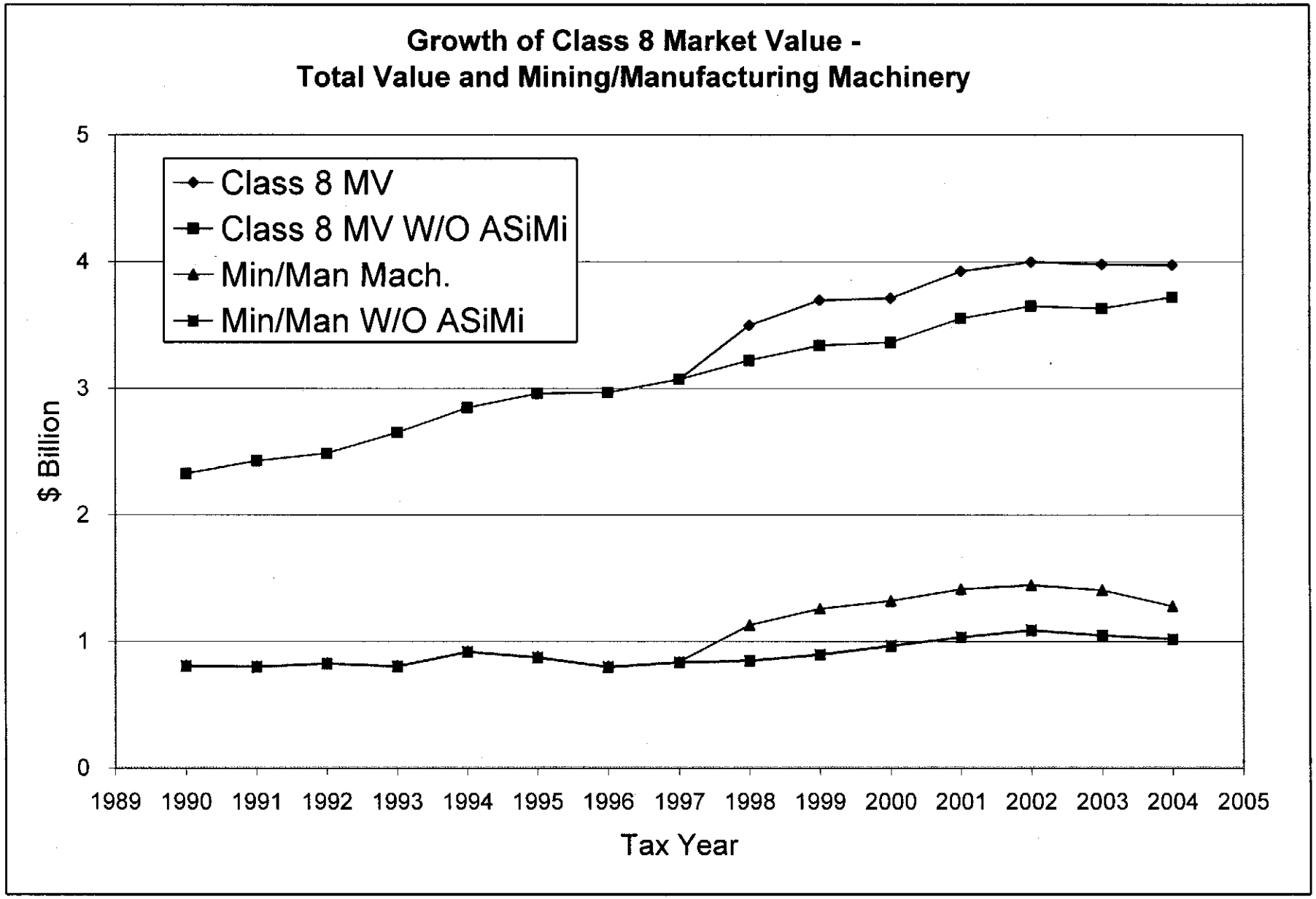
Federal Corporation Income Tax	CL	PL	Diff
Total Income	$ 23,000,000	$ 23,000,000	$ -
Deductions:			
- Taxes and licenses	3,689,000	2,665,000	(1,024,000)
- Other Deductions	17,125,000	17,125,000	0
Total Deductions	20,814,000	19,790,000	(1,024,000)
Taxable Income	2,186,000	3,210,000	1,024,000
Tax Liability	$ 743,240	$ 1,091,400	**$ 348,160**

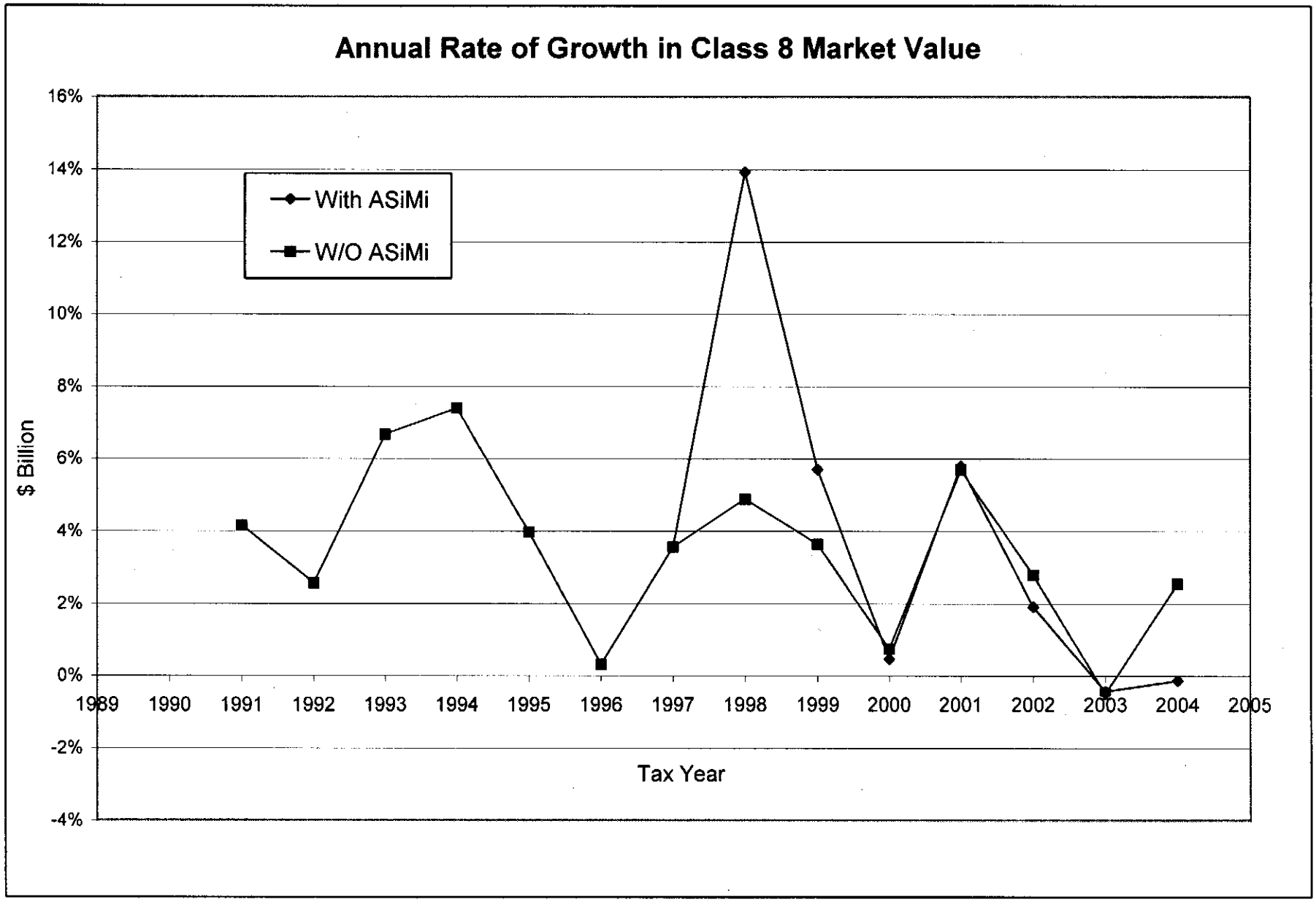
State Corporation Income Tax	CL	PL	Diff
Taxable Income	$ 2,186,000	$ 3,210,000	$ 1,024,000
Tax Liability	$ 147,555	$ 216,675	**$ 69,120**

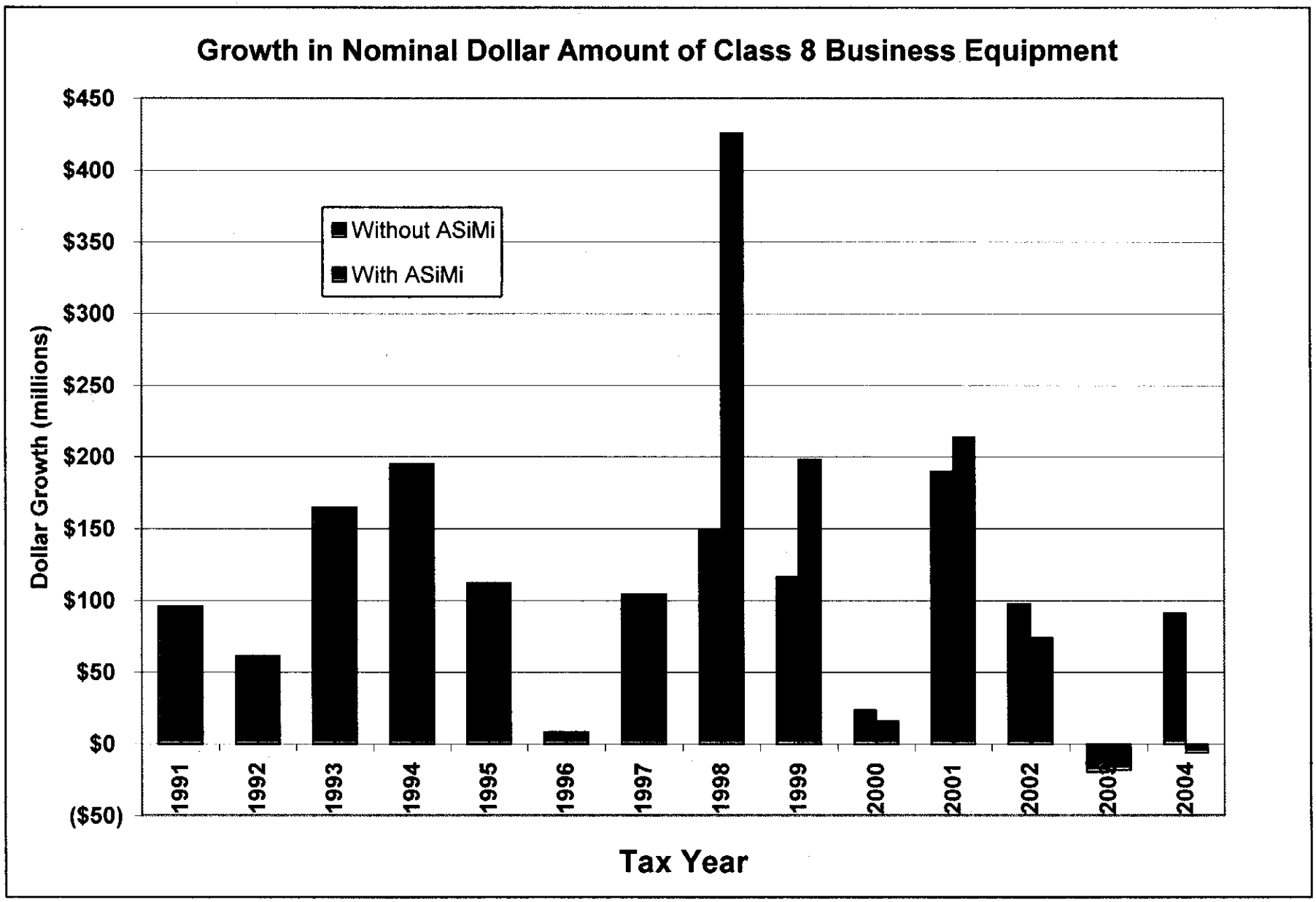
Combined Change in Federal and State Corp Tax:	**$ 417,280**
Combined Change as a Share of Property Tax Reduction:	**41%**

Market Value of Class 8 Property, Total and By Property Type - Tax Year 1990 to 2004

Tax Year	Tax Rate	Agricultural Implements	Furniture & Fixtures	Mach. Other Than Farm, Min., Manuf.	Mining and Manufacturing Machinery	Supplies & Materials	Oil & Gas Equip / Flow Lines	New/Expan Mach. & Equip	All Other	Total For Tax Year	Total For Tax Year Without ASiMi
1990	9%	547,063,533	343,925,346	302,105,314	801,895,385	70,603,693	138,344,678	36,219,151	81,006,837	2,321,163,937	2,321,163,937
1991	9%	613,903,892	353,613,309	291,740,085	795,099,828	74,123,603	126,110,410	85,371,864	77,278,479	2,417,241,470	2,417,241,470
1992	9%	605,193,680	382,292,519	297,777,091	821,260,569	72,935,786	119,231,796	99,918,326	80,140,366	2,478,750,133	2,478,750,133
1993	9%	617,475,692	400,870,920	326,624,322	799,122,856	71,005,130	114,511,402	231,908,744	82,082,982	2,643,602,048	2,643,602,048
1994	9%	655,567,666	425,007,891	337,403,307	913,741,437	76,097,135	103,264,015	239,141,096	88,311,619	2,838,534,166	2,838,534,166
1995	9%	708,047,500	483,644,909	367,155,884	869,396,419	78,704,720	97,078,659	261,626,471	85,081,934	2,950,736,496	2,950,736,496
1996	8%	661,774,062	523,251,730	416,113,330	793,789,591	80,619,531	94,807,402	298,656,228	90,251,639	2,959,263,513	2,959,263,513
1997	7%	694,732,957	557,566,043	444,754,229	831,067,314	86,152,529	95,581,643	262,693,522	91,445,414	3,063,993,650	3,063,993,650
1998	6%	730,296,341	595,805,177	477,248,266	1,120,236,845	87,665,682	93,198,164	280,180,338	105,290,389	3,489,921,202	3,212,984,934
1999	6%	726,378,605	651,633,271	491,676,922	1,250,313,093	90,431,923	106,224,811	253,279,588	118,245,292	3,688,183,505	3,329,198,303
2000	3%	710,360,955	645,292,011	508,999,349	1,312,371,362	98,354,633	120,055,802	222,539,898	86,491,833	3,704,465,843	3,352,937,162
2001	3%	700,489,758	746,256,257	556,320,560	1,404,617,294	100,521,550	106,530,378	207,254,544	96,419,151	3,918,409,492	3,543,059,829
2002	3%	715,689,923	805,981,667	558,171,154	1,435,625,233	101,759,004	106,661,541	166,913,955	101,499,286	3,992,301,763	3,640,828,004
2003	3%	714,662,211	812,548,049	578,058,366	1,397,876,298	107,700,871	111,949,807	141,759,270	109,928,324	3,974,483,196	3,621,706,574
2004	3%	732,918,037	821,617,098	593,456,992	1,270,695,629	109,749,916	125,189,888	187,599,207	127,201,379	3,968,428,146	3,712,914,295


Growth of Class 8 Market Value -
Total Value and Mining/Manufacturing Machinery
Class 8 MV
Class 8 MV W/O ASiMi
Min/Man Mach.
Min/Man W/O ASiMi
$ Billion
0
1
2
3
4
5
1989
1990
1991
1992
1993
1994
1995
1996
1997
1998
1999
2000
2001
2002
2003
2004
2005
Tax Year


Annual Rate of Growth in Class 8 Market Value
16%
14%
12%
10%
8%
6%
4%
2%
0%
-2%
-4%
$ Billion
With ASiMi
W/O ASiMi
1989
1990
1991
1992
1993
1994
1995
1996
1997
1998
1999
2000
2001
2002
2003
2004
2005
Tax Year


Growth in Nominal Dollar Amount of Class 8 Business Equipment
Without ASiMi
With ASiMi
Dollar Growth (millions)
$450
$400
$350
$300
$250
$200
$150
$100
$50
$0
($50)
1991
1992
1993
1994
1995
1996
1997
1998
1999
2000
2001
2002
2003
2004
Tax Year