



Revenue and Transportation Interim Committee

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59th Montana Legislature

SENATE MEMBERS

JIM ELLIOTT--Chair
GREGORY BARKUS
JERRY BLACK
KIM GILLAN
SAM KITZENBERG
KEN TOOLE

HOUSE MEMBERS

KARL WAITSCHIES--Vice Chair
JILL COHENOUR
CYNTHIA HINER
BOB LAKE
DAVE MCALPIN
PENNY MORGAN

COMMITTEE STAFF

JEFF MARTIN, Lead Staff
LEE HEIMAN, Staff Attorney
DAWN FIELD, Secretary

MINUTES

September 30, 2005

Room 102, State Capitol
Helena, Montana

Please Note: These are outlined minutes with audio recording. These minutes provide abbreviated information about Committee discussion, public testimony, actions taken and other activities. For each activity listed, the minutes indicate the amount of time (in hours, minutes and seconds) that has elapsed since the start of the meeting. This time may be used to locate the activity on the audio recording. "Part 1" contains the a.m. portion of the meeting. "Part 2" contains the p.m. portion of the meeting.

COMMITTEE MEMBERS PRESENT

SEN. JIM ELLIOTT, Chair
REP. KARL WAITSCHIES, Vice Chair

SEN. JERRY BLACK
SEN. SAM KITZENBERG
SEN. KEN TOOLE

REP. JILL COHENOUR
REP. CYNTHIA HINER
REP. BOB LAKE
REP. DAVE MCALPIN
REP. PENNY MORGAN

COMMITTEE MEMBERS EXCUSED

SEN. GREGORY BARKUS
SEN. KIM GILLAN

STAFF PRESENT

JEFF MARTIN, Lead Staff
LEE HEIMAN, Staff Attorney
DAWN FIELD, Secretary

AGENDA & VISITOR'S LIST

Agenda, [Attachment #1](#).
Visitors' list, [Attachment #2](#).

COMMITTEE ACTION

The Revenue and Transportation Interim Committee:

- approved the June 17, 2005, meeting minutes, as written;
- adopted recommendations for special session revenue estimating procedures;
- tentatively adopted the HJR 43 study plan, allowing for revision at the next meeting;
- endorsed the gasoline tax agreement between the DOR and the Blackfeet Nation;
- tentatively adopted the HJR 44 study plan with the suggested changes from SEN. BLACK; and
- adopted the proposed schedule for review of business taxation topics.

PART 1 - TAPE 1 - SIDE A

CALL TO ORDER AND ROLL CALL

00:00:34 The Committee approved the minutes as written.

00:02:53 **Terry Johnson, Principal Fiscal Analyst, Legislative Fiscal Division (LFD)**, presented a General Fund Status report for Fiscal Year 2005 (Powerpoint slides and written report - [EXHIBIT #1](#)), in which he discussed Fiscal Year 2005 actual and 2007 Biennium projected revenues and fund balances. The report provides preliminary fiscal 2005 ending fund balance data for the general fund account.

Estimated Revenues for Each Tax Category of Tax Collected in Montana:

00:10:26 Individual Income and Audit Revenue;

00:12:04 Corporation Income Tax;

00:14:26 FEMA Reimbursement;

00:15:03 Oil and Natural Gas;

00:16:49 Coal Trust Interest Earnings;

00:17:18 Coal Severance Tax;

00:17:49 Vehicle Taxes and Fees, Lottery Profit, and Insurance Tax;

00:18:56 Property Tax;

00:20:07 Institution Reimbursements - Medicare and Accounting Change; and

00:20:58 All Other Remaining General Fund Categories.

- 00:21:34 Mr. Johnson said that disbursements and reversions are contributing factors to the higher than anticipated ending fund balance. Mr. Johnson reviewed disbursements for the current year, non-budgeted disbursements, and prior year activity.
- 00:24:17 Mr. Johnson discussed the actual, prior year, budgeted, and unexpected reversions for Fiscal Year 2005. Agencies with major reversions included the Legislative Branch, the Office of Public Instruction, the Department of Revenue, the Department of Public Health and Human Services, and several other agencies.
- 00:28:22 Mr. Johnson discussed fund balance adjustments.
- 00:29:13 Mr. Johnson presented the balance change summary.
- 00:29:54 Mr. Johnson discussed the 2007 biennium outlook. He told the Committee that the LFD has not taken into account revenue trends in 2005, any proposed solutions to public school funding, or the unfunded liability of state retirement systems.
- 00:34:35 Mr. Johnson presented his recommendations for special session revenue estimating ([EXHIBIT #2](#)) focusing on four key areas: individual income tax, corporation income tax, property tax, and oil and natural gas production tax. **TAPE 1 - SIDE B** Mr. Johnson asked the Committee for direction on how to proceed with the revenue estimating procedure. He said the LFD, in cooperation with the OBPP, would prepare a document that would highlight the key assumptions to allow the Committee to focus on the critical components.
- 00:47:37 **Judy Paynter, Office of Budget & Program Planning (OBPP), Governor's Office**, said in the event of a special session, the focus should be on school funding. Ms. Paynter also said it is important that the revenue estimates come out clean, early, and not hold up the appropriation process.
- 00:49:02 **COMMITTEE QUESTIONS**
- REP. LAKE asked what percentage of the increased revenue is ongoing, versus one-time income. Mr. Johnson said he could not definitively say until detailed tax returns for individual income tax for calendar year 2004 become available in November. Mr. Johnson discussed possible outcomes when the information is received.
- 00:55:29 REP. LAKE asked if, after one or more financially disastrous events, it is normal to see a significant recovery spike in revenues before it returns to constant growth. Mr. Johnson said that such an argument could be made but that he could not recall, in his 32 years of service, such a large growth in individual income tax revenue or corporate income tax revenue.

- 00:57:39 REP. LAKE asked if the expiration of the tax adjustments made as a result of 9/11 could account for the recent spike in revenues. Mr. Johnson said that accelerated depreciation initially reduced state corporation tax revenue; but long-term there would be more corporation tax revenues, because there will be a smaller write-off for depreciation in subsequent years. Mr. Johnson said federal changes also reduced federal individual income tax payments resulting in higher state tax payments. SB 407 capped the amount of deductions for federal taxes paid, which affected revenue amounts. Mr. Johnson noted that it is not a simple process and that there are a number of factors at play.
- 01:00:40 SEN. TOOLE said that increasing energy prices result in increased revenues, which is good, but only up to a point because high energy prices begin to dampen other economic activity. He asked if there is a way of looking at corporate income tax and individual income tax to determine how much is related to escalating oil prices and energy prices. Mr. Johnson said LFD staff has tried to do this in past without satisfactory results because, in order to gather accurate data, the LFD would have to have examine individual tax returns.
- 01:03:52 REP. MCALPIN asked if the LFD has contacted other states to compare notes. Mr. Johnson said that he gathers information from the National Conference of State Legislatures (NCSL), the Wall Street Journal, and other sources. He said information on what is happening in other states indicates that capital gains and dividend income are causing increased tax revenues.
- 01:05:18 REP. COHENOUR asked if dividend income will continue. Mr. Johnson said that, based on the fact that it is a permanent tax policy at the federal level, he anticipated that it would continue.
- 01:05:55 REP. WAITSCHIES asked if there is a way to separate by region estimated payments from royalty payments. He said oil revenue is driven by the eastern part of the state, real estate revenue and capital gains are driven by the western part of the state. Mr. Johnson said the tax return data would have a county identifier on it, so to a certain extent, some general distinctions could be made. If the LFD could look at estimated tax returns, it could make more specific correlations.
- 01:07:20 SEN. TOOLE **moved** to adopt Mr. Johnson's recommendations for the procedure for the special session revenue estimating. The **motion passed on a unanimous voice vote.**
- 01:08:43 Jeff Martin introduced Dawn Field as the Revenue and Transportation Committee Secretary. He said that minutes would be recorded in an audio format and explained the advantages of using the audio format.
- 01:10:08 SEN. TOOLE requested, given the postponement of the U.S. Senate vote on estate tax, that the estate tax discussion be removed from the agenda. Mr. Martin said he had prepared a report on federal and state estate taxes ([EXHIBIT 3#](#)).

UPDATE ON PPL MONTANA PROPERTY TAX PROTEST

- 01:12:14 **David Hoffman, PPL Montana**, distributed information regarding PPL Montana's property tax appeals ([EXHIBIT #4](#)). **TAPE 2 - SIDE A**
- 01:22:48 SEN. TOOLE asked if there is a limitation on PPL's rate of return. Mr. Hoffman said PPL does not operate in a regulated, cost-based system, so a rate of return is not applicable. There is the potential of reward and risk associated with operating and selling in an open market. SEN. TOOLE said Mr. Hoffman was comparing PPL's facilities to facilities which operate under a regulated rate of return ([EXHIBIT #4](#)). He said the argument that these facilities are exactly the same can not be made, because PPL's potential for profit and also potential risk is much higher. Mr. Hoffman said there is truth to that statement but that the risk component is an equalizing factor. He said PPL's position is not that it needs to be treated identically with the others and that there are differences in income components that can take into account the difference in the way PPL markets its power.
- 01:24:56 SEN. TOOLE asked Mr. Hoffman about the recent Federal Energy Regulatory Commission decision that PPL exercises market power. Mr. Hoffman said he could not comment because it remains a hypothetical issue at this point. SEN. TOOLE asked if PPL is planning to follow Northwestern Energy's challenge for contributions to a heating assistance program during the winter. Mr. Hoffman said a decision has not yet been made but pointed out that in the past, PPL has contributed millions of dollars to Montana in a variety of ways.
- 01:27:17 SEN. BLACK asked how this issue in other states has been handled. Mr. Hoffman said he is not fully aware of what is happening in other states but that what he does know would lead him to believe that those situations significantly differ from Montana.

DEPARTMENT OF REVENUE REPORTS

- 01:28:21 **Director Dan Bucks, Department of Revenue (DOR)**, distributed and discussed:
- a document that explained the revisions made to the Montana Individual Income Tax Booklet, an IRIS Status Update, and other issues being addressed by the Department ([EXHIBIT #5](#));
 - the 2004 Montana Individual Income Tax Booklet ([EXHIBIT #6](#));
 - the revised 2005 Montana Individual Income Tax Booklet ([EXHIBIT #7](#)); and
 - several charts detailing many of the specific changes made to the tax booklet, ([EXHIBIT #8](#)).
- 01:50:10 REP. MORGAN asked if the Department anticipates an increase or decrease in revenues with the new tax forms. Director Bucks said he anticipates an increase in the level of accuracy of returns which could affect revenue either way, but not significantly.

- 01:51:43 SEN. BLACK asked about the Montana Society of CPA's involvement with the new form. Director Bucks said the Society had extensive input on the revisions and that generally, the CPA's view the revisions positively. SEN. BLACK asked if the Montana Taxpayers Association had input or has offered comment. Director Bucks said that the Association has received a copy but that he has not received comments.
- 01:53:39 Director Bucks provided an Integrated Revenue Information System (IRIS) status update (Pages 10 - 12 - EXHIBIT #5). Director Bucks said that as of November 1, 2005, the Department will begin sending out monthly bills to delinquent taxpayers. He said a Customer Service Center has been established to help taxpayers with their questions and encouraged the Committee to tell constituents to contact the Service Center at 406-444-6900 if they experience any difficulty. He also asked the Committee members, as legislators, if they become aware of a taxpayer who is experiencing difficulty, to call the Department at 406-444-1900.
- 02:00:29 Director Bucks presented a "Draft for Comment" letter (EXHIBIT #9) sent to Montana's congressional delegation and to Montana senators and representatives to help them explain and assist constituents with the changes being made. He asked the Committee members to comment on the draft letter. Also included in EXHIBIT #9 was a press release issued by the Department and a letter which will be sent to delinquent Montana taxpayers explaining their account. Director Bucks noted that the Department is moving toward a more consumer-friendly format.
- 02:03:00 REP. MORGAN asked how the Department plans to handle disagreements between taxpayers and the Department. Director Bucks said many of the problems have been corrected, but that taxpayers are encouraged to call the Department if they have trouble. **TAPE 2 - SIDE B**
- 02:05:31 REP. WAITSCHIES asked how much of the outstanding balance of \$40 million could actually be collected. Director Bucks said that it is likely that about half of the \$40 million are actual assessments, which would have a high collection rate. He said he would get that information to REP. WAITSCHIES later in the day. The remaining \$20 million, primarily made up of estimated assessments, would not be as easily collected. Director Bucks explained the difference between actual and estimated assessments.
- 02:08:39 REP. LAKE asked for a specific number of people who would be receiving these notices. He said these are the constituents that legislators would likely be hearing from. Director Bucks said that information is unavailable because the old system did not track the last date of contact.
- 02:10:17 REP. LAKE said he didn't understand why the contracted firm could not be made to provide that information. Director Bucks said he would pursue it but was skeptical that the information would be made available.
- 02:11:57 Director Bucks resumed his presentation (Pages 21 - 23, EXHIBIT #5) regarding:

- the U.S. Supreme Court decision regarding the direct shipment of wine into a state;
- the Montana First Judicial District Court ruling on non-resident ownership of retail alcoholic beverage licenses; and
- tribal Tobacco and Alcohol Revenue Sharing Agreements.

02:16:25 REP. MORGAN asked if the court decision on out of state ownership of alcoholic beverage licenses would affect gaming licenses as well. She said that when a Holiday Inn in Billings was sold it was forced to give up the gaming license for the lounge because it had out of state owners. Director Bucks said the DOR does not administer the gaming statutes, but predicted that gaming licenses would be affected. He said he would contact the Justice Department and get that information for REP. MORGAN.

02:18:22 Director Bucks discussed:

- compliance studies (Page 13 - EXHIBIT #5);
- income tax audit collections (Page 14 - EXHIBIT #5);
- illegal tax shelters (Pages 15-17 - EXHIBIT #5);
- nonresident sales of property tax payment compliance (Page 18 - EXHIBIT #5);
- the state employee cross match (Page 19 - EXHIBIT #5); and
- employee embezzlement (Page 20 - EXHIBIT #5).

02:36:12 REP. LAKE asked if the Department anticipated revisiting HB 799 from the 2005 Legislative Session on the sale of nonresident property. Director Bucks said efforts have been made to eliminate problems and to be able to distinguish clearly between a pure property sale and a property exchange. He said no decision has been made regarding HB 799 and explained the complexity of Montana law with respect to this issue.

02:42:17 SEN TOOLE asked for the total number of state employees in the state employee cross-match. He wanted to know why this group is being singled out. **TAPE 3 - SIDE A** Director Bucks said there are approximately 10,000 state employees affected by the cross-match. He said the Department is providing this information as a followup to recent press coverage. Director Bucks said the rate of nonfiling among public employees is higher than it should be.

02:45:49 SEN. TOOLE said his concern is that state employees are being singled out unfairly and that other taxpayers would probably have similar statistics.

02:47:50 SEN. BLACK asked if Director Bucks expects to see a substantial decrease in the occurrence of illegal tax shelters, now that there has been a crack down. Director Bucks said much remains to be done. He said that experts are of the opinion that because of the crackdown, the activity will subside for a period of time, but will resume in a more complex and difficult to track format. SEN. BLACK asked if the IRS has to approve plans. Director Bucks said that Congress has been increasing requirements for tax practitioners and taxpayers to disclose their transactions, but in terms of reviewing what is sent to them, the

IRS is reading only 18% of the cases. Most of these illegal shelters have been discovered by IRS audits.

02:51:07 SEN. BLACK asked about the new tobacco and alcohol revenue sharing agreements and whether it was an increase or a decrease in revenue from the previous agreement. Director Bucks said it was an extension of the prior agreement and brought the cigarette tax rate current with the new tax rate. He explained the differences between the old agreement and the new agreement.

PUBLIC COMMENT

02:53:47 **Mary Whittinghill, Montana Taxpayers Association (MTA)**, submitted a letter from various organizations asking the Committee to consider forming a stakeholders group to work with the Committee and the DOR regarding tax policy and the state's income tax system ([EXHIBIT #10](#)). She noted that four other associations wanted to be signatories on the letter: the American Insurance Association, the American Council of Life Insurers, State Farm Insurance, and Farmers Insurers Group.

02:56:15 SEN. TOOLE said he has been involved in many stakeholder groups and has observed that legislatively-mandated collaborative efforts often do not work. He asked if the working group would be willing to agree in advance to support legislation that may come forward. Ms. Whittinghill said the intention of the group is to fully support the product of the working group and the DOR.

02:57:59 SEN. ELLIOTT asked what role the MTA would play in the instance of out of state sellers of Montana realty. Ms. Whittinghill said the role would be to work with Department and other interested individuals through the Revenue and Transportation Committee to find solutions and to ensure that the income is being reported when it should be reported. Ms. Whittinghill said that by working together with a broad base of associations, the end result would be a product that would have broad support.

02:59:51 SEN. ELLIOTT asked how such a broad constituency could contribute to an issue that essentially encompasses only realtors and title agents. The purpose of a stakeholder group is to encourage open dialog. SEN. ELLIOTT asked if Ms. Whittinghill would object to Director Bucks directly consulting with the groups individually. Ms. Whittinghill said that would be the Director's prerogative but that she would still like to be able work throughout the process as group and that she thought that would better ensure passage of any proposed legislation. SEN. ELLIOTT said the broad question, is should people pay taxes that they owe the State of Montana. Ms. Whittinghill said that the end result would be that taxes be would be paid, but the policy question is, at what point should it be withheld and paid.

03:03:25 SEN. WAITSCHIES said it would be better if the organizations can send people that have a consensus of the organization, rather than just individuals going in and having input. When there is consensus, there would be a better feeling of the proposed legislation.

UPDATE ON QUALITY SCHOOLS INTERIM COMMITTEE

- 03:14:05 **Connie Erickson, Research Analyst, LSD**, discussed the status of the Quality Schools Interim Committee (QSIC). Ms. Erickson provided a memo from the Office of Budget and Program Planning to the QSIC discussing the equalization of school mills (K-12) statewide ([EXHIBIT #11](#)). Ms. Erickson reviewed the work of the QSIC, working group, and the consultants. The consultant will issue a final report by October 3, 2005. Ms. Erickson said audio minutes are available on the QSIC web page. She said the QSIC has made a significant amount of progress, has made a good faith effort to address the situation, and is determined to come up with new funding formula. The QSIC will continue to meet through October in anticipation of a possible special session.
- 03:29:44 REP. COHENOUR asked if the Sherlock decision found that the current funding formula is unconstitutional or if the funding itself is the part that is unconstitutional. Ms. Erickson said the formula was found unconstitutional because the current formula has no definition and that entitlements are not tied to costs. The QSIC is trying to figure out actual costs in order to have a rational basis for the amount of money it will recommend to be put into the system. REP. COHENOUR said the system needed a rational basis for the numbers that were being into a formula, so the formula itself really wasn't the issue, it was how the associated costs were being determined. She asked, if there is a rational basis for the money that is plugged into the formula, could the current formula be used. Ms. Erickson said it could be used but that it would have to be modified and discussed several issues that would have to be dealt with. REP. COHENOUR reiterated that it is the lack of a rational basis for how that money goes into the formula that is the problem. Ms. Erickson agreed, saying the QSIC believes a solution must be defensible and it must be tied to actual costs.
- 03:33:24 REP. LAKE, who has been attending the QSIC meetings, gave his perspective on the work of the QSIC and by the working group. **TAPE 3 - SIDE B** He discussed salary and retirement issues, reports from Woods and Associates, the Stoddard and Young salary study, and actions taken by the QSIC. He said that SEN. DAVE LEWIS had recommended \$4,000 per classroom and explained some of the other funding proposals. He said the funding proposals would total about \$100 million and it is anticipated that this will not require any additional tax burden. REP. LAKE asked if the RTIC wanted him to continue attending the QSIC meetings.
- 03:49:22 SEN. TOOLE asked whether Sen. Lewis's proposal included health insurance or teachers retirement. REP. LAKE said it did not.
- 03:49:47 REP. MCALPINE asked what the \$4000 per class included. REP. LAKE said that the QSIC did not want to attach funding to teachers specifically, due to collective bargaining agreements already in place, and that the money would go towards the costs of operating a classroom, including maintenance costs.
- 03:51:06 SEN. ELLIOTT asked REP. LAKE if he thought it would be beneficial for him to continue attending the QSIC meetings. REP. LAKE said that it would be

beneficial for him to continue to attend. SEN. ELLIOTT was in favor of REP. LAKE's continued attendance. SEN. BLACK agreed. REP. COHENOUR agreed but asked for a budget update. Mr. Martin said he has examined the budget and that, based on full attendance of members at meetings, the Committee would come very close to maximum budget. He offered several suggestions on how to best utilize remaining funds.

03:55:12 SEN. ELLIOTT said the work plan and budget would be discussed later in the meeting and said that the decision to approve REP. LAKE's continued attendance would be delayed until that time.

HJR 43 STUDY OF THE VALUATION OF AGRICULTURAL LAND

03:56:18 Mr. Martin presented the proposed study plan for the classification, valuation, and taxation of agricultural land ([EXHIBIT #12](#)). He said the intent of Legislature was to ensure that lands which are devoted to agricultural purposes are not influenced by land speculation activities in the surrounding area. He discussed the valuation of agricultural land and presented several questions to be considered in the study. Mr. Martin discussed a timeline for conducting the study and the option of coordinating with the DOR Agricultural Advisory Committee. **TAPE 4 - SIDE A** Mr. Martin provided copies of a letter from Steve Pilcher of Montana Stock Growers Association (MSGA) requesting that Rep. Jim Peterson and Dr. Myles Watts participate in the HJR 43 study ([EXHIBIT #13](#)).

04:15:06 **John Youngberg, Montana Farm Bureau**, supported the inclusion of Rep. Peterson and Dr. Watts in the HJR 43 study.

04:15:33 **Mike Murphy, Executive Director, Montana Water Resources**, concurred with the statements made by Mr. Youngberg.

04:16:32 REP. WAITSCHIES commented that he supports the work plan but said that he is hesitant to allow the study to stretch out into another interim.

04:17:16 **Randy Wilke, DOR**, supported the study plan and also supported the idea of extending it over an additional interim because some key information will not be available until 2008. He said the committee final report is due the fall of 2006, so the report may be difficult to complete.

04:18:39 REP. MORGAN expressed her concern about stretching the study out over another interim.

04:19:31 REP. LAKE said that he would like to see the Committee determine who will conduct the study and to determine if the study can be conducted in the allotted time.

04:20:35 SEN. ELLIOTT suggested adopting the work plan tentatively and allow for revision at next meeting. SEN. BLACK **moved** to tentatively approve the HJR 43 work plan. The **motion passed unanimously** on a voice vote.

PART 2

MONTANA DEPARTMENT OF TRANSPORTATION REPORTS

- 00:00:04 REP. ELLIOTT called the meeting back to order at 1:35 p.m.
- Jim Lynch, Director, Montana Department of Transportation (MDT),** presented a report on the federal reauthorization of highway funding:
- The total guaranteed spending nationally is \$286.4 billion and the contract authority nationally is \$295 billion;
 - Montana's average amount each year is \$355 million, based on the new formula;
 - Montana did not suffer any major loss of funding under the new formula;
 - Montana received an additional \$216 million through the core program for additional earmarked projects.
- 00:05:50 Director Lynch also discussed disbursement of federal fuel tax revenue, the type of funding formula used, and the allocations for construction, transit, and earmarked projects.
- 00:12:27 REP. MORGAN said the Bozeman parking garage made national news because FEMA asked that some of the earmarked funding be returned for disaster assistance. She asked what the Department's position was. Director Lynch said the matter would be decided by the federal delegation. He explained the earmarked funding for the parking garage in Bozeman. He said that Montana has tremendous needs and that in his opinion, returning the funding may not be the wisest avenue.
- 00:16:23 REP. LAKE asked Director Lynch for an update on the repair of the Beartooth Highway. Director Lynch reported that the highway is due to open before October 15, 2005, and will be completed under budget. He reported that all involved with the project were tremendously supportive and worked cooperatively to complete the project.
- 00:20:30 REP. LAKE asked if the alternative routes would need repair. Director Lynch said many of the routes were in Wyoming and that Wyoming was very cooperative throughout the project. Some repairs will have to be made and the MDT may also need to look problems with slide area which could not be addressed with these emergency funds.
- 00:23:43 SEN. BLACK asked if the transit budget contains money for rural bus transportation. Director Lynch said it does and explained some of the changes regarding operational expenses.
- 00:24:18 SEN. BLACK asked how earmarked projects are prioritized. Director Lynch said almost of all of the earmarks are for state highways and are already underway. The MDT is in the process of working with communities to explain how the earmarks will be applied and is asking for input from those communities.

- 00:28:16 SEN. ELLIOTT asked if the funding included money for senior citizen busing. Director Lynch said that it does.
- 00:28:47 **Loren Frazier, Chief Engineer, MDT**, discussed the status of roundabouts. Mr. Frazier said that Northwestern Traffic Institute provides training for local governments and consultants on roundabouts. The draft update to the traffic manual to include roundabouts has been completed and is up for public comment. There are two projects to construct roundabouts in Helena.
- 00:30:05 REP. COHENOUR asked where the roundabouts will be located. Mr. Frazier said that they will be installed at the Montana City and the South Hill interchanges.
- 00:31:17 **John Blacker, Administrator, Maintenance Division, MDT**, reported on ethanol use for the State motor pool and E-85 vehicles. Mr. Blacker provided a brief history of the E-85 vehicles purchased for State use. **TAPE 4 - SIDE B** He said that misblended fuel caused many problems with the E85 vehicles but the proper blend of ethanol fuel is now available. He said that these cars have met their life expectancy and will be sold. Although the Department is not planning to purchase more, it would consider a bid.
- 00:36:13 SEN. KITZENBERG asked if the State ethanol fuel tank is empty and stated his concern that there are no plans to replace the E85 vehicles. He asked if the State is going to abandon ethanol. Mr. Blacker said the MDT owns the fuel tank and that it is empty. He said because of the misblended fuel, the fuel would be purchased at another location in Helena. The Department is not specifying that new vehicles purchased be E85 vehicles because it is still difficult to find fuel for these cars statewide and because the vehicles do not get good gas mileage. Mr. Blacker said he believes that state fleet could use alternative fuels but needs a good supplier.
- 00:40:45 SEN. KITZENBERG said he doesn't think the Department's actions are consistent with Governor Schweitzer's ethanol policy and asked if the MDT has discussed this issue with the Governor.
- 00:44:42 SEN. BLACK asked about the price differential between the blended fuel and regular gasoline. Mr. Blacker said that typically, blended fuel costs less than regular gasoline. He said the Department has been directed to provide a list of all Montana service stations selling E10 fuel in all motor pool vehicles and that all state employees are encouraged to use E10 fuel whenever possible. He said the Department is not moving away from the administration's policy for using ethanol.
- 00:46:57 Director Lynch said the Department is looking at this issue and that it is cognizant of the fuel crisis.
- 00:48:17 SEN. BLACK said that SB 293 (2005) requires that any operating ethanol plants or proposed ethanol plants must update the Department on any plans to build or to update. He asked Mr. Lynch if that is being complied with. Director Lynch

said at this point in time, no new plants have started production and that he is working with two plants currently being built in the state.

GASOLINE REVENUE SHARING AGREEMENT, GOVERNOR'S OFFICE, DAVID EWER

- 00:51:21 Mr. Lynch spoke on behalf of David Ewer, Budget Director. He discussed a memo summarizing the State and Blackfeet Nation gasoline tax revenue sharing agreement ([EXHIBIT #14](#)). Mr. Lynch also provided copies of the actual agreement ([EXHIBIT #15](#)).
- 00:56:18 REP. MORGAN asked if the gas tax revenue is collected for road maintenance. Director Lynch said that is correct. REP. MORGAN asked which entity is responsible for maintaining roads on the reservations. Director Lynch said state highways that run through reservations are maintained by the state, that the State is required to provide a 13% match for maintenance of some nonreservation roads. On most reservation projects there is no match requirement, so 100% of the cost is paid by the federal government. He said there has never been a requirement that the Blackfeet Tribe has to use this money for roads. SEN. ELLIOTT said Montana law requires that the Montana fuel tax money must be used for roads. Director Lynch explained how the gas tax money was allocated. SEN. ELLIOTT said that since this is an agreement between two sovereign governments, the Blackfeet Tribe can spend the gas tax money however it chooses.
- 00:58:17 REP. LAKE asked if the Department uses the total of the gross dollars to match the federal highway funds prior to reimbursing the tribes. Director Lynch said that statutorily, a certain portion of the gas taxes collected have to go to certain areas. The balance remaining is used for the highway program and typically amounts to about 65-70% of the total.
- 01:00:00 REP. COHENOUR **moved** to endorse the agreement. The **motion passed 7-1**, with REP. MORGAN voting no. SEN. GILLAN voted yes by proxy (SEN. ELLIOTT); SEN. KITZENBERG, SEN. TOOLE, and REP. WAITSCHIES were absent ([ATTACHMENT #4](#)).
- 01:01:50 SEN. BLACK asked for clarification on the dollars per enrolled member formula (Page 4 of [EXHIBIT #14](#)). Director Lynch explained how the formula was determined. He said the enrollment numbers are verified each quarter before the tax money is returned to the Tribe.
- 01:04:10 REP. LAKE **moved** to reopen the vote to allow absent members to vote on the proposed revenue sharing agreement.
- 01:05:17 Ms. Paynter, OBPP, said the agreement cannot go into effect until the Attorney General signs it. Ms. Paynter asked the Committee to take immediate action, in order to have the agreement signed by October 1, 2005.

01:06:37 REP. COHENOUR **moved** that the Committee endorse the gasoline tax agreement between the DOR and the Blackfeet Nation. The **motion passed** on a 9-1 roll call vote, with REP. MORGAN voting no ([ATTACHMENT #5](#)).

HJR 44 STUDY OF PROPERTY TAXATION OF OIL AND GAS PRODUCTION

01:07:59 **Tom Richmond, Administrator & Petroleum Engineer, Board of Oil and Gas Conservation**, gave a Powerpoint presentation on:

- definitions used in the industry;
- Montana oil and gas production;
- factors in designing oil production facilities **TAPE 5 - SIDE A**;
- factors in designing gas production facilities; and
- processing oil and gas for market ([EXHIBIT #16](#)).

01:34:02 SEN. KITZENBERG asked why more gas wells are not being drilled in Montana and noted that the price of natural gas has increased by 27%. Mr. Richmond said every crew and rig available in the state are busy drilling wells. SEN. KITZENBERG said the price has increased by 27% and asked who is benefitting from that increase. Mr. Richmond said that natural gas royalties paid to the mineral owners is based on its value at the time it is sold. The price paid to the mineral owner should be the same price paid to the producer. Mr. Richmond explained that most of Montana gas is sold into the midwest market and that the price is determined outside the state. He said that it is not Montana supply and demand that drives the price, but the supply and demand elsewhere.

01:38:58 SEN. KITZENBERG said he asked Montana Dakota Utilities (MDU) to build a fertilizer plant at Saco. Mr. Richmond said he could not respond and suggested that he contact MDU directly.

01:40:31 **John Alke, Attorney for MDU**, responded to SEN. KITZENBERG's remarks. He said the majority of the gas sold by MDU is produced by independent producers and not MDU. He said that the national price of gas drives the price of gas in Montana. He explained how the price of gas changes from month to month and how it is tied to the Colorado Interstate Gas (CIG) Index. Mr. Alke said the price that gas can be sold for in Denver dictates the price in Montana. He agreed that the price of gas is definitely going up. He said worldwide energy markets are driving prices and there is little that can be done about it at the state level.

01:43:41 SEN. TOOLE said utility companies should have a mix of different term contracts. Mr. Alke said producers no longer want long-term contracts because of the potential for rising prices. They will agree to sell for a long term but will not agree to fix the price for a long term.

01:45:48 SEN. TOOLE asked if MDU has storage facilities. Mr. Alke said MDU has large storage facilities but that prices have not gone down in the summer as they used to. MDU used to be able to buy cheaper gas in the summer, store it until winter, and then sell it at a lower price.

- 01:47:23 Mr. Martin presented the history and background of the proposed study of the property taxation of oil and natural gas ([EXHIBIT #17](#)). Topics covered by Mr. Martin's presentation included:
- the reason for the study;
 - Montana's Constitutional requirements for assessment of property for property tax purposes; and
 - questions and issues to be considered regarding the classification and taxation of certain oil and natural gas property in Montana.
- 01:52:31 SEN. KITZENBERG referred to Page 5 of EXHIBIT #17 regarding MDU's appeal of the valuation of its property and the classification of "indirect subsidiaries". He asked if one of the purposes of this study is to give MDU a tax break on its property. Mr. Martin said this relates to the central assessment of property owned by MDU affiliates. HJR 44 doesn't deal with the classification or taxation of transmission lines, just from the well to the transmission line. That is the issue: should it be centrally assessed and how should that property be defined, in terms of assessment. **TAPE 5 - SIDE B**
- 01:54:41 SEN. WAITSCHIES asked, in light of the lawsuits, if it wouldn't be prudent to wait until those are settled. Mr. Martin said the Committee could choose to do that, but that conducting the study may help the Committee to prepare to deal with those legal decisions.
- Mr. Martin discussed:
- the unit value approach;
 - centrally assessed property and the different property classes within that classification; and
 - the DOR administrative rule list for valuing centrally assessed property.
- Mr. Martin told the Committee that a recent District Court decision had ruled that subsection 3 was an invalid rule.
- 02:02:37 SEN. TOOLE asked if the Legislature reduced electrical centrally assessed property tax rate from 12% to 6%. Mr. Martin said most generation facilities are taxed under class thirteen. Telecommunication property is also in that class.
- 02:03:56 Mr. Martin discussed the major study areas and a proposed schedule.
- 02:10:34 SEN. ELLIOTT asked Mr. Walborne for an explanation of how this issue began and what effect potential court rulings could have on the HJR 44 study. **Gene Walborn, Department of Revenue**, said this situation began with the divestiture of the Montana Power Company (MPC) and of MPC production assets, and the merging of Pan Canadian and Alberta Gas to form Encana. Encana argued that it should be locally assessed and not centrally assessed. Encana sold most of its Montana assets to Omimex, which is the appeal that Mr. Martin referred earlier to. MDU is using a similar argument, it has broken up some of the production companies into smaller companies and acquired Red Stone Gas. Mr. Walborn discussed other appeals in the State that have been resolved.

- 02:14:01 SEN. ELLIOTT asked why some pipelines that cross county lines are centrally assessed and others are locally assessed. Mr. Walbourne said it is his opinion that the State has properly and clearly defined who ought to be centrally or locally assessed. He said review processes are in place to make sure all involved receive fair treatment. He said FERC regulations are also a factor. He noted that 15-23-101, MCA, specifically lists oil and gas pipelines. He said the debate centers around when a pipeline starts.
- 02:16:01 SEN. ELLIOTT asked what effect an adverse ruling would have. Mr. Walbourn said if the Department loses the central assessment argument, that will have a big financial impact. Another concern is that a decision that could be applied to electric utilities or electric generators.
- SEN. TOOLE asked if the basis of the lawsuit is constitutional or statutory. Mr. Walbourn said he believed equalization to be a constitutional issue.
- 02:18:07 SEN. TOOLE said before deregulation, on the gas side, this was never an issue because it was essentially a "pass through to rates". He said now the pass through to rates isn't automatic and asked if he was correct in that statement. Mr. Walborn said he didn't know.
- 02:18:43 Mr. Richmond said that when the MPC system was intact, MPC owned the compression and gathering facilities, so the point of sale was a meter on the lease at the well head. When that became unbundled, a third party system was formed to pick up the gas from the wells and move it to some intermediate stage to be sold to the sales company. The sales end of it is fine but the problem is the middle area where the system that used to be owned by the purchaser is now owned by the producers or a consortium of producers.
- 02:20:10 **John Alke, Attorney, MDU**, said the issue in MDU's property tax protest is not the pipeline or the gathering lines. The issue is that the DOR is taxing Fidelity Exploration and Production Company as a centrally assessed property, which has not and has never been a pipeline company. Mr. Alke explained MDU's perspective of how the dispute arose and that MDU thinks this a situation of constitutional magnitude. MDU's opinion is that the Legislature must define what the appropriate place to divide between what is taxed at 12% and at 3%, so that the local taxing jurisdictions will get what they are entitled to.
- 02:24:38 **Jerome Anderson, Encore Acquisition Company**, spoke about natural gas flow lines going across county lines. Mr. Anderson said if there is a change in how flow lines and collecting systems are taxed, it would uproot the whole oil and gas production system in the state. He said it would quadruple the taxes paid by Encore Acquisition and would be a tremendous financial burden.
- 02:28:01 **Ed Diemert, Liberty County Commissioner**, said that the Legislature needs to come up with legislation to resolve the issue of property tax classification. Mr. Diemert said that lawsuits are not the way this should be addressed and that if changes are made, the Legislature must consider the tax consequences to other taxpayers.

- 02:29:31 **William Duffield, Executive Director, Montana Association of Oil, Gas, and Coal Counties**, said that surrounding states do not have this problem and suggested that the Committee study the taxation methods.
- 02:30:07 SEN. TOOLE asked if Mr. Duffield if he has talked with his clients about taxation rates and said one solution would be to lower the tax to 3% and having it all locally assessed. Mr. Duffield said local governments would not be happy with that solution but that they may be willing to compromise in order to gain some stability and predictability.
- 02:31:35 SEN. ELLIOTT said the Committee must decide if it wants to approve the study plan and recommended adopting it tentatively.
- 02:32:29 SEN. BLACK said he would like a study done of the tax consequences to the local counties.
- 02:33:30 Mr. Martin said the study plan will address SEN. BLACK's concern and referred to items 6 and 7 on page 7 of the study plan. SEN. BLACK said because of the potential tremendous effect, that he would like it to be more specific to the impact on a county.
- 02:34:56 SEN. BLACK asked to have the words "and the taxing jurisdictions, including the county and state" added to the end of item 6 on page 7 of the study plan.
- 02:36:24 SEN. TOOLE said he is interested in seeing what the property tax percentage impact is on the commodity price. He said he is not clear on what the change would be in market value/commodity price.
- 02:37:13 REP. LAKE supported doing the study but not in the terms of how it will affect one county, but to emphasize that a consistent and fair system be established. The Legislature's job is to make sure it is equitable, fair, and consistent. REP. LAKE **moved** to tentatively adopt the study. REP. COHENOUR asked if the motion included the suggested changes. REP. LAKE said he did not support including the changes. SEN. BLACK said the information would be used only to determine the ramifications of the policy.
- 02:40:09 SEN. KITZENBERG did not support moving forward with the study, saying that in his opinion, he doesn't see this as fair taxation.
- 02:41:39 SEN. ELLIOTT said there is no preconceived result of the study and that the study will not be done to produce a certain result. It is a matter that needs to be looked at.
- 02:42:27 REP. COHENOUR **made a substitute motion** to amend the motion to include the counties and the fiscal impact in the study plan.
- 02:42:50 The substitute motion to tentatively approve the study plan with the suggested changes **passed on a unanimous voice vote**.

SB 276 - REVISED TAXATION OF BENTONITE

- 03:03:35 Mr. Martin reviewed the changes made by the 2005 Legislature regarding the bentonite tax. He said the problem arose because appropriation bills cannot be introduced in the Senate and so it did not have the necessary appropriation. The House did not make the appropriation, so the counties can't receive their share of the tax. Mr. Martin said the Governor has proposed a budget amendment under the emergency provision.
- 03:05:54 **Amy Sassano, OBPP**, said the Governor's Office feels it is appropriate to use the budget amendment statute to fund SB 276 [Title 17, ch. 7, part 4, MCA] Mr. Martin raised the question of whether this is the appropriate solution. He said that the budget amendment will be submitted to the Legislative Fiscal Division for review. The Legislative Finance Committee does not have the authority to approve or disapprove the amendment.
- 03:08:20 REP. LAKE asked if the lack of funding would revert the law back to the old tax structure. Mr. Martin said the law has been revised but there is not a mechanism to distribute the tax.
- 03:09:59 Mr. Martin said this will have to be addressed legislatively in the future.
- 03:10:16 SEN. ELLIOTT said he would accept blanket proxies and would like them in writing. He asked the Democratic members to give their proxies to him and the Republican members to give their proxies to REP. WAITSCHIES.

PROPOSED SCHEDULE FOR REVIEW FOR BUSINESS INCOME TAXATION

- 03:11:18 Mr. Martin presented a proposed schedule for review of business taxation topics ([EXHIBIT #18](#)).
- 03:14:37 REP. WAITSCHIES said he objected to using the word "avoidance" in the plan. He said it is perfectly legal. SEN. ELLIOTT asked if the DOR agreed. Director Bucks said it did.
- 03:15:21 REP. MCALPIN **moved** to adopt the proposed schedule. The motion **passed on a unanimous voice vote**.
- 03:16:21 SEN. ELLIOTT asked if the Committee should schedule additional two day meetings. After discussion, SEN. ELLIOTT said that the Committee would schedule one two-day meeting at a time, starting in February. Mr. Martin had copies of the committee budget available ([EXHIBIT #19](#)).
- 03:17:46 REP. MORGAN commented that for committee members who have to travel, two-day meetings are more economical.
- 03:18:31 Mr. Martin discussed the Committee budget. SEN. ELLIOTT said that he had contemplated subcommittees but after examining the budget, he no longer supports that idea. Mr. Martin said mileage has recently been increased from 45

to 48.5 cents per mile. SEN. ELLIOTT said the OBPP has asked that the Committee consider moving up the date of the next meeting, in order to prepare the revenue estimates in a more timely manner. He asked the Committee for permission to set the date of the meeting at the call of the Chair, suggesting November 17 and 18, 2005.

03:25:35 SEN. BLACK asked to have meetings on Wednesdays and Thursdays, instead of Thursdays and Fridays.

03:27:35 REP. MORGAN asked if a date for a special session has been announced. SEN. ELLIOTT said if the Committee has to have the revenue estimates done by mid-November, he guessed that a special session would be in early to mid-December.

03:28:27 REP. LAKE said the Governor has said he will not call a special session until the QSIC has completed its work. He asked if the Committee wanted him to continue attending the QSIC meetings. The Committee asked that he continue.

ADJOURNMENT

03:29:52 With no further business before it, the Committee adjourned at 5:07 p.m.

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