



**ROOTS OF SPRAWL II:**  
**SHARING THE TAX BURDEN**

Property taxes, urban sprawl *and* you

KALISPELL, MONTANA

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# TABLE OF CONTENTS

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<i>Chapter 1</i>	
TAXES, SPRAWL <i>and</i> YOU:	
How tax-shifting changes our communities.....	4
<i>Chapter 2</i>	
TAX SHIFTING:	
Why is this thing so heavy? .....	6
<i>Chapter 3</i>	
POSITIVE TAX SHIFTING:	
Solving the incentives puzzle .....	10
<i>Chapter 4</i>	
TOURISTS RIDE FOR FREE:	
Local “resort” taxes ease property taxes .....	12
<i>Chapter 5</i>	
LOCAL GOVERNMENTS :	
Can quibble or cooperate .....	14
<i>Chapter 6</i>	
FEDERAL GOVERNMENT HELPS:	
Flathead Valley’s tax burden .....	16
<i>Chapter 7</i>	
BIG BOX STORES:	
Are they tax-shifting in disguise? .....	18
<i>Chapter 8</i>	
STATE-SPONSORED SPRAWL:	
Taxpayers get fleeced .....	22
<i>Chapter 9</i>	
POWER DEREGULATION:	
Higher power bills and higher taxes .....	24
<i>Chapter 10</i>	
SHARING THE BURDEN	
.....	26
<i>Chapter 11</i>	
MONTANA TAX REFORM	
The Time is Now.....	28



# 1

## TAXES, SPRAWL *and* YOU

### How tax-shifting changes our communities

**TAXES!** Property tax. Income tax. Excise tax. Sales tax. Americans love to hate taxes. Americans have protested taxes ever since the Boston Tea Party, at the same time knowing taxes are necessary for democracy to function.

Voters frequently complain about being over-taxed. Politicians have responded by promising to cut taxes and cut government. They pledge to pinch pennies, swing the budget ax and look out for the folks who pays the bills. Such promises sound good and win votes.

Yet, our taxes keep climbing.

In Flathead County, Montana, for example, our property taxes have out-paced population growth during the boom years of the 1992-97. In that half-decade, our population grew by 22.6 percent. Yet on average, homeowners' local property tax bills climbed by 65 percent. Ouch! No wonder voters complain about their taxes.

We often demand our elected officials lower taxes. But we don't ask, who is receiving these tax breaks? And who is left to carry the burden of paying for our government?

Too often, politicians play an elaborate shell game. That is, they cut taxes for one segment of society, but shove the tax burden on other portions of the public. This phenomenon is called **tax shifting**. There are winners *and* losers.

In recent years in Montana, tax shifting has meant homeowners, in particular homeowners in cities, pay a steadily increasing share of the total tax load.

Tax shifting impacts us all in many ways. Most obviously, it hits the losers in the wallet. It also hits our communities. When the tax burden is unbalanced, taxes create incentives for sprawl and discourage smart growth. The goal of this document is to explain how subtle changes in Montana's tax laws help fuel the urban sprawl that is changing the face of Montana.

To do that, it will examine Flathead County. Flathead County has three incorporated cities: Kalispell, Whitefish and Columbia Falls. This report will also discuss Evergreen, a non-incorporated area along U.S. Highway 2 east of Kalispell, which includes residential, commercial and industrial uses.

Imagine you are on a hike with a friend.

Together, you have a tent, food, cooking gear, and other supplies to keep you safe and comfortable overnight. As you start your hike, you stagger under your backpack. Meanwhile, your so-called "friend" whistles, as he carries nearly nothing. What kind of friend is that?

Tax shifting works the same way. Society has a burden—taxes that pay for police, roads, fire and other services that keep us safe and comfortable.

Everyone who can help carry that burden should help carry it.

There's a question to ask: How is that tax burden distributed? *Let's take a look...*

*"Hey! This isn't fair"*



# 2

## TAX SHIFTING:

### Why is this thing so heavy?

Recently, the Montana Legislature has taken great pride in being “pro-business.” Legislators wanted to lighten the tax load carried by businesses. They said this would boost the state’s economy.

But watch out! If you’re a typical city homeowner, the new tax laws slipped the tax load into your backpack.

The result? If the new business tax breaks boosted the economy as the Legislature promised, the boost is hard to find. But it’s easy to see how the Legislature put a greater tax burden on the shoulders of Montana homeowners.

After the 1999 and 2001 sessions, Legislators could go home and claim they cut taxes for business. But did they cut taxes overall? Hardly. They mostly shifted a greater portion of the tax burden to homeowners.

#### FIRST, SOME BACKGROUND

Remember: Taxes do not exist in a vacuum. We tax ourselves because we want services from the government. From the dog pound to the Pentagon, government services cost money and the money generally comes from taxes. In a perfect world, business, homeowners, and other property owners would each pay their fair share.

The primary tool local governments—cities and counties—have to tax their residents is property taxes. When assessing these taxes, cities and counties must follow a formula set by the Montana Legislature.

The 1999 Legislature tweaked that formula, to benefit businesses.

Specifically, the Montana Legislature passed four tax reduction bills:

- Senate Bill 200, reduced the tax on business equipment tax from 6 to 3 percent.
- House Bill 174 reduced the tax rate on dams and other means of generating electricity from 12 to 6 percent.
- House Bill 228 reduced the tax rate on telecommunications property from 12 to 6 percent.
- Senate Bill 184 further reduced the residential and commercial real estate tax base.

Before the changes (in tax year 2000), the state’s total tax base was \$1.9 billion. Of that, the

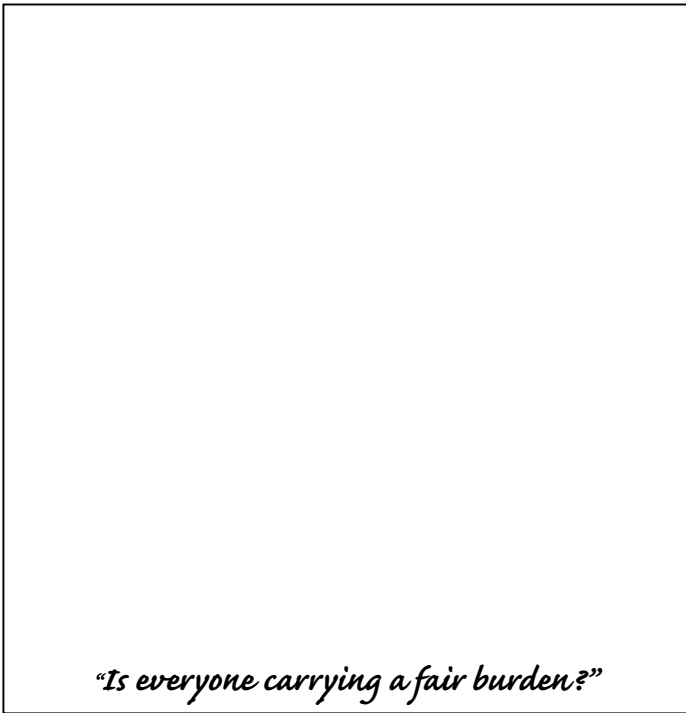
homeowner’s share was \$654 million or 34 percent.

After the changes, (starting in tax year 2001) the state collected about \$1.68 billion. But now, the homeowner’s share was \$669 million, or 40 percent.

The “reformed” tax laws trimmed the total tax base from \$1.9 billion to \$1.68 billion, statewide. In other words, \$221 million in business property was put off-limits for taxation or

taxed at a lower rate. That put more burden on the remaining property, particularly homes.

Because of the work of the 1999 Legislature, Montana homeowners are now responsible for 16 percent MORE of the tax base.



So did tax bills go down? For business, you bet.

But did the demand for government services go down? Not much, if at all. Growing numbers of Montanans wanted more and more services. Roads still need maintenance. Police are still necessary. In short, the tax burden was simply shifted to the homeowner.

*Does your pack feel heavier?*

## IMPACTS IN FLATHEAD COUNTY

So how much of the heavier load did you have to carry? Statewide, the average was a 16 percent increase in the tax burden carried by residential homeowners. But the specifics vary, from town to town. In general, the more your city depends on businesses for its tax base, the more taxes were shifted to homeowners.

In **Kalispell** before the tax shifting, homeowners were responsible for 38 percent of the city's tax base. Afterward, homeowners were responsible for 42 percent of the tax base. Adjust the figures for the shrinking total tax base and Kalispell homeowners saw an increased share of 9 percent. While that's a substantial increase, it is less than the statewide average of 16 percent.

But next, look at **Columbia Falls**, the self-proclaimed "industrial hub of the Flathead."

Traditionally, Columbia Falls depended heavily on local industry for its tax base. Before tax-shifting, Columbia Falls homeowners were responsible for 38 percent of the tax burden. Afterward, homeowners were responsible for 44 percent of the tax burden.

Again, adjust for the shrinking tax base and that comes to a whopping 17 percent increase in the homeowner's share of the Columbia Falls tax burden. That is above the state average of 16 percent.

**Whitefish** homeowners fared better than either Columbia Falls or Kalispell. Before tax-shifting, Whitefish homeowners were responsible for 60 percent of the tax burden. Afterward, homeowners were responsible for 64 percent of the tax burden.

Once again, adjust for the decreased tax base and Whitefish homeowner's share of the tax base grew by 6.5 percent. That's less than half of the statewide average of 16 percent, and lower than the other two

Flathead cities.

Whitefish homeowners enjoyed several advantages that spared them from the new tax bite. Whitefish has relatively little industry and thus depended more on its residential sector for its tax base in the first place. In short, there were fewer industries to give tax breaks to, so less slack for homeowners to take up.

Furthermore, Whitefish collects a local-option sales tax because it is a resort town. That allowed the city to refund 33 percent of real property tax back to taxpayers. (*More on that in Chapter 4.*)

So, faced with this new tax burden, what were cities to do? The Legislature gave local governments the option of changing the "mill" that is, adjusting the equation used to determine taxation. Columbia Falls and Kalispell took advantage of that. The result was even more taxes for homeowners in those cities. (Whitefish did not increase its mill rate, largely because it had an alternative revenue source through the local sales tax.)

Look more closely at Columbia Falls. After the tax equation was adjusted, the average homeowner there saw his or her tax bill jump 11 percent, that represented about \$50 per household.

Cities are left to look elsewhere for revenue as well. That means depending more on gambling revenues, user fees, and other, often "hidden," taxes. City councils are forced to raise those taxes and fees, or cut services. Or both.

So when politicians want credit for cutting taxes, the important question to ask is: Cut them for whom?

## IT AIN'T OVER YET

More tax storms are on the horizon for residential taxpayers. First, property is due for reappraisal in 2003. That will increase property assessments and potentially result in higher taxes. The 2001 Legislature did little, if anything, to reapportion the tax load that they shifted to homeowners in earlier sessions.

When politicians brag of cutting business taxes they often use the rationale that such tax breaks will boost the economy and create more jobs. There's

one big problem with this argument: There's little evidence to support it. It's more likely that homeowners simply got stuck with a bigger tax burden and the economy remained just as crummy as before.

### **THE SPRAWL CONNECTION**

So what does this have to do with urban sprawl? Well like they say in the movies, follow the money.

Sprawl is at least in part an economic phenomenon. All other things equal, folks build homes where it's cheapest. Taxes are a big part of those costs. Tax shifting made it even more expensive to own a home in one of the cities. That's more incentive to build in the rural outlands, to avoid paying those taxes.

The result? The shifting of property taxes from businesses to homeowners is part of the financial equation that leads to sprawl.

## **BREAKS FOR BUSINESS**

### *But what about you?*

During recent Montana legislative sessions, lawmakers cut taxes for businesses. Here's how that merely shifted taxes to the backs of homeowners.

In the name of boosting the economy, lawmakers cut taxes on utilities, airlines, railroads. Lakeshore property owners also saw a decrease in the percentage of the tax burden they are expected to carry.

Perhaps the Legislature's most dramatic move was phasing out the tax on business equipment.

Business equipment went from being 11 percent of the property tax base to zero percent. These tax cuts are being phased in. They aren't in full effect yet, but are scheduled to be in a few years. Legislators can go home to brag that the total amount of taxes collected went down.

But that fails to tell the whole story. The devil hides in the details. The tax base was cut, but demands for services remained. Someone had to carry the weight.

After the legislature reworked Montana's tax laws, homeowners and farmers were left to pick a larger share of the tax burden. Taxes were shifted. The full impact of tax legislation passed in the 2000 Legislature may not be fully felt until well into this decade.

Legislators knew the new tax laws could increase the property taxes homeowners pay for local government.

So lawmakers wrote in tax reimbursements for local governments to use as they saw fit. Local governments could have used these reimbursements for additional tax relief. And in Whitefish they did. (See associated article on the resort tax.)

For Flathead County, these reimbursements amounted to \$700,000 for general tax relief in the 2001 budget year and \$100,000 for the road department.

The city of Kalispell received \$79,000 in tax aid.

But did that equate to lower taxes? Well, no.

Instead of lowering taxes by lowering the mill levy, Flathead County and the city of Kalispell raised their mill levies by 7% each, basically nullifying any tax relief from the legislature.

Elected officials often brag that they have held the line. They say taxes have not increased. Business owners may look at their business taxes and agree. Homeowners, on the other hand, read their tax bills and see their taxes have gone up.

Bingo. That's tax shifting.



# 3

## POSITIVE TAX SHIFTING:

### Solving the incentives puzzle

Harvard University urban planning professor, Alex Kreiger, boils sprawl down to simple economics:

In his words, people migrate to the periphery of cities “to find more housing for less money.” He continues: “Until this advantage is neutralized, sprawl will remain our future.”

Some of the price differences between property inside a city and on the outskirts is the result of free market dynamics, such as the availability of land. But government policy is another part of this puzzle. And government policy usually plays out in tax policy.

Property owners within Kalispell city limits must pay taxes to both the city government and the county government. Property owners outside city limits need only pay to the county.

The difference is considerable. Say you owned a piece of property on the very edge of the city and your neighbor owned an exact replica of that property, just outside of the city.

All other things equal, your general or local tax bill will be 89 percent higher than your out-of-town neighbor. (This does not count taxes for schools.) Say your property is worth \$1 million. You would pay \$3,500 more in taxes than your neighbor just beyond the city limit. That’s a sizable annual savings.

The tax saving is even greater for some businesses. Around Kalispell for example, land on the outskirts of town is appraised at roughly half the value of land downtown. That combination is a big tax savings for those who build in the outskirts of town. All in all, it’s a powerful incentive to sprawl.

The unincorporated commercial strip that defines Evergreen is the manifestation of tax legislation that feeds sprawl. Businesses move to Evergreen, in part because of the highway frontage, but also in part

because it’s cheaper to operate a business there than it is in the city, because of lower taxes. Evergreen has little infrastructure besides roads, water and sewer. The result is a place with no sense of place.

Furthermore, businesses and homes immediately outside city limits still tend to rely on city services. (For example, interagency agreements might often send city police and fire crews are called outside city limits.)

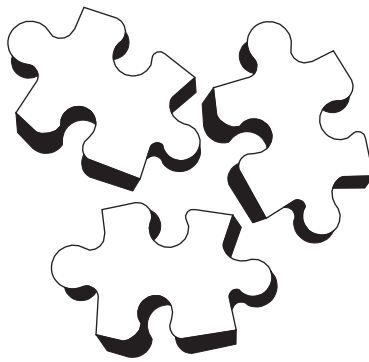
Imagine if cities could erect toll booths, collecting quarters from rural residents every time they used city streets, sidewalks, parks, parking lots, police protection and so on. Those city booths would collect a lot of quarters. Rural residents would soon see just how much they rely on city services.

Of course, no city is going to erect toll booths. But there are other ways to collect fair payment for out-of-town residents who use city services. By examining the underlying incentives, and adjusting the taxes or fees, municipalities can actually entice freeholders to become part of the city.

Whitefish offers another picture entirely. After giving city property taxpayers a resort tax rebate, Whitefish levies 73 percent less taxes than Flathead County and 88 percent less than the city of Kalispell. Whitefish has minimized the financial incentive to locate onto the strip.

In fact, the average Whitefish resident with sewer and water pays some 6 percent less annually in real taxes and fees, than does a counterpart in the county paying for the same services. In addition cities generally provide services not available in the county. (Quicker police response, for example, or more convenient garbage collection and the like.)

With that scenario, the incentives do not favor sprawl, but rather encourage development to become a part of the city.



# GOOD DESIGN MEANS GOOD BUSINESS AND A STRONGER TAX BASE

The distinctive character of our cities is a point of pride for city residents and an important anchor for local businesses.

This is particularly important in a place where we depend heavily on the tourism economy. Visitors come to the Flathead Valley because it is different, or even unique. No doubt, our natural environment is unmatched, anywhere. However, our human environment is becoming more and more homogenized.

Haphazard development, however, can paint a city in “blah.” Cheap, blocky buildings that lack character tend to destroy a community’s distinctive appeal. They also result in a lower tax base, since property tax rates are based in part on the value of construction materials and quality of the design.

Design standards help equalize the tax burden. Under our current tax system, new box stores that rely on cheap construction and bland designs effectively get a tax break. Instead, we need tax incentives or design standards to encourage high-quality development.

Local communities have many tools at their disposal, to protect and enhance the character of their community\*:

- **Design guidelines** are aesthetic regulations based on the issues, needs and desires of the community. Guidelines may cover a development’s height, size, architectural style, materials and landscaping.
- **Design review** is a more rigorous process, by which a **design review board** studies proposed developments, to make certain the developments meet community standards.
- **Historic and neighborhood conservation districts** are more localized districts, designed to preserve the general character of a particular neighborhood. Neighborhood conservation districts are more flexible, allowing a wider variety of building styles and time periods than a historic district.

Communities also have a choice of strategies to choose from, to reach their design goals.

- **Education.** Workshops and other programs can introduce residents and leaders to the benefits of good design.
- **Honoring voluntary design efforts.** By offering awards or otherwise recognizing good design efforts, communities can encourage better design throughout their cities. Other voluntary efforts include organized painting, cleaning and restoration efforts.
- **Financial incentives.** Grants, matching funds, and tax breaks can all give businesses the boost they need to justify investing in good design. For example, Wisconsin, Oregon, Michigan, Minnesota and North Carolina all grant tax incentives for building design features and land conservation efforts.
- **Regulations.** Legislative guidelines address issues such as building design, commercial signs, layout and landscaping.

\* Source: Scenic America. Contact at 202-543-6200. Or visit [www.scenic.org](http://www.scenic.org).

# 4

## TOURISTS RIDE FOR *FREE*

### Local “resort” taxes ease property taxes

According to the rules of fairness, everyone pulls his own weight. In other words, people should pay for what they receive, as much as they can.

But when it comes to local taxes and services, one big component of the Montana economy essentially gets a free ride (or at least a dirt cheap one). These folks consume local government services without paying much at all in local taxes. These folks are tourists.

Some 2 million people a year visit Glacier National Park. Thousands more visit The Big Mountain or other attractions. That’s a huge influx of people, considering Flathead County has only 70,000 or so residents.

Tourists crowd the roads. Tourists call the police or fire department when they get into trouble. They leave garbage behind to be hauled to the landfill. They use our city parks and beaches. In short, tourists use public services.

We don’t mean to complain about tourists. They contribute to the local economy. But what do they pay in taxes? What do they contribute toward paying for those government services they use?

In most of the Flathead Valley, not much. We all are left to carry *their* tax burden. But it doesn’t have to be that way.



#### THE BED TAX DOESN’T HELP

True, there is a bed tax in Montana. Anyone who stays at a commercial campground, hotel or motel must pay a tax, per night. However, that tax does not go toward providing local services.

To the contrary. The bed tax money goes to the state tourism office. That bureau spends the money on advertising campaigns designed to *attract more tourists*. So when it comes to demands on services, the bed tax increases the demand without offering

anything to help pay for those services.

So what’s a city to do?

#### THE WHITEFISH EXAMPLE

Squeezed between a beautiful lake and a world-class ski hill, Whitefish is a prime example of a resort town. Yet Whitefish has been able to hold the line on property taxes. Meanwhile, the once-notorious Whitefish city streets are receiving a badly needed overhaul.

How did Whitefish do that? In part, Whitefish did it by getting tourists to pay a fair share of taxes for local services.

In 1995, Whitefish created a local option resort tax. In brief, the city collects 2 cents in tax on every dollar spent on “luxury” purchases within city limits. That includes restaurant meals, hotel rooms, retail goods and the like.

The law that created the Whitefish resort tax dictates that city property owners receive a property tax break because of the resort tax. Specifically, 25 percent of the money collected through the resort tax is funneled back into a property tax break.

The law also dictates that 65 percent of the money collected from the resort tax go to repair city streets, curbs, gutters and sidewalks. Some five percent is earmarked for parks and bike paths. Merchants can keep five percent of the tax to help pay for book-keeping and other costs related to collecting the tax.

In other words, the tax burden is being “shifted” off the backs of city homeowners and businesses and onto the visitors who use services.

As the new-and-improved streets of Whitefish attest, the program can mean benefits for financially strapped tourist towns.

In 2001, Whitefish will collect \$1.2 million through the resort tax. That funds a \$270,000 tax break for Whitefish property owners. Essentially, that's a 33 percent rebate on property taxes.

Not every city can impose a local resort tax. The authority for a city to start a local option tax comes from the Montana Legislature. So far, only small resort towns like Whitefish, West Yellowstone and Big Sky have such authority.

### **RURAL RESIDENTS ALSO USE CITY SERVICES**

Tourists aren't the only folks who are getting a free ride on city services. As we discussed in Chapter 3, rural residents often use city services without paying city taxes. The Whitefish resort tax helps balance that tax load, as well. When a rural resident goes out to dinner in a Whitefish restaurant, he pays a few pennies toward city services through the resort tax. This helps pay for the city services he uses.

Again, the resort tax works somewhat like that imaginary toll booth from Chapter 3, collecting a fair price for services used.

### **PLUSES AND MINUSES**

Everyone who spends money in Whitefish, not just tourists, must pay the resort tax. Sales tax have proven particularly unpopular in Montana, as they are seen as unfairly taxing the poor. Under a sales tax, the more you spend, the more you're taxed.

The poorer a family is, the larger percentage of their income they must spend. For this reason, sales taxes are sometimes considered "regressive."

In Whitefish, only "luxuries" are taxed, but the city was left to decide what was a luxury. Food and medicine, for example, are not subject to the tax, but books and restaurant meals are. Deciding what purchases are to be taxed or not taxed is bound to be controversial. Critics also allege the added cost of a sales tax may push some shoppers to towns without the tax.

Yet the resort tax has one great advantage: It allows cities to get some payment from the visitors they serve.

In 2000, Whitefish was able to hold the line on homeowners' property taxes. Kalispell had to raise residential taxes. So did Flathead County. The Whitefish resort tax doesn't explain that difference all by itself, but it is a big part of the picture.

Some officials in Kalispell have expressed interest in obtaining authority from the Montana Legislature to levy a local option tax. So far, the Montana Legislature has not given Kalispell the authority to do so.

Local option resort taxes are not a cure-all for the woes of city budgets. But they are something to think about, next time you're stuck in traffic on an over-crowded road, behind a slow RV.



# 5

## LOCAL GOVERNMENTS

### Can quibble or cooperate

Turf battles are nothing new in local politics. However, the budget arguments used to support these bureaucratic disputes are often thin and ragged.

In the end, cooperation between city and county governments is more efficient and fair than fragmentation.

Again, let's take Flathead County as an example. Flathead County has its county commission, while the cities of Kalispell, Whitefish and Columbia Falls all have their own city councils.

#### COOPERATIVE PLANNING OR FRAGMENTED PLANNING?

For decades, Flathead County had capable and cost-effective planning office called the Flathead Regional Development Office. The planning office merged the planning efforts of Flathead County and the three cities.

In 2001, the Flathead County Commissioners decided to bail out of the office, effectively undermining the cooperative planning process. The County Commissioners said they would do things their way.

The commissioners justify deserting the planning office by saying they are simply being responsible to their taxpayers. The commissioners frequently complained that the county ended up paying for planning efforts within the planning jurisdiction of the cities.

But wait. That sword cuts both ways. There remains an unasked question about the responsibility of elected officials to their taxpayers: "What do city residents get for the taxes they pay to the county?"

Cities have professional managers, trained in public administration, who are answerable to elected officials. However, the county is solely in the hands of three elected officials who tend to manage not along professional guidelines, but by political whim.

Lately, that whim has been an ideological swing toward the "protection" of property rights. The irony is, these lop-sided efforts often trample a neighborhood's collective property rights, in favor of the property rights of a single developer.

So while the cities and the county feuded over the planning office, city residents subsidized both sides of that battle.

#### CITY TAXPAYERS DESERVE COUNTY REPRESENTATION

In 2000, municipal taxpayers in Kalispell, Whitefish and Columbia Falls paid nearly \$3 million to county coffers. That's about 22 percent of all property taxes paid to Flathead County.

Plus, all those city residents paid city taxes. That is, they paid for city police, city dog catcher and city garbage collection.

At the same time, the city residents are paying for the county sheriff's office, the county dog catcher and the county garbage collection.

City taxpayers pay for 25 percent of county weed control, bridge fund, welfare, county fair, district court, employee salaries and benefits, county parks program, county library, county extension services, county search and rescue, Glacier International Airport, the port authority and more.

During the American Revolution, a battle cry was "No Taxation without Representation."

Yet in Flathead County, city residents are taxed by county governments—and seem to receive little representation from the county commissioners. While this "double taxation" is perfectly legal, it illustrates once again how the tax burden is carried by city homeowners, resulting in more incentives for sprawl outside city limits.



## LAW ENFORCEMENT

Let's look more closely at law enforcement, one of the basic duties of local government.

If a Kalispell resident finds his home burglarized, he calls the city police. Yet he is still taxed to support the county sheriff. Currently Kalispell, Whitefish and Columbia Falls taxpayers contribute \$800,000 annually, or over 25 percent of all property taxes paid into the county sheriff's budget.

The sheriff does provide benefits for the city police department, for example staffing and maintaining the jail. At the same time, the sheriff receives benefits from the city police, such as back-up during emergencies.

The cost of providing rural police protection is sure to increase, especially under current growth patterns. In Flathead County, about 75 percent of the growth is occurring outside city limits. That is, in the jurisdiction of the county sheriff.

In order to ensure the safety of county residents, there must be enough police staff to serve the population. As the general population grows, so does the need for law enforcement officers.

Unfortunately, the taxes paid by these new residents do not cover the increased expense of police services. Therefore, city residents end up subsidizing the growth of the county in rural areas.

## THE FLIP SIDE

There's another side to this coin. That is, people who live outside the city limits often exploit city services, without paying for them. This is another, more informal, form of tax-shifting.

Rural county residents may use the city parks or swimming pool, which they didn't pay for. While they may technically be in the jurisdiction of the county sheriff or rural volunteer fire department, they often receive services from city police and city fire departments. (This is because these agencies sign interlocal agreements to cover each other in emergencies. In theory, this goes both ways. But in fact, county offices have fewer resources, per citizen.



County services tend to be more strapped, so tend to need more help.)

Certainly, no one wants to let a crime go unpunished or a home to burn down, simply because of a jurisdictional line. But if sprawl continues unabated right outside a city, people on the outskirts get more than they pay for. In essence, the city dwellers are once again carrying an extra tax burden.

## WHAT TO DO?

As we saw with the fate of cooperative planning in Flathead County, some politicians are eager to draw sides and fight over our collective tax burden.

A more enlightened view, however, points to the fact that cities and county governments are all in this valley together. We can quibble over things like who is getting the best deal, or we can work together to make all local governments work as efficiently and effectively as possible.

Sometimes, elected county commissioners must be reminded they represent ALL the county's taxpayers, not only those in rural outlands. Because city taxpayers pay 25 percent of the commissioners' generous salaries, city residents should expect commissioners to respond to municipal needs. To do less would be, (as the patriots charged) taxation without representation.

## BALANCING THE LOAD

One way to lessen the burden on city taxpayers and to make sure that new development pays its own way is through impact fees. With impact fees, a new development is required to pay an additional

fee earmarked to cover the impact of that development on services such as fire and police protection and water and sewer service.

Annexation is another tool to help balance this burden. Yet current state law makes it difficult for cities to annex adjoining property, even though there is a growing need for police, sewer, water and fire protection. The 2001 Legislature established an interim committee to study this issue.

# 6

## FEDERAL GOVERNMENT HELPS:

### Flathead valley's tax burden

In a county and state where anti-government rhetoric often runs hot, it's important—and only fair—to point out how federal and state government provide to help carry Montana's tax burden.

While "the feds" often receive enormous blame for government policies, the federal government rarely receives credit where credit is due.

Between national parks and national forests, 85 percent of Flathead County is public land, managed for the benefit of all Americans by the federal government. Few places in the United States—and few other countries in the world—provide their citizens such a wealth of public land where we are able to camp, fish, hike and hunt for free or a minimal fee.

Public lands are also a major tourist draw, from Glacier National Park and The Bob Marshall Wilderness to the summit of the Big Mountain. Unlike national parks, portions of national forests are also open for timber, grazing and mining. A federal dam at Hungry Horse helps control our floods and federal fire fighting forces regularly protect our property from forest fires.

While we may dread sending a check to the IRS on April 15, Montana residents receive almost double their money back to our state and county from the federal government.

Specifically, according to a 1997 study by the Northwest Midwest Institute, for every \$1 that Montanans pay in federal taxes, we receive back \$1.76 from the federal government. The figure today may be even higher.

In other words, the "feds" we love to gripe about are carrying *our* tax load. Our county property taxes

would be considerably higher if we were to go it alone.

#### HOW THE FEDS CARRY OUR LOAD

The Montana Legislature sets a budget every two years. The last budget was \$5.8 billion for that two-year period. Of that, *47 percent* was from federal sources.

A big chunk of that budget is for roads. If you think Montana roads are bad now, imagine how they would be without the nearly \$260 million from the *federal* Transportation Endowment Act. That's money that goes straight toward improving our state highways. For every \$1 Montanans pay in federal gas tax, we receive \$2 back. That's a sweet deal.

But there's more here than roads. Additional federal dollars are funneled to human service programs on both the state and county level.

While the federal government doesn't pay county property taxes, *per se*, the feds instead pay "payment in lieu of taxes."

In Flathead County, payment in lieu of taxes added up to about \$1.48 million in 2001. These payments are derived from timber sales and other Forest Service revenue through the Secure Rural Schools and Community Self Determination Act of 2000.

Federal payments to Flathead County may soon be augmented by pending legislation called the Conservation and Reinvestment Act. This bill would send a portion of royalties from off-shore oil drilling to counties with public lands. This could

mean millions for Flathead County. The Conservation and Reinvestment Act passed the U.S. House of Representatives, with the support of Rep. Dennis Rehberg, R-Montana.



In the 2001 Montana Legislature, some lawmakers complained of the state's dependence on federal dollars. But with a tight state budget, no one moved to reject those dollars. As one legislator pointed out, regardless of whether money is state money or federal money, it's all "taxpayers' dollars." Our point is, Montanans benefit greatly from federal taxpayers.

### **KEEPING PROPERTY TAXES IN PERSPECTIVE**

Local taxes, usually means property taxes. That's because elected local officials (such as county commissioners) have more authority over property taxes than they do about income or other taxes.

No doubt, county property taxes can be painful. But they should also be kept in perspective.

Flathead County has a 2001 budget of about \$62 million. Of that, about \$13 million comes from current property taxes.

Of that \$62 million, about \$54 million will be spent and \$8 million will be kept in reserve. So out of total spending, property taxes will make up only about 25 percent of the county budget.

The rest comes from non-property tax sources. These include \$48.5 million in grants, fees and cash carryover from 2000. Cash carryover from 2000 totaled \$19.9 million. Of that, just about half was from was from previously levied taxes.

Fees are generated from the use of county soccer and baseball fields, garbage collection and disposal, library fines and the like. Basically, these are "user" fees paid for receiving a particular service.

Here's the bottom line: Property taxes cover only about a fourth of the cost of running Flathead County. Without federal support—via grants and payments—our individual tax burdens would be much heavier.

# 7

## BIG BOX STORES:

### Are they tax-shifting in disguise?

Competition is a cornerstone of economic policy in the United States. Healthy competition is said to encourage efficiency, creativity and reduce costs. All these, in the end, benefit the consumer.

But an equal cornerstone is fairness. In order for consumers and communities to benefit from competition, the playing field must be level.

More and more communities are questioning if the emerging dominance of big box stores constitute fair competition. They're asking this question: Does this new style of "competition" benefit local economies or simply bleed them dry?

First, let's define what we mean by a "big box" store. These stores typically range from 90,000 to 250,000 square feet. That is, they're two to five times the floor space of a typical downtown retailer. They tend to be owned and directed by large, out-of-state corporations.

Big box stores purport to offer a wider selection at lower prices. They boast of creating new jobs and increasing tax revenues for public services. Many of us assume this is true.

However, a growing list of studies contradict these assumptions. Like everything else in life, big box stores come with a cost.

These costs include a loss of community character and downtown vitality. Big box stores may cause an overall *decline* in the community's tax base.

In short, we're talking about another sort of tax shifting.

#### RESEARCHERS TEST THE ASSUMPTIONS

Stacy Mitchell is a researcher with the Institute for Local Self-Reliance and author of "The Home Town Advantage: How to Defend Main Street Against Chain Stores and Why It Matters." At a recent visit to Bozeman, she said:

"Study after study has found that new retail growth generally destroys about as many jobs and as much tax revenue as it creates. This is because retail spending is a relatively fixed pie. Growth in sales at one location will invariably be offset by declines in sales at existing businesses, many of which will be forced to either downsize their operations or close altogether."

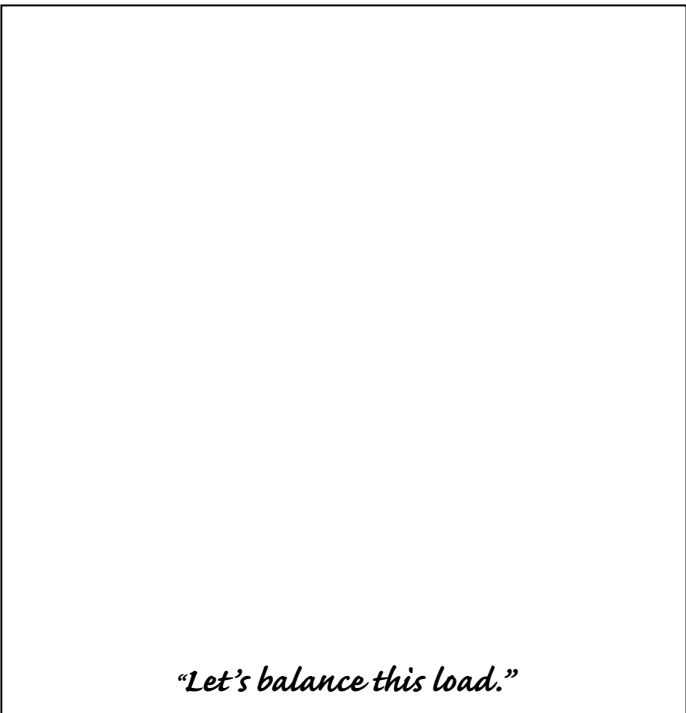
In other words, big box store may attract customers,

but those are customers lost by other businesses. The big boxes may hire people, but at the same time they force other businesses to lay off their workers.

Take the example of Greenfield, Mass. A study there found that a Wal-Mart expansion could cost existing merchants \$35 million in sales. The 177 jobs expected to be gained at Wal-Mart would be offset by the loss of 148 jobs at other businesses.

A Vermont study found

that big box stores would cause dozens of local businesses to close, leading to a net decline in overall retail employment. Similar conclusions have been reached in studies of big box stores in California, Maine, Minnesota, New York and Virginia.



*"Let's balance this load."*

## **BUT WHAT ABOUT TAXES?**

If new retail expansion fails to generate new jobs and new sales, but rather results in a net loss of current jobs and retail sales, the tax base gets hammered. The Flathead Valley may soon provide an example of this.

In the Flathead, retail sales total about \$875 million a year. Those dollars are generated by sales at existing stores, selling a wide variety of goods in a competitive atmosphere. The fast-growing population in the Flathead Valley may foster some retail growth as well. The key question is: How much commercial expansion does Flathead County need?

Let's examine one slice of the retail sector, the Flathead's building material and supply centers. As of 1997, some 87 businesses sold these kinds of goods. Their receipts exceeded \$132 million. They employed 742 workers with an annual average wage of \$21,700.

That's just the kind of scenario that attracts big box stores. Sure enough, Home Depot secured final approval to open a new 130,000 square-foot store just north of Kalispell.

When the big box Home Depot opened in Missoula, existing Missoula-area building supply stores saw a 25 percent drop in business, according to industry insiders. Another Home Depot, right in the Flathead Valley, will take a similar bite out of Western Building Center and other the 87 locally owned stores supplying building supplies. How big that bite will be is anyone's guess.

The typical Home Depot store depends on retail sales of \$44 million annually. That's about one third of the current home supply annual sales in the Flathead. While the Flathead Valley's population is growing, this growth is unlikely to generate \$44 million in new sales annually. Quite probably, someone's going to get squeezed out of the market.

Here are some points to ponder:

Where will Home Depot get the money to support itself?

What will happen to locally owned businesses like Western Building Center when Home Depot drops in on the Flathead Valley?

Will the change promote the health and general welfare of the community? And how will this impact tax burdens?

## **FINDING THE ANSWERS**

Answering these question is not simple. But these kinds of questions are the purview of local zoning bodies, such as county commissioners and city councils. Yet when Home Depot came to the Flathead Valley, no elected officials wanted to ask these tough questions.

By law, zoning decisions may not be used to regulate competition. However, zoning authorities have the legitimate power to maintain property values, protect tax revenues, provide stable neighborhoods, attract business and industry and encourage conditions which make a community a pleasant place to work.

Communities in other states are setting up zoning rules as they try to better understand and mitigate the impacts of big box stores.

Under these rules, large stores may be required to provide an objective, third-part economic analysis those stores have on a community. (The threshold for these big stores can be defined by floor space, automobile traffic or other measurable standards.) Ideally, these economic analyses would document how the big box store impacted the existing market and on local tax revenues and services.

Having such economic studies in hand is a first step toward planning and zoning for big box stores. That is, without taking these first steps, zoning restrictions are open to lawsuits from existing local businesses or developers.

## **BACK TO TAXES**

Tax base management is a critical issue here.

Local government zones specific areas for commercial development. When those governments decide to expand the total amount of land zoned for commercial uses, their decisions make a big difference.

For example, if the amount of land zoned commercial expands too quickly, it might flood the market. This leads to lower property values and reduced tax revenues. Governments may have to make that up by increasing taxes for existing home and business owners.

Nationwide, hundreds of communities have laws

that limit the size of new retail stores. These rules are aimed at managing problems like traffic congestion. But these communities have also learned their communities can absorb only so much new retail capacity, without bumping dozens of local businesses into bankruptcy. That's bad for the tax base and tax payers.

Some communities have set a ratio of commercial acreage to population. That ratio serves as a benchmark to trigger the need for retail expansion.

### **LOCATION, LOCATION, LOCATION**

Location of permitted retail expansion can also hammer tax revenues.

Taxes on land are based on location. In short, the farther a property is from downtown, the lower the taxes. This is a questionable policy that encourages businesses to sprawl away from existing business districts. Consider these three examples from the Flathead:

In downtown Kalispell in 1999, businesses were taxed at an average rate of \$7.25 per square foot for the land their stores are built on.

Meanwhile, just outside town, Wal-mart was taxed at \$2.75 per square foot for its land.

Next, consider Costco, three miles out of town. Costco was taxed at .25 cents a square foot for its land.

Businesses looking to cut costs go away from downtown. That's a recipe for sprawl.

It's also a recipe for tax shifting. New big box stores drain tax revenues out of the existing business cores. Local governments receive less money, yet have the same or more demand for services. Taxpayers get pinched again.

Fortunately, there's an antidote, as well. It's called "infill development." That is, land use plans which encourage new businesses to cluster around existing central business districts, instead of lax policies that allow sprawl at the whim of developers.

### **THE ART OF THE DEAL**

Cities often have architectural standards for new businesses. Cities benefit when they have a

nice appearance.

Big box stores often appeal to city governments for reduced architectural standards. This ploy saves the big box store money, but it costs taxpayers money.

Part of the reason is that taxes are lower on cheap, ugly buildings, because the assessed value is lower. So taxpayers get less out of the deal.

Buildings which lack enduring value and character often become a community liability when retail trends shift and businesses are left vacant. Flathead County has this in the concrete shell of an old Ernst building, which has stood vacant for years now. This type of deserted big box is a drain on the tax base, not a benefit.

Big box stores will also try to plead out of sidewalks, bike paths, landscaping, and road or stormwater infrastructure. The business again gets an annual tax break. Again, the community cumulatively becomes a less attractive and less desirable place to locate or live.

### **OTHER IMPORTANT AMENITIES**

Consider again the Home Depot that moved to Kalispell. Home Depot was willing to pay for expanding city sewer and water service to the store. But the company did not want to pay a fee to cover a portion of the rapidly approaching need for a new sewage treatment plant.

Home Depot was willing to donate land for a future fire station (and thus get a fat tax break). But the company did not want to help pay for a needed fire station. Impact fees need to be put in place to capture such costs, so they aren't unfairly shunted to the shoulders of existing taxpayers.

### **KISS YOUR MONEY GOOD-BYE**

Big box stores tend to drain money out of local economies through their centralization.

Locally owned stores tend to spend and invest locally. Out-of-town big box stores, however, create efficiencies by being centralized. This centralization means that many goods and services are contracted outside the community where the store stands.

Operators of big box stores tend to use international lending institutions, instead of borrowing from local banks. They tend to bypass the local media when developing their advertising. They tend to buy supplies nationally, instead of spending locally.

Studies by the National Trust for Historic Preservation reveal that locally owned businesses return 60 percent of their profits back to the community where it is rooted. But a typical chain store returns only about 20 percent of its profits back to the community.

### **IT'S ABOUT MORE THAN JUST MONEY**

Stacy Mitchell makes a strong case that locally-owned businesses build strong communities. She points out that local stores help maintain shopping districts designed for people, not cars.

Downtowns create a vibrant street life. When we go downtown—or visit some other shopping district we tend to bump into our friends and neighbors. Those chance encounters are important—they build a sense of trust and community.

Local stores most often reflect the local culture. They make the places we live special and distinct from all the other cities and towns in America. (If you want to know what local fish are biting, for example, you're far better off at a local tackle shop, instead of the mass-purchased sporting goods counter at the big box store.)

Locally owned businesses contribute to civic and cultural life by taking leadership roles in the community. Local businesses donate more than twice as much per employee to charitable organizations than do large companies.

Over the past two years the Flathead Valley has seen proposals floated for more than 1.5 million square feet of new retail development. That's enough floor space for 15 new Wal-Mart-sized box stores.

There are choices and creative tools for local governments. We should insist that our elected officials are both be pro-active and well-informed when they decide to approve or reject new retail expansion. To make decisions allowing large-scale expansion, without first doing any sort of economic analysis, is akin to shooting in the dark.

Our communities, our children, and our tax bills will all pay for our poor decisions.

“Change is inevitable,” says Stacy Mitchell. “We will have change whether we will it or not. But we'll have progress only if we channel the forces of change in directions that are compatible with our values and in ways that improve our lives.”

For more information, visit these websites: <http://www.newrules.org> and <http://www.sprawl-busters.com>

# 8

## STATE-SPONSORED SPRAWL:

### Taxpayers get fleeced

Across Montana, the state owns and manages land that is rapidly being converted from traditional uses like logging, grazing and cultivation to commercial and industrial purposes.

This trend has important—and often misunderstood—consequences for taxpayers. Beware. It can be another example of tax shifting. To illustrate this, let's take a look at one parcel, north of Kalispell.

On official maps, Montana is divided into 36-square-mile units called "townships." Each square mile within a township is called "section" and is given a number. Within each township, the 16th and 36th sections are state property. Congress granted these lands to the state at statehood, to help pay for schools.

One of those parcels, a Section 36, is located north of Kalispell. For 100 years, it was pasture and farmland. Now, Kalispell has grown around it. Its value for commercial development has become obvious.

The land is managed by the Montana Department of Natural Resources and Conservation. The agency's mandate is to make money for the state's school trust fund, often by leasing the state land. So it's no surprise the agency is eager to convert this land from agriculture to something that pays better.

As of the summer of 2001, the section was zoned agricultural and appraised at \$1 per square foot. The department insists the land "represents the highest valued farmland in Flathead County."

Yet with improvements such as water and sewer, the department figures the value of the land will jump four times, to \$4 per square foot. (The cost of commercial land in Kalispell varies. Downtown is assessed at \$7 a square foot. A developer recently assessed the fairgrounds at \$4 a square foot.)

The state wants to lease 60 acres of the section to a private technology park. Certainly, that could be good for the local economy and the school trust fund. But what does it mean for local taxpayers?

If the land is assessed at its current value as agricultural property (at \$1 per square foot,) the tech park land will be assessed at \$2.6 million. However, if the tech park land is assessed at the estimated commercial value, (at \$4 per square foot) it will be assessed at \$10.4 million. Remember, these are the numbers upon which the owner of the new tech park will pay property taxes.

There's a \$7.8 million difference between the two assessments.

That's quite a difference. But to tell the truth, if the land were private property, it wouldn't be that big a deal. If the land were private, it would be reassessed in January 2003 and changed from agricultural to commercial and the owner would pay taxes similar to other businesses in the community.

However, the rules are different for state lands. Private land is reassessed much more quickly than state land. Because of lease stipulations, Section 36 may not be reassessed for another 20 years. For every reappraisal of state land, a matching parcel of private land will be reassessed three times.



In short, without reappraisals, the department is locking in the appraised valuation at \$1 per square foot, through 2020.

As a result, the developer is poised for a very substantial tax advantage. And the rest of us taxpayers can be left carrying the tax burden. Elsewhere in the Flathead Valley, investors are offering business park development in Evergreen, Creston and Whitefish. These developers won't get the kind of tax break the state land developer is due to receive. How fair is that?

Under the lease for Section 36, there is only a limited provision to assure that local taxes generated for this land will cover the costs of services provided by the city of Kalispell and the local school district. Repeatedly, the Department of Natural Resources and Conservation has insisted that it does not fall under the mandate of the city. This could cost Kalispell school and municipal taxpayers millions of dollars over the next 20 years.

Clearly, the future of Section 36 is not agricultural. The land should be appraised with an eye towards its real future. That is, a mix of business, light industry, schools and homes.

When developers of state land play (and pay) by

different rules than developers of private land, there are ripple effects. In this case, there is more incentive to develop state land, drawing business out of the downtown.

The Land Board entered into an agreement with Kalispell which outlines that private use of the state land is subject to a "beneficial use tax." What they fail to agree on is what cycle reappraisals will occur and whether the Department of Revenue will perform the assessment. This type of "beneficial use tax" would be consistent and competitive with private lands. The state agency has full charge of assessing all property subject to taxation and equalizing values. The appraisal should follow statutory and administrative guidelines, as assessed for private property and be based on land use.

The Department of Natural Resources and Conservation could tweak the proposed lease to level the playing field. But until they do, the rest of us will have to shoulder up and make up the difference, carrying a larger portion of the tax burden as this project phases in over this decade.

Because similar parcels of land exist throughout Montana, this scenario is poised to repeat itself well beyond the Flathead Valley.

# 9

## POWER DEREGULATION:

### Higher power bills and higher taxes

Montana's swan-dive into the pool of an unregulated power market has proven to be controversial. As power rates skyrocket, there's plenty of blame going around.

But one element of power deregulation has been largely overlooked: The fact that power deregulation left homeowners shouldering \$32 million more of the state's property tax burden. That burden comes on top of higher power bills and in addition to layoffs and shut-downs in energy-hungry industries like the Columbia Falls Aluminum Plant.

In other words, a side-effect of deregulation is tax-shifting. As a home owner, your property tax bill will likely take a sizable jump. If you rent, expect to pay it through the monthly payments to your landlord.

Here's the deal: In the decades before 1999, Montana's power system was tightly regulated. In 1999, the Montana Legislature—led by the Flathead Valley delegation—decided to end all that.

Trusting that the free market would better serve Montana and working closely with the industries themselves, the Legislature began erasing the rules that had governed the state's power marketing, production and distribution system.

Suddenly, after years of regulation, those institutions (such as Montana Power Co.) were at the mercy of the free market. To give those institutions a softer landing, the Legislature cut their tax rates in half on property such as dams and coal-fired power plants.

These actions are having enormous consequences for local government and schools. While local governments are continuing to provide services, their

tax bases have been significantly reduced. As a result, the deregulation tax cuts means a massive tax shift onto other property taxpayers. Mainly, that means home-owners.

In 1999, before the effects of deregulation, homeowners shouldered about 34 percent of the total property tax burden statewide. After deregulation, homeowners shouldered 40 percent. (In 2001, the number will be about 41 percent.)

Again, in 1999, utilities carried about 30 percent of the property tax base. Today, utilities account for a mere 24 percent.

After one adjusts for the smaller size of the total tax base, 19 percent of the tax burden was shifted from the utilities to the homeowners.

The tax shift isn't over yet. Power companies have already seen a 50 percent reduction in their tax

rates for "tangible" properties, such as dams and power plants. But more tax breaks are still being phased in. Next year utilities will get a tax break on so-called "intangible" property, such as licenses, stocks, bonds and the like. Homeowners can prepare for a bigger tax load, to make up the difference. Again, many

of these laws were the handiwork of Flathead's delegation to the Montana Legislature.

In short, power deregulation handed power companies a \$32-million tax cut. By and large, home-owning taxpayers are left to pick up the difference.

That's tax-shifting, in a big way.

Unfortunately for homeowners and small business, most of the Legislature's recent tax cuts were



given to big businesses—particularly big businesses that were formerly publicly regulated utilities. Since the demand for government services has remained steady, those reductions have done little to benefit families, family-owned businesses or the self-employed. Those folks have simply had to pick up the burden dropped by the power companies.

This story doesn't end with power deregulation.

The Montana Legislature has also recently deregulated the telecommunications industry. Tax shifting resulting from telecommunications deregulation resulted in \$15 million less money collected from that industry. That's money that other property taxpayers will have to pick up. Count that \$15 million on top of the \$32 million from power deregulation, and one begins to see some of the hidden costs of deregulation.

## THE MONTANA TAXPAYER'S BILL OF RIGHTS.

(From 15-1-222, Montana Codes Annotated)

The Department of Revenue shall in the course of performing its duties in the administration and collection of the state's taxes ensure that:

- (1) the taxpayer has the right to record any interview, meeting, or conference with auditors or any other representatives of the department;
- (2) the taxpayer has the right to hire a representative of the taxpayer's choice to represent the taxpayer's interests before the department or any tax appeal board. The taxpayer has a right to obtain a representative at any time, except that the selection of a representative may not be used to unreasonably delay a field audit that is in progress. The representative must have written authorization from the taxpayer to receive from the department confidential information concerning the taxpayer. The department shall provide copies to the authorized representative of all information sent to the taxpayer and shall notify the authorized representative concerning contacts with the taxpayer.
- (3) the taxpayer has the right to obtain tax advice from the department. The taxpayer has a right to the waiver of penalties and interest, but not taxes, when he has relied on written advice provided to him by an employee of the department.
- (4) at the discretion of the department, the taxpayer has the right to pay delinquent taxes, interest, and penalties on an installment basis. This subsection applies only to taxes collected by the department, provided the taxpayer meets reasonable criteria.
- (5) the taxpayer has the right to a complete and accurate written description of the basis for any additional tax assessed by the department;
- (6) the taxpayer has the right to a review by management level employees of the department for any additional taxes assessed by the department;
- (7) the taxpayer has the right to a full explanation of the available procedures for review and appeal of additional tax assessments;
- (8) the taxpayer, after the exhaustion of all appropriate administrative remedies, has the right to have the state tax appeal board or a court, or both, review any final decision of the department assessing an additional tax. The taxpayer shall seek a review in a timely manner. A taxpayer is entitled to collect court costs and attorney fees from the department for frivolous or bad faith lawsuits as provided in 25-10-711.
- (9) the taxpayer has the right to a full explanation of the department's authority to collect delinquent taxes, including the procedures and notices that are required to protect the taxpayer;
- (10) the taxpayer has the right to have certain property exempt from levy and seizure as provided in Title 25, chapter 13, part 6, and any other applicable provisions in Montana law;
- (11) the taxpayer has the right to the immediate release of any lien the department has placed on property when the tax is paid or when the lien is the result of an error by the department;
- (12) the taxpayer has the right to assistance from the department in complying with state and local tax laws that the department administers; and
- (13) the taxpayer has the right to be guaranteed that an employee of the department is not paid, promoted, or in any way rewarded on the basis of assessments or collections from taxpayers.

# 10

## SHARING THE BURDEN

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Often times, people put land use and planning issues in one box, and taxation issues in another. As we have illustrated in this document, land use planning issues and tax issues are blended together.

The first step in resolving any problem is understanding the issues surrounding it. Citizens For A Better Flathead has published *Roots of Sprawl* and “*Roots of Sprawl II*,” as an attempt to clarify and explain these often complex and inter-related issues.

There is more to striving for fair taxation than griping about government and public servants. The rights of taxpayers and the rights of communities are a fundamental part of the overall package called “property rights.”

Citizens For A Better Flathead has advocated smart growth in the Flathead Valley for almost a decade. It is a group of citizens dedicated to protecting the unique quality of life that is still possible in the beautiful, fast-growing Flathead Valley of northwestern Montana. Citizens is a non-profit organization whose mission is to promote sustainable development and economic diversity through comprehensive, citizen-driven planning, thus protecting the ecology and culture of the Flathead.

We would like to thank the Turner Foundation and the Bullitt Foundation, along with the members of Citizens For A Better Flathead, for making this report possible.

*“Fair and square.”*

# 11

## MONTANA TAX REFORM:

### The Time is Now

By Tom Towe

Virtually everyone agrees Montanas current tax system is unfair and should be reformed.

Yet, every comprehensive tax reform effort in the past 30 years has failed. We are further away from tax reform now than at any time since 1970. Why?

Tax reform is not a Democrat/Republican thing. Let me give you an example. In 1971, I was impressed with a bill introduced by Republican Matt Himsl of Kalispell. It would have replaced our states complex income tax with a very simple system Montana taxes would be a percentage of the federal tax. It was so simple it would require only a postcard tax return. Since federal income taxes were more progressive and updated, I was impressed.

That year, Republicans controlled the state House. Every Democrat plus one, Matt Himsl, voted for this bill, and it failed. The next year, the Democrats were in control. I introduced the same bill. Every Republican plus one Democrat, myself, voted for it, and it failed again.

Why is tax reform so hard to achieve? I submit the real reason tax reform has failed is that taxes are powerful instruments of social control, and neither legislators nor citizens can agree on how our society should be controlled.

The real motive of most tax reform proposals is a tax shift from one segment of society to another. When this fact is discovered by the voters, they vote it down. Thus, sales taxes are pushed by persons who want to shift a big part of the tax burden from the high and upper middle class to the lower-income and lower middle-class taxpayers. The same is true with a flat tax.

A more progressive income and property tax would shift more of the tax burden away from the lower-income and middle-income taxpayers to the large and wealthy corporations.

Perhaps it is time to admit that tax reform is never neutral. If our true motives are to produce a tax shift, we should admit it. I think it can be justified.

We are collecting taxes from people who have in-

comes of less than one-third the poverty level. Montanans pay income taxes starting at incomes of \$2,890 a year. In 1994, 15,714 persons with adjusted gross income of less than \$4,000 paid Montana income taxes. This is outrageous. By contrast, the federal income tax law does not even require a person to file a return until their income reaches \$6,800.

On the other hand, 33 Montana households with income in excess of \$150,000 per year paid no Montana income taxes whatsoever in 1994. Of those in the highest 10 percent income level, 123 do not pay any tax whatsoever. This is outrageous.

A Montana corporation that makes \$750 a year and a Montana corporation that makes \$750 million both pay the exact same rate of Montana income tax (Corporate License Tax), namely 6.7 percent. In view of the impact each entity has on government services, this is also outrageous.

Elderly people on moderate or low, fixed incomes must pay a huge percentage of their spendable income on property taxes on their home in comparison to a high-income person. This ought to be outrageous.

We need tax reform to shift the tax burden away from those who can least afford to pay the costs of government to those who can best afford to pay. Except for user fees, all taxes ought to be progressive.

There is another reason to make taxes more progressive. The rich are getting richer by leaps and bounds in this country, and the poor are getting poorer. As Ralph Stone says in the first issue of *The Provocateur*, the net worth of the top 1 percent of our country is greater than the combined net worth of the bottom 90 percent. Pay levels of the average corporate CEO compared to the average factory worker have increased from a ratio of 42 to 1 in 1980, to 209 to 1 in 1996. This is also outrageous.

I drafted a comprehensive tax reform proposal with the support and assistance of the American Federation of State County and Municipal Employees for the December 1993 special session. It was a good start. The legisla-

tion, which didn't garner enough support to be introduced, would have dropped 50,000 low-income Montanans from the income tax rolls. It would have given 70 percent of Montanans a tax reduction while still dropping the maximum income tax rate from 11 percent to 8.5 percent. (You can do wonders by repealing the federal tax deduction, which all but six states have already done.)

Under my proposal, the states Corporate License Tax would have been increased by 1 percent, putting it closer to the national average of 7.67 percent. It would have made this tax truly progressive by setting a lower rate for smaller corporations and a higher rate for big corporations.

And, it would have given an effective homestead exemption of \$15,000 on everyone's home. The property tax portion was revenue neutral by increasing the taxable rate from 3.86 percent to 4.5 percent. Nevertheless, all homes valued at less than \$80,000 would have received a reduction.

Unlike the so-called homestead exemption in House Bill 184 of the 1999 legislative session, which gives everyone an across-the-board 16 percent (in 1999) and 23 percent (in 2000) reduction, the homestead exemption in the 1993 proposal would have exempted the first \$15,000 of everyone's home. To those with a \$15,000 home, this is a 100 percent tax reduction. To those with a \$1 million home, this is a 1.5 percent tax reduction. This makes property taxes on homes truly progressive.

Finally, there was a commercial property and agricultural component of the bill. By giving a little to ev-

eryone, it was designed to attract support. Unfortunately, widespread support was elusive.

As mentioned before, good tax reform is necessary to shift taxes from those who can least afford to pay to those who are most able to pay. At the very least, we must stop the tendency over the past 20 years to do the opposite, namely to shift the tax burden from the wealthy to the low and middle income taxpayers.

One way to attain greater overall equity is to restore the severance tax on minerals to the levels that existed in the late 1970s. In other words, the states coal tax should be restored to 30 percent, the oil and gas tax should be 15 percent, and other minerals the same. These taxes are almost entirely exported, meaning they are passed on to people outside the state who are using the minerals.

Despite what some critics say, the severance taxes have not negatively affected jobs in Montana. The price of coal, oil, gas, gold or platinum often fluctuates more in one day than the total amount of the tax. If the price is so low that it is not economical to pump the oil and gas, or mine the coal or hard rock minerals, they should be left in the ground until the price does support their extraction. They will keep. They won't spoil.

Tom Towe is a Billings attorney and former state legislator who served four years in the House of Representatives and 16 years in the Senate between 1971 and 1994. While in the Legislature, Towe was chairman of many panels, including the Revenue Oversight Committee and the Senate Taxation Committee. He sponsored a wide variety of legislation during his tenure, including the bill that created the states Coal Tax Trust Fund.

**Price:**  
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