MONTANA LEGISLATIVE SERVICES DIVISION
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Revenue Interim Committee
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NEW OR EXPANDED INDUSTRY CREDIT

EXPLANATION OF THE CREDIT

The new or expanded industry credit, provided for in 15-31-124 through 15-31-127, MCA, is a credit against corporate income taxes available to a new or expanding manufacturing corporation. The credit is equal to 1% of wages paid to new employees in Montana for a period of 3 years.

There is no maximum allowable credit. The credit is not refundable and may not be carried forward or back to another tax year.

> The Legislature enacted the new or expanded industry credit in 1975 and has made few changes since its enactment.

"NEW" AND "EXPANDING"

As provided in 15-31-124, MCA, a "new corporation" is a corporation that engages in manufacturing for the first time in this state and includes:

- a manufacturing corporation that exists outside of Montana and enters into manufacturing in the state;
- a nonmanufacturing corporation within the state that enters into manufacturing in the state; or
- a corporation newly formed in Montana that enters into manufacturing operations.

A "new corporation" does not include:

- a corporation reorganized from a previously existing corporation that has been engaged in manufacturing in Montana; or
- a corporation created as a parent, subsidiary, or affiliate of an existing corporation engaged in manufacturing in Montana of which 20% or more of the ownership is held by the corporation or stockholders of the corporation.

"Expanding" manufacturing is expansion or diversification of a present operation to increase total full-time jobs by 30% or more.

"MANUFACTURING"

The definition of "manufacturing" in 15-31-124, MCA, includes:

- the process of mechanical or chemical transformation of materials or substances into new products as described in the North American Industry Classification System Manual (NAICS); or
- the production of energy by means of an alternative renewable energy source such as solar energy, wind energy, geothermal energy, conversion of biomass, fuel cells that do not require hydrocarbon fuel, or methane from solid waste.

The Department of Revenue, which is directed in 15-31-127, MCA, to determine eligibility for the credit and promulgate rules, includes in ARM 42.4.1604 additional details about what qualifies as manufacturing. The rule provides the following guidance related to the Department's consideration of what constitutes manufacturing:

- Manufacturing facilities are generally described as plants, factories, or mills that use power driven machines and materials handling equipment.
- Materials processed include products of agriculture, forestry, fishing, mining, and quarrying. Products may be finished and ready for consumption or semi-finished products that are used as raw materials by another corporation.
- Materials used by manufacturing establishments may be purchased directly, obtained through trade channels, or transferred from one establishment to another under the same ownership.
- Manufacturing production is usually carried on for the wholesale market, for interplant transfer, or for industrial users rather than for direct sale to consumers.
- The Department will use its best judgement to determine the classification between manufacturing and other divisions of the NAICS.

The following table summarizes what is included as manufacturing and what is not considered manufacturing as provided in ARM 42.4.1604.

Manufacturing	Not Manufacturing
Corporations engaged in assembling component parts	Products that are structures or fixed improvements
Milk bottling and pasteurizing; fresh fish packaging; logging	Agriculture; forestry; fishing; custom grist milling; threshing; cotton ginning – processing on farms is not manufacturing if raw materials are grown on the farm and if the manufacturing is on a small scale without extensive use of paid labor
Blending of materials such as lubricating oils, plastics, resins, or liquors; apparel jobbing (assigning materials to contract factories or shops for fabrication); contracting on materials owned by others; leather converting; wood preserving; electroplating; plating; metal heat treating; polishing for the trade; lapidary work for the trade; fabricating of signs and advertising displays; publishing	Wholesale and retail trade including cutting and selling purchased carcasses, preparing feed at grain elevators and farm supply stores, stemming leaf tobacco at wholesale establishments; production of wiping rags; breaking of bulk and redistribution in smaller lots including packaging, repackaging, or bottling products such as liquors or chemicals
Ready-mixed concrete production	Mining with the dressing and beneficiating of ores; the breaking, washing, and grading of coal; the crushing and breaking of stone; the crushing, grinding, or otherwise preparing of sand and gravel and nonmetallic chemical and fertilizer minerals other than barite classified as mining
Service industries to the manufacturing trade such as typesetting, engraving, plate printing, preparation of electrotyping and stereotype plates	Blueprinting or photocopying services
Prefabrication of sheet metal, concrete, and terrazzo products and similar construction materials	Construction – fabricating operations performed at the site of construction by contractors; ship and boat building and repair; rebuilding of machinery and equipment on a factory basis; machine shop repair
	Selling products to the public that are produced on the premises such as bakeries, candy stores, ice cream parlors, and custom tailors
	Services including tire retreading and rebuilding, sign painting and lettering ships, and motion picture production

PURPOSE AND LEGISLATIVE HISTORY

1975: ENACTMENT OF THE CREDIT

The 1975 Legislature enacted the new or expanded industry credit[1] without including a purpose statement. A review of the legislative history may allow the committee to infer the intended purpose.

The title of the bill enacting the credit included the following title: "to provide an incentive for development of new industry in Montana." Materials available from the 1975 Legislature do not include a record of the hearing in the House Taxation Committee or discussion of the House Committee of the Whole or the Senate Committee of the Whole. However, summary minutes are available from the Senate Taxation Committee hearing.

The Senate Taxation Committee minutes include the sponsor's description of the bill as "an attempt to encourage either expansion of existing business, or initiation of new business, thus creating new jobs and helping the employment situation in Montana, in addition to the encouragement of new industries in the state."

Four proponents testified for the bill, including Fred Barrett from the Department of Labor & Industry (DLI) and Mr. Winsor from the Montana Chamber of Commerce. The minutes state that Barrett "said he thought the bill might help in creation of jobs and thus take people off the unemployment rolls." Barrett also provided a memorandum from the research supervisor at DLI. The memorandum estimates a $91 credit per new employee based on average manufacturing wages of $9,099.75. If a new average-sized firm (24 employees) opened in Montana and paid the average wage, the corporation would be eligible for credit of $2,184. Or, if an existing firm of the average size increased employees by 30% (the threshold to qualify as expanding), 7.2 new jobs would be created and the total credit would be $655 (assuming average manufacturing wages).[2]

Mr. Foster of the Department of Revenue spoke during the time for opponent testimony and, according to the minutes, said he did not object to the concept of the bill but "felt the bill did not attain the goals it aimed at and further, that it would create numerous administrative problems."

1991: REVISED DEFINITION OF "NEW COPORATION"

The 1991 Legislature amended the definition of "new corporation" in a larger bill revising industries considered class five property and making changes to the new or expanded industry property tax abatement.[3]

The definition of "new corporation" in the legislation enacted in 1975 was:

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[1] Ch. 435, L. 1975.
[2] The fiscal note for the bill did not include an estimate of the fiscal impact. The note stated, "Due to lack of historical information, as outlined in the above assumptions, it is not possible to estimate the magnitude of the expected corporation license tax revenue loss."
[3] Ch. 694, L. 1991.

> a corporation engaging in manufacturing for the first time in this state and manufacturing a product not currently manufactured or substantially similar to a product currently manufactured by that corporation or any affiliate corporation in this state; it does not include reorganizing an existing corporation in this state or the creation of a parent, subsidiary or affiliate of which fifty percent (50%) or more is owned or controlled by the same person, corporation or association.

The 1991 amendments changed the definition of "new corporation" in three ways:

- removed language requiring a new corporation to manufacture a product "not currently manufactured or substantially similar to a product currently manufactured by that corporation or any affiliate corporation in this state";
- provided that a new corporation includes: a manufacturing corporation existing outside of the state that enters into business in the state, a nonmanufacturing corporation in Montana entering into manufacturing, and a newly formed Montana corporation entering into manufacturing; and
- and revised the language pertaining to corporations that do not qualify as new corporations to exclude a parent, subsidiary, or affiliate with more than 20% ownership by an existing manufacturing corporation.

A review of the legislative history of the 1991 amendments shows that the changes to the definition of "new corporation" were discussed only in the House Taxation Committee. Ron Klophake of the Missoula Economic Development Corporation indicated in his testimony in support of the bill that the Department of Commerce was having a difficult time determining which products are substantially similar to products already manufactured by the corporation in the state.

The fiscal note for the bill states that the revised definition of new corporation "would significantly expand the number of companies that could potentially qualify for the new or expanded corporate tax benefit…" but did not quantify the impact.

2001: EXTENSION OF CREDIT TO ALTERNATIVE ENERGY PRODUCTION

The 2001 Legislature revised the definition of "manufacturing" to include the production of energy by means of an alternative renewable energy source, which allows a new or expanding corporation producing energy using an alternative renewable energy source to claim the credit for wages paid to new employees. The bill also created a revolving loan fund to finance alternative energy systems and amended existing tax incentives to allow their use for alternative energy production.[4] The legislative record did not include any discussion of the new or expanded industry credit.

[4] Ch. 591, L. 2001.

The amended language referred to the definition of "alternative renewable energy source" in 90-4-102[5], MCA, which was also amended in the bill as follows:

> "Alternative renewable energy source" means a form of energy or matter, such as solar energy, wind energy, geothermal energy, conversion of biomass, fuel cells that do not require hydrocarbon fuel, small hydroelectric generators producing less than 1 megawatt, or methane from solid waste, that is capable of being converted into forms of energy useful to mankind, including electricity, and the technology necessary to make this conversion, when the source is not exhaustible in terms of this planet and when the source or the technology are not in general commercial use.

TAXPAYER USE OF NEW OR EXPANDED INDUSTRY CREDIT

The following table shows the dollar value of new or expanded industry credits claimed since 1997, the years for which Department of Revenue data is available. Fewer than 10 taxpayers claimed the credit in each year so the "Number of Credits Claimed" column is marked with an "*" for each year in which any credit was claimed.

Total credits claimed between fiscal years 1997 and 2016 totaled $197,521, with credits claimed in 9 of the 20 fiscal years. The credit claimed was less than $5,000 in 6 of the years but topped $83,000 in FY 2006 and FY 2007. The dollar amount of credits claimed and average Montana wages can be used to estimate that credits may have been claimed for about 619 jobs between 1997 and 2016.

The most recent Department of Revenue Biennial Report indicates that manufacturing is the second largest sector in terms of tax year 2016 corporate income tax liability, accounting for 17% of corporate income tax collections.[6]

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[5] Ch. 405, L. 2003 repealed 90-4-102, MCA, and changed the reference in 15-31-124(3)(b) to 15-6-225. That definition of "alternative renewable energy source" is structured differently than the one in 90-4-102 but the meaning is the same.
[6] Montana Department of Revenue, "Biennial Report: July 1, 2016 – June 30, 2018," p. 87.

NEW OR EXPANDED INDUSTRY CREDIT USAGE AND ESTIMATED JOBS CREATED

Fiscal Year	Number of Credits Claimed	Dollar Amount of Credits Claimed	Estimated New or Expanded Jobs[7]	Credit as % of Corporate Income Tax Collections
1997	0	$0	0	0%
1998	0	$0	0	0%
1999	0	$0	0	0%
2000	0	$0	0	0%
2001	*	$1,721	7	0.0017%
2002	*	$994	4	0.0015%
2003	0	$0	0	0%
2004	0	$0	0	0%
2005	*	$14,659	49	0.0149%
2006	*	$84,708	271	0.0551%
2007	*	$83,570	256	0.0471%
2008	*	$4,311	13	0.0028%
2009	0	$0	0	0%
2010	0	$0	0	0%
2011	0	$0	0	0%
2012	0	$0	0	0%
2013	0	$0	0	0%
2014	*	$4,221	11	0.0029%
2015	*	$2,465	6	0.0014%
2016	*	$872	2	0.0007%

[7] Calculated by dividing credits claimed by 1% (to get wage for which credit was claimed) and dividing by Montana annual average wage. Wage data from: https://www.governing.com/gov-data/wage-average-median-pay-data-for-states.html, https://www.bls.gov/oes/current/oes_mt.htm. Average Montana wages for 2002 was unavailable so calculation uses 2001 data.

ADDITIONAL CONSIDERATIONS

POSSIBLE FACTORS AFFECTING USE OF CREDIT

The new or expanded credit has not been widely used and two factors may contribute to nonuse of the credit.

The credit is a corporate income tax credit and is only available to manufacturing companies formed as corporations and subject to the corporate income tax. Manufacturers that pass income through to their owners (who pay the individual income tax) may not claim the credit. Tax credits enacted more recently that are aimed at business activity are generally available to both corporate income taxpayers and individual income taxpayers so the business structure does not impact whether the credit may be claimed.

The credit is available for wages paid to employees in the first 3 years of operation or expansion of the corporation. A new or expanding manufacturer may not have income for tax purposes because of low income levels and/or large capital expenses. The credit is not refundable and may not be carried to another tax year, so it only benefits a manufacturer with a corporate income tax liability in the first 3 years. A corporation may not expend the effort to claim the credit if the corporation only owes the $50 minimum corporate income tax.

ADMINISTRATION OF THE CREDIT

Staff met with the Department of Revenue and asked if the agency has any concerns about administering the credit. The agency did not raise any concerns about the credit's administration.

SIMILAR INCENTIVES IN MONTANA

There are two other tax credits and one property tax abatement in Montana aimed at expanding business or creating jobs. They are discussed briefly below to provide context for consideration of the new or expanded industry credit.

EMPOWERMENT ZONE NEW EMPLOYEES CREDIT

Certain employers that create new jobs within an empowerment zone can claim an individual income tax credit, a corporate income tax credit, or an insurance premium tax credit as provided in 7-21-3710, MCA. The per-employee credit is $500 in the first year of employment, $1,000 in the second year, and $1,500 in the third year. The corporate income tax credit was not claimed between tax years 2009 and 2016. Fewer than 10 taxpayers claimed the individual income tax credit in tax years 2010, 2011, 2014, and 2016, and no taxpayers claimed the credit in the other tax years between 2009 and 2017. The 2003 Legislature enacted the credit and it is scheduled for review during the biennium beginning July 1, 2025.

INFRASTRUCTURE USERS FEE CREDIT

Section 17-6-316, MCA, allows a local government to obtain a loan from the Board of Investments to build infrastructure for the location or creation of a business in Montana that will create at least 15 jobs. The local government may charge fees to the business using the infrastructure and the business may take a credit against individual income taxes or corporate incomes taxes for the fees charged for use of the infrastructure. Fewer than 10 taxpayers claimed the corporate income credit each year between 2009 and 2016. Use of the individual income tax credit is available on p. 329 of the Department of Revenue Biennial Report. The 1995 Legislature enacted the credit and it is scheduled for review during the biennium beginning July 1, 2023.

NEW OR EXPANDING INDUSTRY PROPERTY TAX ABATEMENT

As provided in 15-24-1401 and 15-24-1402, MCA, a city or county may grant an abatement for their mills and local school district mills for the property of new or expanded industry. If granted, the abatement provides that the property is valued at 25% or 50% of taxable value (as determined by the local government) for 5 years after which the taxable value increases by an equal amount each year until the property is taxed at its full value by the 10th year after the abatement is granted.

To qualify as "new" the firm must be new to the taxing jurisdiction and invest at least $125,000 in improvements. An "expansion" is the addition of at least $50,000 of improvements. "Industry" includes but is not limited to:

- the mechanical or chemical transformation of materials into products in the manner defined as manufacturing in the NAICS;
- extraction or harvesting of minerals, ore, or forestry products;
- processing of Montana raw materials;
- transportation, warehousing, or distribution of commercial products if 50% or more of the gross sales are earned outside the state;
- any firm that earns 50% or more of its annual gross income from out-of-state sales;
- the production of electrical energy in an amount of 1 megawatt or more by means of an alternative renewable energy source; or
- the operation of a qualified data center or new industrial property.

Because state mills are not abated, the Department of Revenue does not publish data on usage of the abatement in the Biennial Report. The 1981 Legislature originally enacted the abatement.