TEAMSTERS UNION LOCAL NO. 190

Affiliated with the International Brotherhood of Teamsters

P.O. Box 50969
437 Kuhlman Drive
Billings, Montana 59105

www.teamsters190.com
teamsters190@teamsters190.com

Telephone 406.248.2658
Fax 406.248.1503

Joe Dwyer
Secretary-Treasurer
Business
Representative

PUBLIC COMMENT ON DEPARTMENT OF REVENUE PROPOSED RULE AMENDMENT RELATING TO MONTANA SOURCE INCOME
February 16, 2006

DON JUDGE – TEAMSTERS LOCAL UNION 190

Chairman Elliot, members of the Revenue and Transportation Interim Committee, for the record, my name is Don Judge and I'm speaking here today on behalf of Teamsters Local 190 in support of the Department of Revenue's proposed amendment to ARM 42.2.304 regarding clarification of information related to Montana Source Income.

On behalf of the 1,700 working families throughout Eastern Montana represented by Teamsters Local 190, we urge this committee to recognize the value and importance of providing clarification to individuals engaged in Section 1031 Exchanges. There are a number of reasons we believe this to be important to our members and to the Montana taxpaying public at large.

First, it is clear to us that both residents and non-residents of the state are subject to taxation on gains resulting from sale of property at the time those gains are recognized and realized.

Section 15-30-131 [MCA] establishes: "**Nonresident and temporary resident taxpayers – adjusted gross income**. In the case of a taxpayer other than a resident of this state, adjusted gross income includes the <u>entire amount of adjusted gross income as provided for in 15-30-111</u> [MCA]. (Emphasis added)

Section 15-03-111 [MCA] provides that: "**Adjusted gross income.** (1) Adjusted gross income is the taxpayer's federal adjusted gross income as defined in section 62 of the Internal Revenue Code, 26 U.S.C. 62, and in addition includes the following:" [*An enumeration of additional revenue sources follows.*]

Section 15-30-105 [MCA] adopted by the 2001 legislature and effective in 2002 establishes equal treatment of non-residents and residents alike with: "**Tax on nonresident.** (1) (a) A tax is imposed upon each nonresident equal to the tax computed under <u>15-30-103</u> as if the resident were a resident during the entire tax year, <u>multiplied by the ratio of Montana source income</u> to total income from all sources." (Emphases added)

Section 15-30-101 [MCA] **Definitions.** Subsection (18) (a) "Montana source income" "means:

(i) wages, salary, tips, and other compensation for services performed in the state or while a resident of the state;

(ii) gain attributable to the sale or transfer of tangible property located in the state, sold or otherwise transferred while a resident of

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Exhibit #32

a trade, business or occupation carried on in the state; [*An enumeration of additional subsections defining Montana source income follows.*]

It is clear to us that Montana law, by statute, definition and linkage to Federal Income Tax Codes, establishes that both residents and non-residents alike will be subject to the same requirements regarding payment of taxes on Montana source income. The question then, should not be **if** non-residents are required to be treated equally as residents when it comes to Montana source income, but rather **will** the state of Montana do its best to educate both residents and non-residents as to their potential for tax liabilities under Section 1031 Exchanges.

We believe that the Montana Department of Revenue is attempting to do just that through its amendments to ARM 42.2.304. In our review of the notes prepared by the DOR following the December 29, 2005 Rules Hearing and subsequent written comments, it is clear that what the department is doing is attempting to educate non-resident taxpayers who have availed themselves of Section 1031 Exchange tax deferral provisions that they will become subject to income taxation on any gain realized on the sale or transfer of tangible property located in Montana at such time as that gain is recognized by the Federal Government for income tax purposes.

It is our belief that by educating taxpayers, real estate dealers, tax advisors and others involved with Section 1031 Exchanges, the department is attempting to avoid unnecessary administrative costs associated with chasing down perspective tax payers, and also avoiding costly interest and penalties due by these individuals as a result of tax avoidance. We would hope that this would make sense to any law-abiding citizens who want to make our system as manageable and easy to understand as possible.

Clearly, the working-family members of Teamsters Local 190, their parents, siblings, children and grand-children also have a deep interest in making sure that all individuals who derive income from a Montana source pay their fair share of Montana taxes.

Montana's history of tax revision is replete with a shifting of the property tax burden away from major corporations to homeowners and small business owners. This shift has occurred primarily in the form of tax rate reductions and exemptions for business equipment taxes and centrally assessed properties. In one instance the tax on business inventory was repealed entirely. As a result of these tax revisions homeowners and small business owners have seen their local property taxes rise dramatically to cover the rising costs of public education and local government services. And now, these same taxpayers are seeing more of their income-tax dollars being diverted directly to pay for the costs of public education in our state.

Our members generally don't begrudge paying taxes to support our essential public services and education, (although I couldn't say with any certainty that they are elated about paying taxes) but they darn sure get angry when they learn that there are individuals out there who are not paying their fair share. When this happens, honest, law-abiding taxpayers are forced to pick up the slack through higher income or property taxes or face a reduction in the extent or quality of pubic services. Some who actually work in the public service sector stand the risk of unemployment because of such tax cheats.

We observed in the notes compiled by the DOR on the December 29, 2005 hearing that there were some opponents to the proposed rules amendment who advocated that the department take a futuristic approach to enforcement of the Montana source income – using a "starting next year" we'll begin to collect the tax scheme. We would respectfully disagree with this approach.

ARTICLE XIII, Section 1. (2) of the Montana Constitution provides that: "The legislature <u>shall provide protection and education for the people against harmful and unfair practices by either foreign or domestic corporations, individuals, or associations.</u>" (Emphasis added)

And, ARTICLE VI, Section 4. (1) of the Montana Constitution provides that: "The executive power is vested in the governor <u>who shall see that the laws are faithfully executed.</u> He shall have such other duties as are provided in this constitution and by law." (Emphasis added)

To us, it is clear that to provide any ex post facto grant of such a special privilege would be to ignore both of these provisions of our constitution and, along with the equal protection decisions occurring frequently in the state Supreme Court, would certainly give reasonable ammunition to anyone challenging such an action.

We also read in the notes of that hearing that some opponents were crying foul, and that if the state were actually to enforce its tax laws we would be creating a disincentive for out-of-state investments into our economy. Frankly, we're not impressed. If the incentive for investment in Montana is to avoid the payment of legally-due taxes, we don't want the investment. And, although we believe the vast majority of persons engaged in tax preparation and consulting are honest and law-abiding, if Montana-based consultants, advisors, tax specialists or real estate dealers are advocating avoidance of taxes as a reason to invest in our state, they should be charged with collusion in such tax-avoidance schemes. And if found guilty, they should be sentenced and fined accordingly.

While our members are struggling to pay mortgages, meet rising health care costs, send their kids to college, pay outrageous utility charges and, if lucky prepare for retirement, we read that Bozeman currently has 35 homes listed at over $1 million apiece. Our members won't be buying those homes, and neither will over 97% of current Montana residents. So, if out-of-state investors want to purchase those homes and join in Montana's quality of life, good for them. But if they sell those homes and make a bundle on them and then attempt to avoid paying taxes on their gains, we get angry. And we don't care if it's a 100,000 acre ranch, a chalet in Big Sky's gated community or 3,000 acres of forested Montana lands. If you buy at a price and sell at a profit you should pay taxes on that profit. If we Montana residents were fortunate enough to buy one of those million-dollar homes and sell it for two million dollars a couple years later we would have to pay our fair share of taxes on the gain. Non-residents should be treated equally.

Lastly, Mr. Chairman and members of the Committee, I have just attended two conferences in Washington D.C. dealing with the recently-passed Budget Reconciliation Act, and what I learned is frightening. With the cuts in federal support for child-support enforcement, education, Medicaid and others, our state is going to need all the legal revenue it can find to help defray the impacts of the cuts on Montana citizens.

We all know that Montana is not a rich state in terms of average annual wages or annual income. In fact we consistently rank in the bottom portion of all national surveys on these measures. Montana only had 5,642 Montana tax filers whose income exceeded $200,000 in 2004 and only 328 who reported incomes in excess of $1 million dollars. That means that if we are going to try to offset the costs of the federal budget cuts we need to judiciously recognize and enforce the tax codes of our state.

What the Montana Department of Revenue is attempting to do is to level the playing field for the 97% of Montanans whose incomes are under $200,000 per year by educating those who can afford to invest and make a gain from a Montana property sale or transfer. They are simply suggesting that it would be easier, more responsible and less onerous for such individuals to understand upfront that they will at some point have a Montana income tax obligation, and allow them to prepare for it.

We hope this committee agrees, and we thank you for the opportunity to be with you here today.

Respectfully submitted,

Don Judge
Teamsters Local 190