How Montana Law Taxes Nonresidents on Deferred Gains on Property Sales

Montana's law taxes nonresidents the same as residents with respect to gains on the sale of Montana property, including for expired gains deferred under Internal Revenue Code Section 1031. The basic law and policy on this subject starts with Section 15-30-105 (1)(a), MCA:

> **Tax on nonresident:** A tax is imposed upon each nonresident equal to the tax computed under 15-30-103 as if the nonresident were a resident during the entire tax year, multiplied by the ratio of Montana source income to total income from all sources.

This law provides that residents and nonresidents are treated equally with respect to income earned in Montana. The tax is calculated in the steps below:

Nonresident Tax Calculation of Tax on Gains on the Sale of Montana Property	Legal Citations
Step 1. The nonresident taxpayer calculates his/her taxable income as if they were full-year resident. All gains on the sale of property anywhere that the taxpayer has recognized for federal tax purposes are included in taxable income in this step—including deferred gains for which the deferral has expired. So at this step, gains for which the deferral has expired is specifically included in taxable income. This occurs because Montana adjusted gross income is explicitly tied to federal adjusted gross income for residents and nonresidents.	Section 1031, Internal Revenue Code Sections 15-30-111, 15-30-112, 15-30-116, 15-30-117, 15-30-121, 15-30-122, 15-30-123, and 15-30-131 Montana Code Annotated. There is no deduction, exemption or exclusion for capital gains for state tax purposes on the sale of property for tax years 2002 forward in Montana or federal law.
Step 2. The nonresident taxpayer applies the Montana income tax rate structure to determine the level of tax equal to that of residents. This calculation also includes subtracting the 1% credit for capital gains, calculated as a percentage of gains recognized from all sources.	Sections 15-30-103, 15-30-105, and 15-30-183, Montana Code Annotated.
Step 3. The nonresident taxpayer multiplies the tax amount calculated in Step 2 by the ratio between the taxpayers Montana source income to total income from all sources. Montana source income specifically includes gains on the sale of property located in Montana. Because Montana law is tied to federal law, the Montana source income includes the deferred gains for which the deferral has expired.	Sections 15-30-101(18), 15-30-105, and 15-30-111, Montana Code Annotated. As before, there is no deduction, exemption or exclusion for capital gains for Montana state tax purposes on the sale of property for tax years 2002 forward in Montana or federal law.

Revenue & Transportation Committee Meeting
February 16 & 17, 2006

Exhibit #24