INDIVIDUAL AND CORPORATE INCOME TAX

BIENNIAL REPORT - THE MONTANA DEPARTMENT OF REVENUE

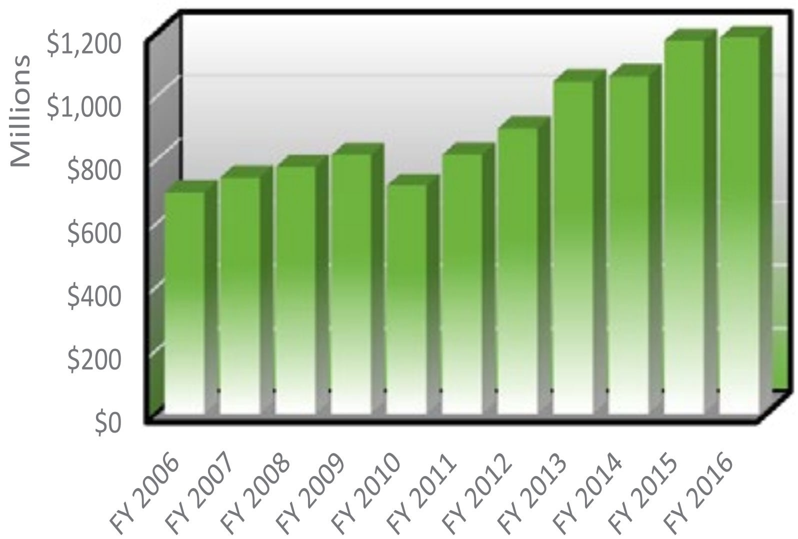
Overview of Individual Income Tax

The individual income tax is the largest source of state tax revenue. All income tax revenue goes to the state general fund, accounting for 56 percent of general fund revenue for FY 2016. Income tax revenue is collected primarily through withholding from wages and other periodic payments, quarterly estimated tax payments, and payments made when a return is filed.

The following tables show income tax revenue and return filings. Income tax revenue is closely related to the state economy. The large drop in revenue for FY 2010, which corresponds to the lower number of returns in 2009, is due to the national recession.

Individual Income Tax Collections

Fiscal Year	Total Revenue
FY 2006	$697,024,118
FY 2007	$743,940,547
FY 2008	$776,574,977
FY 2009	$815,138,193
FY 2010	$717,834,371
FY 2011	$816,089,973
FY 2012	$898,851,201
FY 2013	$1,047,789,985
FY 2014	$1,063,284,408
FY 2015	$1,175,744,881
FY 2016	$1,184,827,762



Income Tax Returns and Refunds
Timely Filed Current Year Returns

Calendar Year	Returns	Returns with Refund	Percent with Refund	Average Refund
2004	547,623	294,025	66%	$468
2005	554,224	297,993	66%	$491
2006	572,256	311,789	66%	$464
2007	591,874	345,972	71%	$506
2008	601,078	345,172	70%	$598
2009	587,425	337,714	70%	$545
2010	596,021	335,904	68%	$532
2011	604,758	341,057	68%	$538
2012	611,360	343,678	68%	$523
2013	626,655	348,137	67%	$532
2014	635,045	350,760	67%	$536
2015	647,329	357,902	67%	$546

Overview of Individual Income Tax

The legislature enacted the income tax in 1933 and has made major changes infrequently. The latest change was enacted in 2003 (effective 2005), and it reduced the number of rates, lowered the top rate, capped the itemized deduction for federal taxes, and provided preferential treatment for capital gains income.

Federal law provides different rate tables for married couples who file joint and separate returns, and couples generally have lower federal tax if they file a joint return. Most states either require couples to make the same choice between joint and separate returns as they did for their federal taxes, have different rate tables for joint and separate returns, or have a single tax rate so that the choice does not matter. Montana is one of only five states that do not have at least one of these provisions. Because of this, most two-income married couples find their tax is lower if they file a joint federal return and separate Montana returns. This is because, when they file separately, each spouse has the first $17,400 of taxable income subject to tax rates that are lower than the 6.9 percent top rate.

Montana also is one of only six states that allows a deduction for federal income taxes. Montana and two other states have a cap on the deduction, while the deduction is uncapped in three states. Most states do not allow this deduction because not having it allows lower rates. To raise the same revenue, a state that allows the deduction must have higher rates to compensate for the smaller tax base. The 2003 legislature partially offset the revenue reduction from lower rates by capping the deduction for federal taxes.

Most of the differences between Montana's income tax and the federal tax structure reflect legislative policy decisions, but a few are due to federal limits on state taxation. These state-specific features increase the department's costs of administering the income tax and complicate return preparation for taxpayers who are affected by them.

Before 1981, the legislature occasionally adjusted rate tables and other tax parameters for the effects of inflation. The 1981 legislature assigned this task to the department, and each year the department adjusts rate brackets, standard deductions, personal exemptions, and the partial exemption for pension income for inflation. This prevents increases in individual tax liabilities that are due simply to inflation. Without this inflation adjustment, a person whose income just kept up with inflation would pay higher effective tax rates over time as inflation moved them to higher rate brackets.

The following bills passed by the 2013 Legislature affected the individual income tax:
House Bill 444 created a refundable credit to private landowners who grant access across their property to state land that was previously inaccessible by the public. The credit is $500 per grant of access, with a maximum credit of $2,000 per taxpayer. This credit was first available in 2014.

House Bill 545 allows taxpayers to exempt employer-paid premiums for disability insurance that are considered taxable compensation under federal law. Federal law treats employer-provided benefits as non-taxable fringe benefits only if the same benefits are available to all employees. If certain employees, such as company executives, part-owners, or the highest paid employees, receive benefits not available to all employees, the extra benefits must be counted as taxable compensation for federal income tax purposes. The legislature previously exempted employer-paid health insurance premiums for select employees. This bill extended that exemption to employer-paid disability insurance premiums for select employees.

Senate Bill 15 changed taxpayer confidentiality law so that when a married couple files separate returns on the same form, the department does not have to obtain explicit consent from one spouse to discuss the return with the other spouse.

Senate Bill 108 renewed the tax credit for contributions to a charitable endowment fund and extended the sunset date to the end of 2019.

Senate Bill 117 expanded the deduction for family education savings accounts to include other states' college savings programs.

Senate Bill 179 requires partnerships with more than 100 partners to file returns electronically. These entities already were required to file federal returns electronically.

The following bills passed by the 2015 Legislature affected the individual income tax:
House Bill 122 clarified that the wages of agricultural laborers are not subject to withholding.

House Bill 359 changed the schedule for inflation indexing of the rate table, personal exemption, standard deduction, and partial pension exemption. Beginning in 2016, these numbers will be known at the beginning of the tax year, rather than two-thirds of the way through the year, as in the past.

House Bill 379 changed penalties and interest for late returns, late payments, or intentionally filing an inaccurate return to be more consistent with federal penalties and interest. It also reduced the time when the department may audit a return from five years to three years.

Senate Bill 175 expanded the credit for providing emergency lodging to victims of domestic violence. Previously, the credit was available for providing emergency lodging to an individual. This bill changed the wording to allow the credit for providing emergency lodging to a family.

Senate Bill 309 expanded the credit for allowing access across private land to isolated parcels of state land. It allowed the credit to be claimed for allowing access to national forest or Bureau of Land Management parcels.

Senate Bill 378 clarified the language exempting the military salaries of National Guard and Reserve members when they are called up for active duty or for homeland defense activity or a contingency operation.

Senate Bill 386 made changes to the circumstances where a pass-through entitiy is required to make payments on behalf of its owners. It also reduced the maximum penalty for a pass-through entity failing to file a return.

Senate Bill 399 created a new type of tax-deferred savings account to be used by families to pay expenses of an individual with disabilities. Deposits of up to $3,000 a year and earnings retained in the account would be exempt from state income tax.

Senate Bill 410 provides a tax credit for contributions to organizations that give scholarships to private school students or to a state account to fund grants to public schools for supplemental programs.

Calculation of Individual Income Tax
Calculation of Montana individual income tax begins with the taxpayer's Federal Adjusted Gross Income. Several adjustments are made to determine Montana Adjusted Gross Income:

- Income taxed by the state but exempted by the federal government is added,
- Income exempted by the state but taxed by the federal government is subtracted,
- Deposits to Montana tax-advantaged savings accounts are subtracted,
- Taxable withdrawals from Montana tax-advantaged savings accounts are added,
- Net adjustments from filing a joint federal return and separate state returns are added, and
- Recoveries of costs deducted in previous years (primarily refunds of federal taxes previously deducted) are added.

The values of the taxpayer's exemptions and either itemized or standard deductions are subtracted from Montana Adjusted Gross Income to determine Montana Taxable Income. The value of exemptions and maximum and minimum standard deductions are adjusted for inflation each year:

Personal Income Tax Exemptions and Deductions

		Single and Separate Returns		Joint Returns	
Year	Exemption Amount	Min. Standard Deduction	Max. Standard Deduction	Min. Standard Deduction	Max. Standard Deduction
TY 2012	$2,240	$1,860	$4,200	$3,720	$8,400
TY 2013	$2,280	$1,900	$4,270	$3,800	$8,540
TY 2014	$2,330	$1,940	$4,370	$3,880	$8,740
TY 2015	$2,330	$1,940	$4,370	$3,880	$8,740
TY 2016	$2,380	$1,980	$4,460	$3,960	$8,920

Tax liability is calculated from the rate table. The rate table shows tax rates to apply to taxable income, defined as income after making all federal and state adjustments and subtracting exemptions and deductions.

The rate table is adjusted for inflation each year: The following two tables show rate tables for the last five years. The top table shows the amount of income subject to each rate, and the bottom table shows the upper limit on taxable income subject to each rate.

Marginal Tax Rate Structure

Year	TY 2012	TY 2013	TY 2014	TY 2015	TY 2016
1% of the first	$2,700	$2,800	$2,800	$2,800	$2,900
2% of the next	$2,100	$2,100	$2,200	$2,200	$2,200
3% of the next	$2,500	$2,500	$2,600	$2,600	$2,700
4% of the next	$2,600	$2,700	$2,700	$2,700	$2,700
5% of the next	$2,800	$2,900	$3,000	$3,000	$3,000
6% of the next	$3,700	$3,700	$3,800	$3,800	$3,900
6.9% of remaining	NA	NA	NA	NA	NA

Marginal Tax Rate Income Limits

Year	TY 2012	TY 2013	TY 2014	TY 2015	TY 2016
1.0%	$2,700	$2,800	$2,800	$2,800	$2,900
2.0%	$4,800	$4,900	$5,000	$5,000	$5,100
3.0%	$7,300	$7,400	$7,600	$7,600	$7,800
4.0%	$9,900	$10,100	$10,300	$10,300	$10,500
5.0%	$12,700	$13,000	$13,300	$13,300	$13,500
6.0%	$16,400	$16,700	$17,100	$17,100	$17,400
6.9%	Unlimited	Unlimited	Unlimited	Unlimited	Unlimited

Any credits the taxpayer may claim are subtracted from the tax liability to give the net tax. Nonrefundable credits can partially or completely offset a taxpayer's tax liability. Refundable credits can more than offset a taxpayer's tax liability so that the taxpayer receives a payment from the state general fund rather than paying tax. Taxpayers with capital gains income are allowed a non-refundable credit equal to two percent of their capital gains. In effect, this taxes capital gains at a lower rate than other income. Other credits generally are a percentage of a certain type of qualifying expenditure the taxpayer has made.

The next six tables show information about individual line items on timely-filed full-year residents' income tax returns for 2014 and 2015. For each line item, the table shows the count of the number of returns with a value on that line and the sum of those values. The total in each counts column is the number of returns with a number on at least one line. It is not the sum of the counts for individual lines.

Information in these tables is from unaudited returns as filed by taxpayers. It does not reflect changes or adjustments that taxpayers or the department may make after the extension filing deadline. It also does not include information from late-filed returns.

Montana Individual Income Tax
Income Reported on Full-Year Residents' Returns
2014 and 2015

	2014		2015	
	Count	**Total**	**Count**	**Total**
Income Items				
Wage and salary income	433,860	$15,910,934,999	440,175	$16,520,002,142
Taxable interest income	188,849	$264,651,316	187,039	$264,049,935
Ordinary dividend income	118,288	$620,581,378	118,134	$658,927,043
Taxable refunds of state/local income taxes	96,880	$92,497,667	99,736	$98,401,855
Alimony received	826	$14,729,161	841	$15,034,681
Business income (Schedule C)	76,027	$832,531,763	76,826	$883,855,134
Capital gains income	116,541	$1,894,583,322	116,373	$1,617,311,845
Ordinary income gains	17,556	$115,716,046	16,685	$118,248,411
IRA distributions - Taxable amount	52,606	$678,714,872	54,851	$728,900,774
Pension and annuity income - Taxable amount	102,662	$2,049,981,285	104,003	$2,138,800,830
Rent, royalty, partnership, etc. income	103,395	$2,571,218,881	103,851	$2,693,443,364
Farm income	18,621	-$115,200,595	18,615	-$150,769,162
Unemployment compensation	26,990	$93,510,592	24,831	$89,447,741
Taxable social security benefits	84,871	$882,215,377	87,888	$941,215,493
Other income	39,067	-$509,350,776	34,012	-$513,477,324
Total income	550,969	$25,397,315,288	559,475	$26,103,392,762
Federal Adjustments to Income				
Educator expenses	10,962	$2,541,113	10,711	$2,485,117
Business expenses	731	$2,004,602	724	$2,133,283
Health savings account deduction	9,459	$30,938,095	10,274	$34,820,388
Moving expenses	3,225	$5,682,184	3,023	$5,389,616
One-half self-employment tax	63,364	$86,986,467	63,859	$89,922,276
Self-employed SEP, SIMPLE, and qual. plans	2,785	$48,366,605	2,779	$49,414,662
Self-employed health insurance deduction	25,117	$130,249,955	26,011	$138,208,738
Penalty on early withdrawal of savings	2,382	$327,070	1,989	$296,791
Alimony paid	1,201	$16,698,729	1,209	$17,776,094
IRA deduction	15,582	$65,989,731	15,410	$65,361,123
Student loan interest deduction	46,450	$43,632,382	47,936	$46,402,195
Tuition & fees deduction	5,361	$11,191,316	5,462	$11,481,274
Domestic production activities deduction	6,632	$47,706,540	6,760	$55,835,207
Federal write-ins	297	$2,131,234	279	$2,576,014
Total adjustments to income	143,766	$494,446,023	145,572	$522,102,778
Federal Adjusted Gross Income	551,025	$24,902,869,265	559,551	$25,581,289,984

Montana Individual Income Tax
Additions Reported on Full-Year Residents' Returns
2014 and 2015

	2014		2015	
	Count	Total	Count	Total
Montana Additions to Federal Adjusted Gross Income				
Interest on other states' municipal bonds	17,688	$81,908,740	18,832	$86,104,788
Dividends not included in FAGI	2,047	$3,075,020	1,045	$458,974
Taxable federal refunds	83,547	$113,016,677	82,262	$110,952,071
Recoveries of amounts deducted in earlier years	148	$171,099	156	$256,948
Additions to federal taxable social security or railroad retirement	9,114	$15,480,974	9,394	$16,463,896
Allocation of compensation to spouse	503	$8,295,571	439	$7,711,808
Medical savings account nonqualified withdrawals	87	$99,814	80	$135,323
First-time homebuyer's account nonqualified withdrawals	*	$4,177	12	$29,261
Farm and ranch risk management account taxable distributions	*	$2,200	*	$993
Dependent care assistance credit adjustment	39	$70,589	44	$71,893
Smaller federal estate and trust taxable distributions	63	$86,072	72	$158,314
Federal net operating loss carryover	5,298	$531,625,614	4,972	$534,457,235
Federal taxes paid by your S. corporation	42	$50,628	56	$3,414,954
Title plant depreciation	*	$725	*	$3,709
Group health premiums reimbursed by Insure Montana credit	504	$2,951,942	445	$2,531,387
Other additions	2,778	$17,145,098	2,584	$16,312,453
Total Montana Additions	110,201	$773,984,940	109,225	$779,064,007

Montana Individual Income Tax
Subtractions Reported on Full-Year Residents' Returns
2014 and 2015

	2014		2015	
	Count	Total	Count	Total
Montana Subtractions from Federal Adjusted Gross Income				
Federal bonds exempt interest	18,287	$20,115,632	17,738	$20,245,070
Exempt tribal income	5,970	$184,937,230	6,244	$204,787,286
Exempt unemployment compensation	26,990	$93,510,592	24,831	$89,447,741
Exempt worker's comp benefits	121	$852,638	138	$998,080
Capital gains from small business investment companies	20	$134,599	14	$48,730
State tax refunds included in FAGI	101,027	$95,370,321	99,736	$98,401,855
Recoveries of amounts deducted in earlier years	23	$121,364	15	$147,057
Exempt active duty military salary	4,592	$169,324,587	4,629	$170,649,803
Nonresident exempt military income	157	$5,918,182	142	$5,379,138
Exempt life insurance premiums reimbursement (National Guard)	35	$48,885	21	$10,766
Exempt pension income	46,021	$163,276,389	46,175	$164,186,433
Elderly interest exclusion	71,846	$29,772,557	73,739	$30,087,414
Exempt retirement disability income (under age 65)	27	$126,247	31	$137,022
Exempt tip income	16,988	$59,993,312	18,963	$67,147,671
Exempt income of child taxed to parent	141	$280,952	138	$329,513
Exempt health insurance premiums taxed to employee	165	$710,685	115	$439,835
Student loan repayments taxed to health care professional	347	$913,226	441	$1,234,654
Medical care savings account exempt deposits	7,838	$19,436,867	7,974	$19,574,075
First-time homebuyer exempt savings account deposits	194	$543,587	257	$678,938
Family education savings account exempt deposits	4,317	$10,075,735	4,504	$10,525,352
ABLE account exempt deposits*			0	$0
Farm and ranch risk management accounts exempt deposits	0	$0	0	$0
Subtraction to federal taxable social security/Tier 1 railroad retirement	38,836	$164,080,079	40,859	$178,175,443
Subtraction for federal taxable Tier II railroad retirement	3,057	$45,197,719	3,028	$46,343,176
Subtraction for spouse filing joint return: passive loss carryover	50	$169,507	47	$457,195
Subtraction for spouse filing joint return: capital loss adjustment	1,289	$2,998,655	1,052	$3,590,186
Allocation of compensation to spouse	518	$8,665,520	441	$7,724,717
Montana net operating loss carryover	3,607	$334,904,229	3,425	$352,681,058
40% capital gain exclusion on pre-1987 installment sales	36	$155,285	32	$134,842
Business expense of recycled material	114	$296,108	114	$240,929
Sales of land to beginning farmers	*	$7,094	*	$7,918
Larger federal estate and trust taxable distributions	208	$795,003	246	$844,234
Wage deduction reduced by federal targeted jobs credit	38	$210,071	54	$311,110
Certain gains recognized by liquidating corporation	*	$6,182	*	$9,121
Other subtractions	3,926	$176,308,440	3,958	$162,354,531
Total Montana Subtractions	245,200	$1,589,257,479	246,238	$1,637,330,893

* First available in 2015.

Montana Individual Income Tax
Deductions Reported on Full-Year Residents' Returns
2014 and 2015

	2014		2015	
	Count	Total	Count	Total
Deductions				
Deductible medical expenses	57,345	$278,443,929	57,479	$284,136,157
Medical insurance premiums not deducted elsewhere	108,363	$390,392,386	113,648	$481,950,204
Long-term care insurance premiums	13,563	$30,079,682	13,282	$30,500,607
Federal Income Tax				
Federal income tax withheld*	273,324	$1,926,973,266	279,246	$2,073,133,444
Federal income tax estimated payments*	50,758	$733,625,195	52,555	$841,786,294
Last year's federal income tax paid (e.g. with return)*	66,513	$441,240,323	73,199	$626,451,252
Federal income tax from previous years*	4,177	$19,351,145	4,277	$20,252,661
Total federal income tax deduction	302,524	$1,241,871,066	309,756	$1,297,118,744
State or local sales tax	374	$458,055	498	$530,408
Local income taxes	185	$122,793	409	$447,040
Real estate taxes	211,187	$438,433,548	217,088	$461,824,346
Personal property taxes	168,364	$55,086,743	171,030	$56,198,651
Other deductible taxes	22,368	$7,865,574	21,814	$7,480,154
Home mortgage interest	159,325	$881,049,492	163,415	$900,243,023
Qualified mortgage insurance premiums	22,329	$26,123,598	22,768	$27,804,697
Investment interest	8,876	$25,935,304	8,207	$26,452,670
Contributions by cash or check	168,354	$435,496,509	169,804	$450,272,008
Contributions other than cash or check	77,747	$79,790,146	80,273	$90,062,103
Carryover of contributions from previous years	3,160	$34,834,107	2,916	$35,565,096
Child and dependent care expenses	590	$1,189,970	516	$1,050,416
Casualty and theft losses	502	$5,096,735	357	$5,334,806
Business Expenses				
Unreimbursed employee business expenses*	57,765	$194,490,712	62,005	$192,414,280
Other business expenses*	140,332	$148,819,166	146,422	$155,491,877
Total business expenses*	162,301	$343,309,878	169,012	$347,906,157
Net deductible unreimbursed business expenses	57,719	$237,897,545	58,942	$239,235,527
Political contributions	8,895	$840,852	7,361	$684,847
All other miscellaneous deductions not subject to 2% floor	2,565	$3,898,851	2,103	$4,876,198
Gambling losses	1,515	$20,429,134	1,639	$22,570,063
Total itemized deductions	326,193	$4,195,336,019	332,811	$4,424,337,765
Unallowed itemized deductions (due to income over threshold)	9,767	$51,278,681	9,739	$55,925,179
Allowable itemized deductions	326,193	$4,144,057,338	332,811	$4,368,412,586
Standard deductions	204,979	$814,878,021	207,581	$830,313,297
Total deductions	547,242	$4,958,935,359	555,950	$5,198,725,883

* Items either are part of another line or include another line. They are not part of the total.

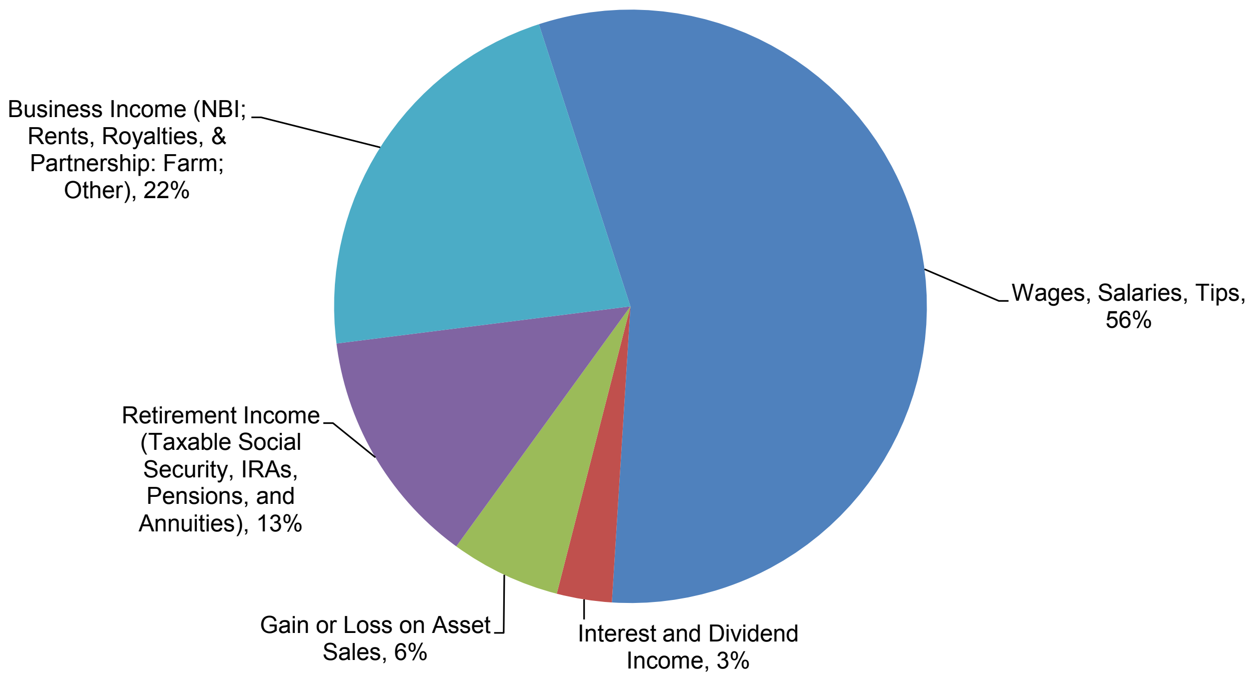
Montana Individual Income Tax
Exemptions, Taxable Income, Tax, and Payments Reported on Full-Year Residents' Returns
2014 and 2015

	2014		2015	
	Count	Total	Count	Total
Exemptions *				
Self Exemption		552,987		561,896
Self 65 and Over Exemption		106,840		111,289
Self Blind Exemption		1,060		1,097
Total Taxpayer Exemptions	552,987	660,880	561,896	674,248
Spouse Exemption		83,792		84,359
Spouse 65 and Over Exemption		22,784		23,818
Spouse Blind Exemption		237		231
Total Spouse Exemptions	83,792	106,812	84,359	108,391
Dependent Exemptions	129,682	233,850	131,172	237,033
Total Exemptions	552,979	1,001,541	561,862	1,019,648
Value of Exemptions		$2,333,406,460		$2,375,334,810
Taxable Income				
Federal Adjusted Gross Income	551,025	$24,902,869,265	559,551	$25,581,289,984
+Montana Additions	110,201	$773,984,940	109,225	$779,064,007
-Montana Subtractions	245,200	$1,589,257,479	246,238	$1,637,330,893
-Deductions	547,242	$4,958,935,359	555,950	$5,198,725,883
-Value of Exemptions	552,903	$2,333,406,460	561,677	$2,375,334,810
Montana Taxable Income	466,227	$17,939,369,911	473,570	$18,450,327,676
Tax from Tax Table	465,620	$1,019,130,334	472,962	$1,049,743,830
Capital Gains Credit	85,633	$38,921,806	83,266	$33,445,616
Tax before Credits & Adjustments	460,628	$982,495,961	468,244	$1,018,503,017
Tax on Lump Sum Distributions	38	$11,683	30	$7,539
Recapture of Credits Claimed Previously	10	$3,720	8	$1,570
Total Tax		$982,511,364		$1,018,512,126
Payments				
Montana income tax withheld from wages	438,851	$767,277,059	446,704	$807,033,685
Tax withheld from mineral royalties	2,927	$4,765,736	3,094	$2,374,281
Tax withheld by pass-through entities	293	$793,166	267	$377,157
Estimated tax payments	49,244	$195,992,483	51,255	$215,388,881
Extension payments	6,564	$33,766,399	5,780	$28,725,589
Total Payments		$1,002,594,843		$1,053,899,593

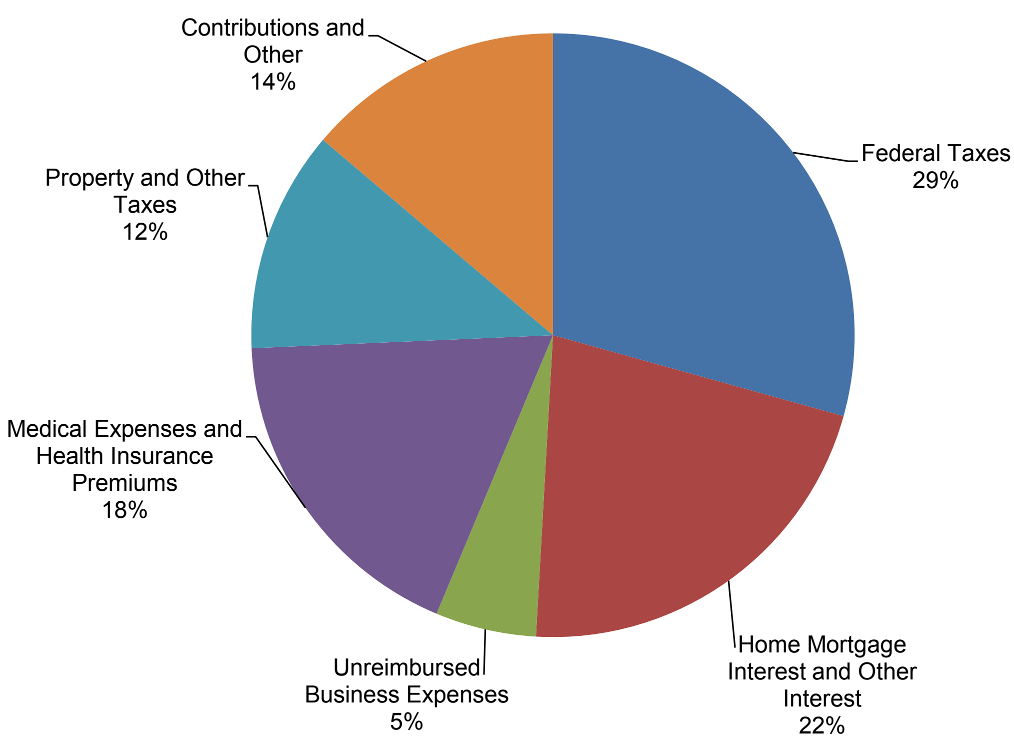
* Taxpayers claim exemptions for themselves and their spouses by checking boxes on the return. The counts for exemptions show the number of returns where the taxpayer claimed at least one exemption for themself, their spouse, or dependents. The totals column shows the number and type of exemptions claimed. For the taxpayer and spouse, the totals column shows the numbers of basic exemptions and extra exemptions for being 65 or over or blind. For dependent exemptions, the count is the number of returns claiming at least one dependent, and the total is the number of dependents claimed.

Montana Individual Income Tax Credits Reported on Full-Year Residents' Returns 2014 and 2015				
	2014		2015	
	Count	Total	Count	Total
Credits				
Non-Refundable and No Carryover				
Other states' income tax credit	13,763	$31,205,001	14,268	$31,375,448
College contribution tax credit	3,308	$285,949	3,438	$306,734
Qualified endowment tax credit	710	$2,471,140	689	$2,461,321
Energy conservation tax credit	11,514	$4,360,886	10,776	$4,176,132
Alternative fuel tax credit	17	$9,905	13	$8,189
Insurance for uninsured Montanan's credit	121	$121,701	74	$64,671
Elderly care tax credit	43	$59,626	41	$55,637
Recycling tax credit	104	$548,118	78	$279,657
Oil seed crushing/biodiesel facility credit	0	$0	0	$0
Biodiesel blending/storage tank credit	0	$0	0	$0
Non-Refundable but with Carryover				
Contractor's gross receipts tax credit	650	$5,391,186	608	$5,219,842
Geothermal systems tax credit	196	$238,535	187	$254,460
Alternative energy systems credit	525	$298,795	588	$258,247
Biomass alternative energy systems credit	579	$319,154	436	$195,343
Alternative energy production tax credit	*	$1,310	*	$11,597
Dependent care assistance credit	*	$13,528	14	$31,586
Historic property preservation tax credit	24	$443,810	19	$305,320
Infrastructure user fee credit	10	$27,269	13	$2,832,145
Empowerment zone credit	0	$0	0	$0
Research activities tax credit	*	$72,474	*	$72,462
Mineral exploration tax credit	0	$0	0	$0
Film production employment tax credit	*	$31,804	0	$0
Adoption credit	240	$257,945	229	$188,426
Total Non-Refundable Credits	30,246	$46,158,136	29,963	$48,097,217
Refundable Credits				
Elderly homeowner/renter tax credit				
Claimed with Income Tax Return	12,778	$6,065,006	12,854	$6,182,410
Claimed without Income Tax Return	3,922	$1,717,104	3,594	$1,560,728
Film production employment tax credit	*	$5,849	0	$0
Film qualified expenditure tax credit	*	$25,687	0	$0
Insure Montana small business health insurance credit	512	$1,423,875	447	$1,299,496
Emergency lodging credit	*	$500	*	$247
Unlocking state lands credit	*	$1,086	*	$1,239
Total Refundable Credits	13,295	$9,239,107	13,304	$7,483,239
Total Credits	42,408	$55,397,243	42,152	$55,580,456

Breakdown of Income Sources - Tax Year 2015



Breakdown of Itemized Deductions - Tax Year 2015



The following tables show Montana adjusted gross income, deductions, taxable income and tax liability by decile group for full year Montana residents. Each decile is 10 percent of the population of full year resident returns, sorted by adjusted gross income. Group 1 is the 10 percent with the lowest incomes, while group 10 is the 10 percent with the highest incomes. In these tables, married couples who file separate returns on the same form are counted as two returns, and their income and tax are counted separately. Non-residents and part-year residents are not included because their tax depends on the fraction of income that is apportioned to Montana, which varies widely for these individuals.

Deciles of Montana Adjusted Gross Income
Full-Year Residents
2014 and 2015

	2014				2015			
Income Group	Returns	Income Range	Montana Adjusted Gross Income		Returns	Income Range	Montana Adjusted Gross Income	
			$ million	% of total			$ million	% of total
1st Decile	55,298	less than $4,330	-$486.9	-2%	56,189	less than $4,273	-$546.8	-2%
2nd Decile	55,299	$4,330 to $1,028	$398.8	2%	56,190	$4,273 to $1,178	$407.3	2%
3rd Decile	55,299	$1,029 to $15,751	$712.0	3%	56,189	$1,179 to $16,102	$737.3	3%
4th Decile	55,298	$15,752 to $21,831	$1,036.4	4%	56,190	$16,103 to $22,475	$1,081.6	4%
5th Decile	55,299	$21,832 to $28,644	$1,390.8	6%	56,190	$22,476 to $29,442	$1,454.0	6%
6th Decile	55,299	$28,645 to $36,942	$1,807.7	8%	56,189	$29,443 to $37,785	$1,883.7	8%
7th Decile	55,298	$36,943 to $46,709	$2,304.3	10%	56,190	$37,786 to $47,667	$2,389.5	10%
8th Decile	55,299	$46,710 to $59,840	$2,922.0	12%	56,189	$47,668 to $60,920	$3,026.1	12%
9th Decile	55,299	$59,841 to $84,977	$3,906.6	16%	56,190	$60,921 to $85,596	$4,018.3	16%
10th Decile	55,299	more than $84,977	$10,095.9	42%	56,190	more than $85,596	$10,272.1	42%
Top 5% *	27,650	more than $116,055	$7,386.5	31%	28,095	more than $116,795	$7,502.7	30%
Top 1% *	5,530	more than $279,898	$3,766.0	16%	5,619	more than $283,345	$3,799.4	15%
Top 0.1% *	553	more than $1,069,675	$1,494.9	6%	562	more than $1,066,999	$1,466.7	6%
All	552,987		$24,087.6		561,896		$24,723.0	

* Included in 10th Decile

Deductions by Decile Group
Full-Year Residents
2014 and 2015

	2014					2015				
Income Group	% Returns Itemize	Itemized Deductions		Standard Deductions		% Returns Itemize	Itemized Deductions		Standard Deductions	
		$ million	average	$ million	average		$ million	average	$ million	average
1st Decile	34%	$131.8	$7,108	$84.6	$2,301	34%	$136.0	$7,058	$85.1	$2,306
2nd Decile	30%	$102.7	$6,271	$88.1	$2,264	30%	$106.0	$6,337	$89.4	$2,264
3rd Decile	38%	$145.4	$6,986	$99.0	$2,871	38%	$213.4	$10,048	$101.7	$2,910
4th Decile	40%	$175.1	$7,863	$125.5	$3,800	40%	$183.4	$8,188	$131.3	$3,885
5th Decile	46%	$213.5	$8,416	$135.7	$4,535	46%	$222.0	$8,646	$139.4	$4,568
6th Decile	60%	$303.7	$9,087	$110.2	$5,036	61%	$313.0	$9,183	$112.8	$5,102
7th Decile	79%	$464.2	$10,674	$73.3	$6,207	79%	$492.1	$11,098	$75.1	$6,340
8th Decile	86%	$602.6	$12,616	$51.9	$6,885	87%	$623.6	$12,747	$50.2	$6,905
9th Decile	92%	$768.9	$15,191	$32.5	$6,941	92%	$787.2	$15,260	$32.2	$7,007
10th Decile	96%	$1,236.2	$23,236	$14.1	$6,709	97%	$1,291.8	$23,788	$13.1	$6,948
Top 5% *	97%	$748.8	$27,858	$5.0	$6,470	98%	$791.4	$28,801	$4.2	$6,768
Top 1% *	98%	$246.6	$45,414	$0.6	$6,224	98%	$265.8	$48,048	$0.6	$6,860
Top 0.1% *	99%	$74.6	$136,945	$0.1	$7,101	99%	$85.7	$153,617	$0.0	$7,648
All	60%	$4,144.1	$12,488	$814.9	$3,685	60%	$4,368.4	$12,904	$830.3	$3,718

* Included in 10th Decile

Deductions as Percent of Montana Adjusted Gross Income
Full-Year Residents
2014 and 2015

Income Group	2014 Itemized Deductions	2014 Standard Deductions	2014 All	2015 Itemized Deductions	2015 Standard Deductions	2015 All
1st Decile	-36%	-73%	-44%	-32%	-69%	-40%
2nd Decile	85%	32%	48%	85%	32%	48%
3rd Decile	54%	22%	34%	76%	22%	43%
4th Decile	42%	20%	29%	43%	20%	29%
5th Decile	33%	18%	25%	33%	18%	25%
6th Decile	28%	16%	23%	27%	15%	23%
7th Decile	26%	15%	23%	26%	15%	24%
8th Decile	24%	13%	22%	24%	13%	22%
9th Decile	21%	10%	21%	21%	10%	20%
10th Decile	13%	5%	12%	13%	5%	13%
Top 5% *	10%	3%	10%	11%	3%	11%
Top 1% *	7%	1%	7%	7%	1%	7%
Top 0.1% *	5%	0.4%	5%	6%	0%	6%
All	21%	20%	21%	21%	20%	21%

* Included in 10th Decile

Taxable Income and Tax
Full-Year Residents
2014 and 2015

Income Group	2014 Taxable Income $ million	2014 Taxable Income Average	2014 Taxable Income % of Total	2014 Tax Liability $ million	2014 Tax Liability Average	2014 Tax Liability % of Total	2015 Taxable Income $ million	2015 Taxable Income Average	2015 Taxable Income % of Total	2015 Tax Liability $ million	2015 Tax Liability Average	2015 Tax Liability % of Total
1st Decile	$0.5	$9	0%	$0.0	$0	0%	$0.4	$8	0%	$0.0	$0	0%
2nd Decile	$105.9	$1,914	1%	$1.3	$24	0%	$108.2	$1,925	1%	$1.4	$24	0%
3rd Decile	$306.2	$5,537	2%	$6.0	$108	1%	$318.3	$5,665	2%	$6.3	$113	1%
4th Decile	$547.1	$9,893	3%	$15.0	$272	2%	$574.4	$10,223	3%	$16.2	$288	2%
5th Decile	$839.2	$15,176	5%	$30.4	$549	3%	$889.4	$15,828	5%	$33.1	$589	3%
6th Decile	$1,181.6	$21,368	7%	$51.8	$937	5%	$1,241.8	$22,100	7%	$55.4	$986	5%
7th Decile	$1,541.1	$27,869	9%	$75.6	$1,367	8%	$1,609.9	$28,650	9%	$79.9	$1,422	8%
8th Decile	$2,027.6	$36,667	11%	$108.3	$1,958	11%	$2,108.6	$37,527	11%	$113.6	$2,021	11%
9th Decile	$2,842.9	$51,410	16%	$163.2	$2,951	17%	$2,933.8	$52,212	16%	$169.2	$3,011	17%
10th Decile	$8,547.2	$154,564	48%	$530.9	$9,601	54%	$8,665.5	$154,218	47%	$543.4	$9,671	53%
Top 5% *	$6,479.9	$234,355	36%	$406.2	$14,691	41%	$6,551.8	$233,201	36%	$415.7	$14,795	41%
Top 1% *	$3,486.9	$630,534	19%	$218.7	$39,544	22%	$3,499.8	$622,860	19%	$224.1	$39,874	22%
Top 0.1% *	$1,417.3	$2,562,895	8%	$85.5	$154,574	9%	$1,377.7	$2,451,412	7%	$86.8	$154,371	9%
All	$17,939.4	$32,441		$982.5	$1,777		$18,450.3	$32,836		$1,018.5	$1,813	

* Included in 10th Decile

Tax as Percent of Adjusted Gross Income
Full-Year Residents
2014 and 2015

Income Group	2014 Montana Adjusted Gross Income $ million	2014 Tax Liability $ million	2014 Tax / Income %	2015 Montana Adjusted Gross Income $ million	2015 Tax Liability $ million	2015 Tax / Income %
1st Decile	-$486.9	$0.0	0.0%	-$546.8	$0.0	0.0%
2nd Decile	$398.8	$1.3	0.3%	$407.3	$1.4	0.3%
3rd Decile	$712.0	$6.0	0.8%	$737.3	$6.3	0.9%
4th Decile	$1,036.4	$15.0	1.5%	$1,081.6	$16.2	1.5%
5th Decile	$1,390.8	$30.4	2.2%	$1,454.0	$33.1	2.3%
6th Decile	$1,807.7	$51.8	2.9%	$1,883.7	$55.4	2.9%
7th Decile	$2,304.3	$75.6	3.3%	$2,389.5	$79.9	3.3%
8th Decile	$2,922.0	$108.3	3.7%	$3,026.1	$113.6	3.8%
9th Decile	$3,906.6	$163.2	4.2%	$4,018.3	$169.2	4.2%
10th Decile	$10,095.9	$530.9	5.3%	$10,272.1	$543.4	5.3%
Top 5% *	$7,386.5	$406.2	5.5%	$7,502.7	$415.7	5.5%
Top 1% *	$3,766.0	$218.7	5.8%	$3,799.4	$224.1	5.9%
Top 0.1% *	$1,494.9	$85.5	5.7%	$1,466.7	$86.8	5.9%
All	$24,087.6	$982.5	4.1%	$24,723.0	$1,018.5	4.1%

* Included in 10th Decile

Business Structure and Taxation

A business's legal ownership structure generally determines how income from the business is taxed. Business organization is a matter of state law, and a business operating in Montana may be organized under the provisions of the laws of Montana (generally Title 35, Montana Code Annotated) or of the laws of another state. States vary somewhat in the options for business organization they allow and in the details of particular business structures.

While tax considerations may affect a business's choice of ownership structure, there are other factors that may have a larger influence. Different business structures give the owners different types of protection from or exposure to the business's legal and financial liabilities. They have different mechanisms for decision making and control of the business's operations. They have different arrangements for sharing of income, expenses, risks and rewards among the owners. And, they offer different levels of privacy or transparency of ownership. How a business is organized can also affect its ability to access capital markets. Most corporations and some types of partnerships can raise funds by issuing new shares, and existing shares can be bought and sold without requiring the other owners' consent. With other business structures, buying and selling ownership interests or raising funds by bringing in new owners may require the other owners' consent.

For taxation, the IRS code puts all businesses in one of three categories, and Montana law generally requires a business to be in the same category for state taxation as it is for federal taxation.

Informally organized sole proprietor businesses are not treated as an entity separate from the owner for income tax reporting purposes. The owner of a sole proprietor business must be an individual or a married couple. Some formally organized businesses with a single owner are not sole proprietor businesses and are treated as separate from the owner for income tax reporting purposes. These businesses are called disregarded entities and are subject to filing a Montana information return and income tax withholding paid on behalf of the owner. The disregarded entity's income is still reported on the owner's tax return and is taxed as part of the owner's income. If the disregarded entity pays income tax on behalf of the owner, the owner can claim the payment as a refundable credit.

Partnerships, limited liability companies, and other unincorporated businesses with more than one owner generally are treated as pass-through entities. A corporation with no more than 100 shareholders, with a single class of stock, and with no shareholders that are another business entity or a nonresident alien may elect to be treated as a pass-through entity. Such a corporation is known as an S corporation, because its taxation is laid out in Subchapter S of Chapter 1 of the IRS code.

For a pass-through entity, there is no tax on income at the business entity level. The entity calculates its net income and each owner's share of that net income. The owners must include that income (or loss) in the calculation of their taxable income. An owner's income from a pass-through is a share of the business's income, not the payments the owner receives from the business. If a pass-through entity retains part of its income to finance expansion or other investment, each owner is taxed on his or her share of the retained income, and the accounting value of each ownership interest is increased by the owner's share of the retained income. If the pass-through pays out more than its annual net income, the excess is treated as a return of a portion of the owner's investment. It is not taxed, and the accounting value of each ownership interest is reduced by the owner's share of the excess distribution.

A pass-through entity is required to file an annual information return showing the calculation of its net income or loss and the distribution of that income or loss to owners. The owners are then responsible for reporting this income on their tax returns and including it in the calculation of their taxable income. If a pass-through entity has a nonresident or second-tier pass-through entity owner, then the pass-through must include the owner in a composite return, withhold income tax on behalf of the owner, or obtain a waiver of these requirements.

A corporation that does not meet the requirements to be treated as a pass-through entity, or that does not choose pass-through treatment, is taxed on income at the business entity level. The corporation calculates its net income and is taxed on it at the corporate income tax rate. The corporation's income is not directly attributed to the owners. A corporation's owners include dividends they receive in the calculation of their taxable incomes. A corporation may pay dividends that are more or less than its net income. If it does, there is no adjustment to the accounting value of individual shares. This allows a corporation to retain profits for reinvestment without the shareholders being taxed on those profits.

The following table shows characteristics of businesses falling into each of the four business tax categories.

Business Structure and Taxation				
	Sole Proprietor	**Pass-Through Entity (S Corporation or Partnership)**	**C Corporation**	**Disregarded Entity**
Legal Business Organization	Informal	Partnership, Limited Liability Company (LLC), Corporation, Limited Partnership, etc.	Corporation	Single Member LLC, etc.
May be Owned By	One Individual or Married Couple	Individuals or Other Business Entities	Individuals or Other Business Entities	Individuals or Other Business Entities
Business Income and Owner's Income	The business net income is all attributed to the owner.	The business calculates its net income, and this income is attributed to the owners.	The business calculates its net income. Owners' income is dividends received.	The business net income is all attributed to the owner.
Distribution of Income to Owners	The business net income is the owner's income from the business.	Distributions to owners need not equal business's current net income.	Business pays dividends to shareholders. Dividends need not equal business's current net income.	Distribution to owner need not equal business's current net income.
Taxation	Owner reports income from business as part of income subject to individual income tax	No tax at the entity level. Owners responsible for tax on income attributed to them.	Business net income subject to corporation income tax. Owners taxed on dividends.	Entity is ignored. business's income is taxed as owner's income.
Reporting	The business receipts and costs are reported on Schedule C of the owner's federal tax return (Schedule F for a farm), and net income is reported on Line 12 for Business Income or Loss (Line 18 for Farm Income or Loss) of the state return.	The business files federal and state information returns. Federal return shows receipts and costs and both show income, deductions, and credits passed through to owners. Owners report their share of net business income from the pass-through as business income (Schedule E and Line 17 of the tax return for individuals). If the business receives dividends, capital gains, or other passive income, owners report those separately on the appropriate return lines.	The business files federal and state corporate income tax returns and a federal information report, Form 1099-DIV, for each owner who received at least $10 of dividends. Owners report dividends received on their tax returns (Line 9 of state return for individuals).	Income is reported on owner's return. Information return required if owner is a non-resident or another business.

Business Structure, Tax Administration, and Compliance

Taxation of business income can be complicated when a business operates in more than one taxing jurisdiction and when one business entity is partly or completely owned by another. When a business operates in more than one taxing jurisdiction, it is necessary to decide how much of the business's income is taxable by each jurisdiction. When one business entity owns another or two businesses have a common owner, it can be necessary to decide how much of the common income is due to each business. When affiliated businesses operate across multiple jurisdictions, the complications are compounded.

A general principle that most U.S. states and most countries follow is that business income should be taxable by the jurisdiction where the business activity that created the income took place and should not be taxable by other jurisdictions. This is often called the source principle of income taxation.[1] When a business operates in more than one taxing jurisdiction, each must decide how much of the business's

1 The source principle of income taxation contrasts with the destination principle of consumption taxation. U.S. states and most countries follow the principle that taxes on consumptions, such as sales taxes, should be levied by the jurisdiction where the goods or services are used rather than by jurisdictions where they are made or sold.

income has its source in that jurisdiction. For example, suppose a company harvests timber and mills it into lumber in Montana and sells the lumber in North Dakota. The company receives all its gross income in North Dakota, and pays most of its costs in Montana. Its net income, which is the basis of taxation in both Montana and North Dakota, is due to the combined operation in both states. Each state decides how much of the combined net income to tax through a process called *apportionment.* Each state uses a formula to determine an *apportionment factor,* the portion of the company's business income[1] to attribute to operations in the state. Montana uses the equally-weighted three-factor apportionment formula where the apportionment factor is the average of the proportions of a company's property, payroll, and sales in a state. Other states use a range of formulas, with some placing more weight on one factor and less, or no, weight on the others.

If lumber production in Montana and lumber sales in North Dakota were separate, unrelated businesses, there would be no need for apportionment. The lumber production company's net income would be the difference between its receipts from selling lumber wholesale and its costs of harvesting trees and milling lumber. This net income would be taxable by Montana. The lumber sales company's net income would be the difference between its receipts from retail lumber sales and its costs of buying the lumber wholesale and operating its lumber yards. This net income would be taxable by North Dakota.

If the two companies are *affiliates*, such as two separate legal entities both owned by a third company, the situation is more complicated. Apportionment is still needed because wholesale lumber sales from the mill in Montana to the yards in North Dakota are not arms-length transactions. The *transfer prices* at which the lumber mill sells to the lumber yards are not determined in a market and do not necessarily reflect the lumber's true value. From the point of view of the parent company, these transfer prices are irrelevant. The mill's revenue from wholesale sales and the lumber yard's expenses for wholesale purchases cancel each other out. The parent company's net income is the difference between the revenue from retail lumber sales and the costs of timber harvesting, lumber milling, and lumber yard operations.

Transfer prices do matter to the states. If the lumber mill charges high prices to the lumber yards, its Montana profits will be higher and the lumber yards' North Dakota profits will be lower. If the mill charges low prices, its Montana profits will be lower and the lumber yards' North Dakota profits will be higher.

Montana law addresses this problem through *combined reporting*. Affiliated companies that are not engaged in completely separate businesses are required to file a single, combined return and to apportion the group's income. The Montana timber harvesting and lumber milling company, the North Dakota lumber yard company, and their parent company would file a combined return and should pay the same Montana taxes as if they were a single company.

Another complication can arise when affiliated companies are pass-through entities and there is a *tiered ownership* structure, with a company that is actually conducting business being owned by a second-tier pass-through entity, which may be one of several owned by a third-tier pass-through entity, which may be a partnership owned by several fourth-tier pass-through entities, and so on. As income is passed through this chain to the individuals who are the ultimate owners, its original source may be lost. For example, a person in New York or California who is a partner in a company that owns other companies may be unaware that part of their income from this partnership ultimately comes from business operations in Montana. In that case, they are likely to pay New York or California income tax on Montana-source income that should be taxed by Montana and not be taxed by the other state.

Montana law tries to address this problem by requiring pass-through entities with out-of-state owners either to have the out-of-state owners agree to file Montana tax returns, to withhold Montana tax for the out-of-state owners, or to file a composite return and pay Montana tax on behalf of its owners.

Montana law requires individual corporations and affiliated groups to report world-wide income and apportion a share to Montana, with one exception. A group of affiliated companies may make what is

1 Income that is not from a company's normal line of business, such as income from sale of some of a company's assets, generally is assigned to the state where the assets are located rather than being apportioned.

called a *water's-edge election.* When a group makes this election, it is only required to include affiliates in its combined report if the primary company owns at least half the stock and at least 20% of the affiliate's payroll and property is in the U.S., the affiliate is one of several types of companies defined in federal law that only engage in international trade, the affiliate has gains or losses from selling U.S. real estate, or the affiliate is incorporated in one of the countries listed as tax havens in section 15-31-322(1)(f), MCA. A corporate group that makes the water's edge election is taxed at a rate of 7% rather than the normal rate of 6.75%.

Abusive tax shelters are arrangements where taxpayers mischaracterize either income or gains and losses in order to avoid taxes. While nothing about pass-through entities or tiered business ownership creates abusive tax shelters, individuals and corporations wanting to evade taxes have used the complexity that tiered ownership can create to try to hide or mischaracterize income.

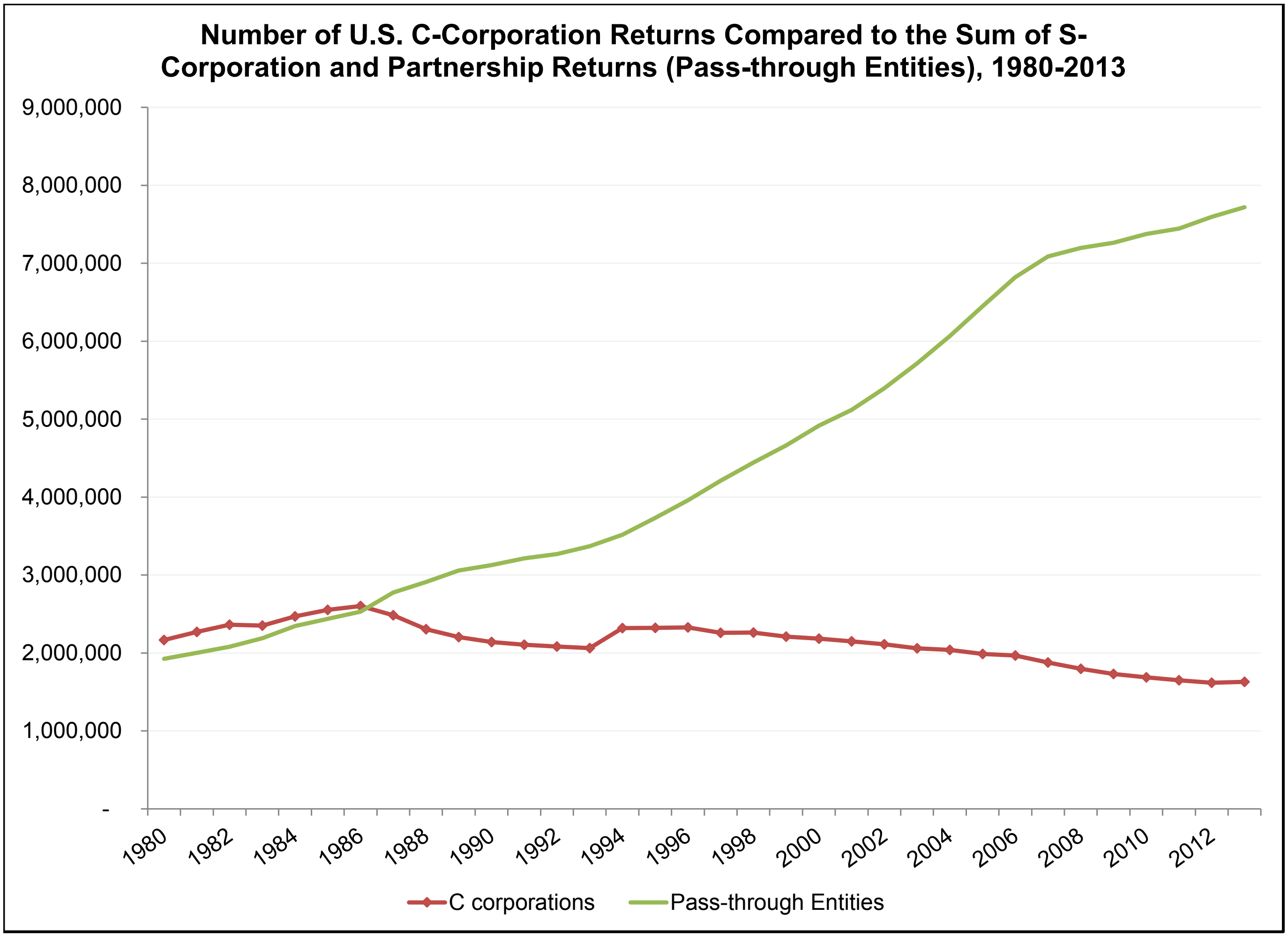
Some abusive tax shelters involve pretending that monetary payments are a loan or that in-kind compensation is actually a business investment. Others involve creating transactions with offsetting paper gains and losses and then recognizing the losses for tax purposes while claiming that recognition of the gains can be indefinitely deferred. In others, the claim is made that the losses were incurred by a taxable entity while the gains belong to an entity that is not subject to taxes in the U.S. Some types of abusive tax shelters make use of complicated, multi-tiered business structures either to try to hide the mischaracterization of income or to shuffle gains and losses between related entities and then claim that they are not related.

For example, one scheme involves creating a series of tiered business entities organized under the laws of several countries, with each passing its income to the next in line and the final entity paying the income to the owner but mischaracterizing it as a loan. The purpose of the tiered business structure in this case is just to make it too hard to track the money. In another scheme, the taxpayer sets up three business entities. Two entities engage in offsetting financial transactions, such as buying and selling offsetting futures contracts. The third is set up in another country. When the two contracts are closed out, one will have a gain and the other will have an equal loss. The taxpayer recognizes the loss and uses it to offset other income. The entity with the gain is sold, at a nominal price that does not reflect the value of the gain on its futures contracts, to the non-U.S. entity, and then the taxpayer claims that the gain is not subject to U.S. taxes.

U.S. courts have consistently ruled that these types of sham transactions with no economic purpose other than evading taxes should be ignored for U.S. tax purposes.

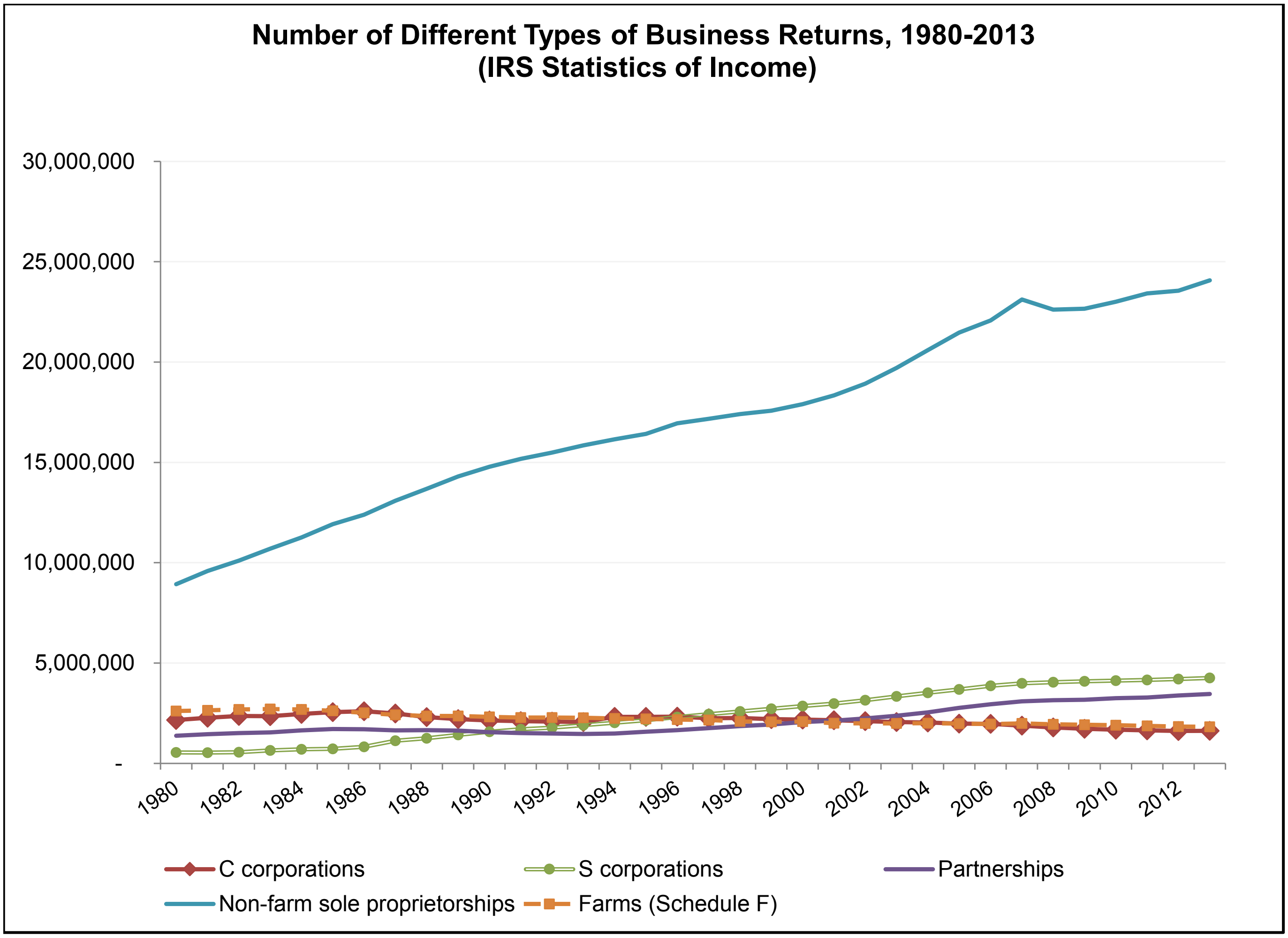
Growth of Pass-Through Entities

Increasingly, in Montana and nationwide, business and investment activities are being conducted by "pass-through entities." The graph below shows the number of returns filed with the IRS by C corporations versus those filed by pass-through entities (partnerships, S corporations, and disregarded entities) from 1980 through 2013 (the graphs and history in this section are from *Selected Issues Relating to Choice of Business Entity*, Joint Committee on Taxation, U.S. Congress, July 27, 2012; 2010, 2011, 2012, and 2013 data is from the IRS Statistics of Income Division).



Over time, Congress has modified the rules governing pass-throughs, particularly S corporations, making those business structures more attractive for business purposes. For example, the number of permitted shareholders has been expanded from the original 10 in 1958 to 35 in 1982, 75 in 1996, and 100 in 2004, where it remains today.

The graph on the next page shows growth over the same period, 1980–2013, of all types of business organizations, including non-farm sole proprietorships, S corporations, partnerships, and farms filing Schedule F.



As can be seen from the graph, non-farm sole proprietorships are the most common type of business entity in the U.S. based upon the number of returns filed. The number of non-farm sole proprietorships has grown substantially – from 9 million in 1980 to over 24 million in 2013.

Sole proprietorships, as the name suggests, are businesses with a single owner and are a familiar sight on many main streets in Montana. The Department of Commerce in its publication, *Economic and Demographic Analysis of Montana,* December 2007, reported that over 60 percent of Montana businesses are sole proprietorships without any employees. The owner of a sole proprietorship will record his or her income on the state individual income tax Form 2 on line 12 as Business Income (or Loss), and will attach a copy of federal Schedule C (or C-EZ), which has been filed with the taxpayer's federal tax return.

If the business owner has a farm or ranch operation that is operated as a sole proprietorship, the taxpayer reports his or her income on line 18 of the state individual income tax form (Farm Income or (Loss)), and attaches a copy of federal Schedule F, which has been filed with the taxpayer's federal form. The number of farms filing under Schedule F is also shown on the graph. The total number of farms in the U.S. filing Schedule F decreased from 2.6 million in 1980 to 1.8 million in 2013. However, it should be noted that farms can also operate as partnerships or be incorporated as S or C corporations.

During the same period, the number of C corporation returns declined, going from 2.2 million corporations in 1980 to 1.63 million in 2013. One thing to note is that C corporations in Montana seem to vary greatly in terms of size – there are large businesses which engage in operations across many states and even countries, but there are also smaller firms that engage in agricultural operations, are main street businesses, or regional operations. Some of these corporations may have been incorporated before the S corporation structure was available; others may have been incorporated as C corporations in order to be better positioned to access capital markets, or for one or more of the advantages that C corporation status provides.

The number of businesses that filed as S corporations has also grown very rapidly during the same time. The IRS data shows the number went from 545,000 in 1980 to over 4.2 million in 2013; an annual average growth rate of 6.6 percent. Partnerships grew more slowly – increasing from 1.4 million in 1980 to 3.5 million in 2013.

Although not shown on the graph, less common types of pass-through entities also increased over the last three decades. These include real estate investment trusts (REITs) and regulated investment companies (RICs), better known as mutual funds, rising from 1,691 returns in 1980 to 17,630 returns in 2012.

Businesses of all sizes can be C corporations or pass-through entities. Sole proprietor businesses generally are small. For 2013, the IRS reports that average receipts were $4.6 million for C corporations, $1.5 million for partnerships, and $1.6 million for S corporations, but only $56,000 for sole proprietor businesses. Many sole-proprietor businesses are part-time or a sideline for the owner. For 2015, 93% of taxpayers whose Montana income tax returns showed income or loss from a sole-proprietor business reported more income from other sources.

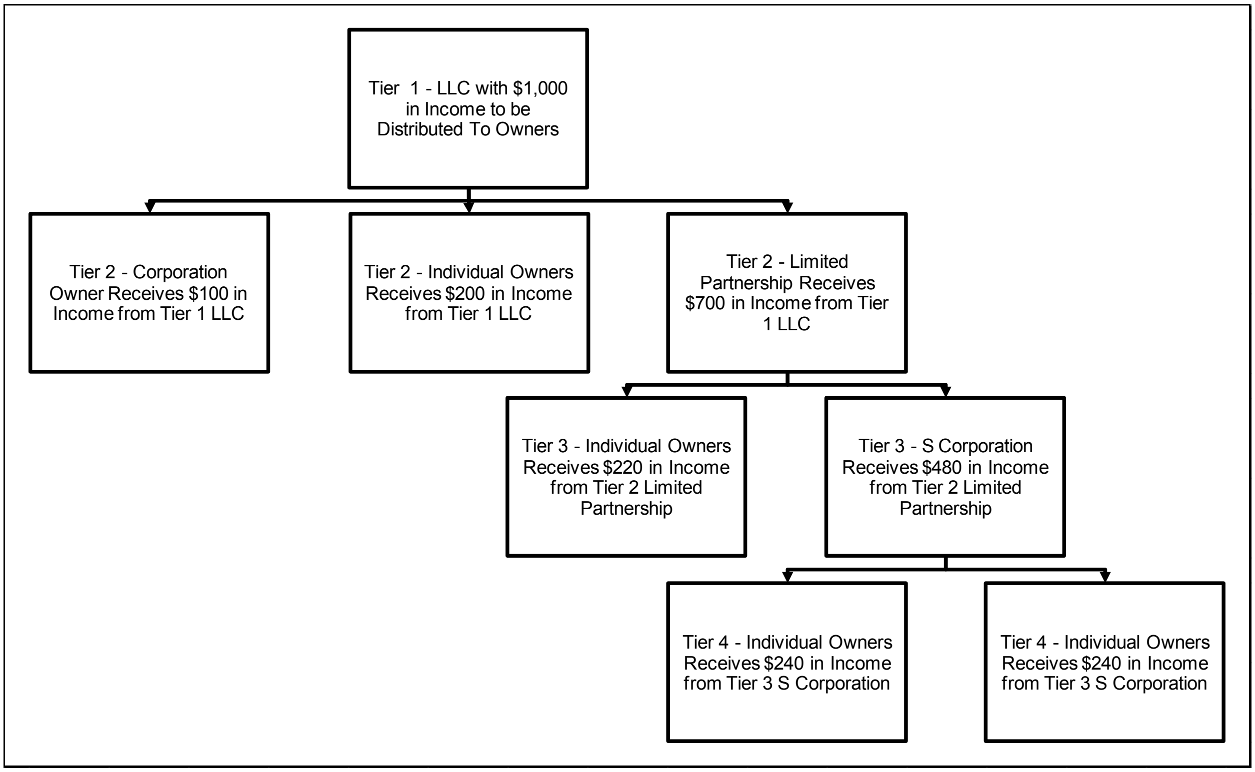
Ownership, Income, Deductions, and Credits Reported on Montana Pass-Through Returns

Pass-through entities include partnerships; S corporations; limited liability companies (LLCs); real estate investment trusts (REITS); regulated investment trusts (RITs), better known as mutual funds; and others. Partnerships are an old and familiar business entity, but S corporations are less so. The S corporation rules were enacted in 1958 and permit a corporation and its shareholders to elect to be taxed at one level.

The most common type of pass-through entity today is the limited liability company (LLC). LLCs are actually a creation of the states since state law generally governs business structure. The first LLC statute was enacted in Wyoming in 1977 and now all states and the District of Columbia have LLC statutes. However, for federal tax purposes, federal law governs the tax treatment (states generally follow the federal treatment). For taxation purposes, LLCs with two or more members are generally treated as partnerships, unless the LLC elects to be treated as a C or S corporation. Unless it elects to be treated as a C or S corporation, a single-member LLC is generally treated as a sole proprietorship if the single member is an individual; if the single-member is a corporation, then the LLC is treated as a branch by the IRS. The taxpayer's state filing must be consistent with its federal filing, so if a business filed as an S corporation at the federal level, it must file as an S corporation at the state level.

A pass-through entity is not taxed itself. Instead, its income and expenses are reported on the tax returns of the owners. The owners can be corporations, individuals, other pass-through entities, or a mix of all of them. When pass-through entities are owned by other pass-through entities, it creates a tiered business structure.

Tiered structures add complexity to tax administration because the taxpayer may be quite remote from the entity doing business in the state. Because pass-through entities can have a corporation, individual, and/or another pass-through entity as a partner, owner, or shareholder, they represent a challenge for tax administration. The diagram on the following page shows how complex a set of ownership, or partnership, relationships can become.



Pass-through entities with Montana source income are required to file an information return each year. The pass-through entity is also required to withhold on behalf of any partner, shareholder, member, or other owner who is a nonresident individual, foreign C corporation, or a pass-through entity (also referred to as a second-tier pass-through entity). An owner for which withholding is required may file an agreement with the state to timely file a Montana return, pay taxes, and be subject to personal jurisdiction of the state with respect to the income from a pass-through entity. If an agreement is on file for an owner, the pass-through entity is not required to withhold on that owner's behalf. If this agreement is not met, the pass-through entity must in all subsequent tax years withhold the appropriate amount and pay the tax payment directly to the state (15-30-3313, MCA). As an alternative to the agreement, owners may elect to be included in a composite tax return. In a composite tax return, the pass-through entity pays tax on behalf of the owner and fulfills the owner's requirement to file their own tax return.

The pass-through information returns show the total amounts of various types of income, deductions, and credits allocated to the owners, and the amount distributed to each owner. Pass-through entities operating in more than one state apportion part of their income to Montana using the same apportionment formula as C corporations. Pass-through returns show the Montana sourced income allocated to each owner and indicate whether each owner is an individual or another business entity.

Owners of pass-through entities taxed as partnerships may be either individuals or business entities. Shares of S corporations can only be owned by individuals, electing small business trusts or employee stock ownership plans. The table to the right shows the number of owners associated with Montana's pass-throughs

Shares of Pass-Through Owners by Residency Status

Type of Owner	Number	%
Resident Individuals	83,923	22%
Nonresident Individuals	201,533	53%
Montana Business Entities	5,616	1%
Non-Montana Business Entities	90,098	24%
Total	381,170	100%

broken down by individuals and business entities. Based upon information provided in each pass-through's tax forms, this table also provides a breakdown of pass-throughs based on the residency status of the owner.

In tax year 2014, there were 381,170 owners associated with the 58,240 pass-throughs filing information returns in Montana. Of the approximately 381,000 owners, 22 percent reported being residents of Montana. Non-resident individuals are the largest group of Montana's pass-through owners, with 201,533 reported owners. Just over 5,600 Montana business entities were listed as owners of pass-throughs according to informational tax returns. More than 90,000 non-Montana business entities were owners of pass-throughs with Montana source income. Overall, individuals comprised 75 percent of the owners associated with Montana's pass-throughs, which is a slight increase from the previous year's 74 percent.

The following table shows owner information from the same group of pass-through returns as in the previous table but splits the ownership data into multi-state, as well as S corporation and partnership, status.

Montana Pass-Through Owners by Residency Status and Pass-Through Type

	S Corporations				Partnerships			
	Montana		Multi-State		Montana		Multi-State	
Type of Owner	Owners	%	Owners	%	Owners	%	Owners	%
Resident Individuals	38,049	88%	1,851	7%	42,304	32%	1,719	1%
Nonresident Individuals	4,272	10%	22,799	81%	51,723	39%	122,739	69%
Montana Business Entities	691	2%	45	0%	4,537	3%	343	0%
Non-Montana Business Entities	247	1%	3,477	12%	33,504	25%	52,870	30%
Total	43,259	100%	28,172	100%	132,068	100%	177,671	100%

Net income from a pass-through entity's business operations is usually allocated to the owners as ordinary business income. Individual owners report this income on Schedule E of their federal tax returns and then report income from Schedule E on Line 17 of the Montana tax return. Income that the pass-through entity receives from passive investments or the sale of assets is allocated to the owners as that type of income, and owners report it on the corresponding lines of their tax returns. For example, if a pass-through entity receives $1,000 of interest and allocates it equally to its 10 owners, who are Montana individuals, each owner should report the $100 of interest on Line 8a of their Form 2.

In the previous two tables, there are Montana and non-Montana business entities that have ownership shares in both partnerships and S corporations. When there is tiered ownership - meaning one pass-through entity is a full or part owner of another - both entities will include the income the first-tier entity allocates to the second-tier entity in their returns. The next table shows the number of returns, types of income, Montana adjustments to income, and deductions that were passed through to owners in tax year 2014. Income and other items passed through to two or more entities are only counted once.

Montana-Source Income Passed Through To Owners, 2014 Net of Distributions from First-Tier to Second-Tier Pass-Throughs				
	S Corporations		Partnerships	
	Montana	Multi-State	Montana	Multi-State
Returns	24,356	6,796	21,397	5,691
Income Items				
Salaries and Other Fixed Payments to Owners	$0	$0	$1,495,227,931	$273,969,689
Ordinary Business Income	$1,534,226,992	-$16,127,449,462	$4,162,198,855	$2,913,215,283
Rental Income				
Real Estate	$34,844,580	-$148,300,033	$63,886,949	-$159,542,438
Other	$8,738,790	$20,130,599	$151,078,266	$11,152,274
Interest	$38,058,435	$14,404,568	$2,811,316,839	$2,525,835,223
Dividends	$41,500,128	$53,504,802	$3,456,367,521	$2,430,310,058
Royalties	$13,855,904	$23,679,798	$650,264,482	$260,241,105
Capital Gains	$243,760,789	$102,550,417	$24,126,235,028	$19,148,982,887
Gains Taxed as Ordinary Income	$197,827,421	-$65,602,746	$4,497,105,195	$1,585,240,813
Other Income	$19,374,355	$14,282,310	$6,542,623,207	$6,268,558,928
Total	$2,132,187,394	-$16,112,799,746	$47,956,304,273	$35,257,963,822
Montana Additions to Federal Income				
Interest on Non-Montana Municipal Bonds	$2,733,745	-$5,027,888	$32,097,310	$49,987,772
State and Local Income Taxes	$2,425,036	$5,462,461	$19,725,831	$28,086,277
Other	$4,375,049	$505,382	$149,810,497	$12,837,326
Total	$9,533,830	$939,954	$201,633,638	$90,911,375
Montana Subtractions from Federal Income				
Interest on Federal Bonds	$4,906,103	$628,749	$50,052,771	$40,197,000
Purchases of Recycled Materials	$319,609	$175,121	$12,437	$0
Other	$150,311,354	-$16,428,662,167	$260,278,411	-$742,708,562
Total	$155,537,066	-$16,427,858,296	$310,343,619	-$702,511,562
Deductions				
Expensing of Capital Purchases	$319,278,727	$283,963,958	$2,825,153,080	$1,460,596,675
Contributions	$26,960,496	-$113,639,654	$59,696,177	$111,266,429
Interest on Funds Borrowed to Make Investments	$16,427,977	$12,575,101	$1,332,631,096	$1,370,684,760
Other	$71,660,566	-$526,103,527	$5,881,817,168	$4,230,112,566
Total	$434,327,766	-$343,204,122	$10,099,297,521	$7,172,660,430
Total Net Montana Source Income	**$1,551,856,392**	**$659,202,627**	**$37,748,296,771**	**$28,878,726,329**

When a pass-through entity does something that is eligible for a tax credit, the credit is usually allocated to the owners. Owners then claim their share of the credit on their tax returns. However, sometimes owners may not be able to claim a credit that is allocated to them. For example, some credits can only be claimed by individuals, so a corporation that owns part of a pass-through entity would not be able to claim those credits. Some credits can only be used to reduce the current year's tax liability, so owners with no taxable income in the current year would not be able to claim these credits. Because of this, the credits actually claimed on owners' tax returns can be less than the credits reported on pass-through returns.

The next table shows credits reported on pass-through entity returns for tax year 2014. Credits actually claimed by owners are included in the credits claimed against individual income tax and corporate income tax.

Tax Credits Passed Through To Owners, 2014 Net of Distributions from First-Tier to Second-Tier Pass-Throughs				
	S Corporations		Partnerships	
Credit	Montana	Multi-State	Montana	Multi-State
Dependent Care Credit	$0	$0	$0	$0
College Contribution Credit	$12,485	$1,700	$1,510	$0
Insurance for Uninsured Montanans Credit	$61,115	$4,300	$8,211	$635
Credit for Investment in Recycling Equipment	$580,991	$51,259	$148,901	$1,042
Alternative Energy Production Credit	$0	$0	$5,643	$0
Contractor's Gross Receipts Credit	$2,518,003	$1,844,225	$76,845	$10,821
Alternative Fuel Credit	$0	$0	$0	$0
Infrastructure Users Fee Credit	$0	$0	$35,548	$0
Historic Building Preservation Credit	$0	$0	$86,081	$0
Mineral Exploration Credit	$0	$0	$0	$0
Empowerment Zone Credit	$0	$0	$0	$0
Film Production Credit	$106,971	$0	$0	$0
Biodiesel Blending Credit	$0	$0	$0	$0
Oilseed Crushing Credit	$0	$0	$0	$0
Insure Montana Credit	$1,276,812	$60,300	$125,625	$7,142
Temporary Emergency Lodging Credit	$0	$0	$0	$0
Total	**$4,556,377**	**$1,961,784**	**$488,364**	**$19,640**

Pass-Through Distributions and Credits by Industry

When preparing an informational tax return, pass-through entities are expected to provide information on the type of industry work the pass-through engages in.[1] The next table lists the Montana- source income that was distributed by Montana's S corporations in tax year 2014, broken down by industry sector type. As the tax return information shows, there is a significant amount of variation in the amount of income S corporations provided to their respective owners at the industry level. S corporations in the Trade, Transportation and Utilities industry generated the largest amount of Montana-source income for their owners, distributing approximately $503 million in 2014. The Financial Activities and Professional and Business Services S corporations also provided a significant amount of income to their owners, passing through $412 million and $318 million in income respectively.

1 Industry data on income tax returns are self-reported and are subject to some reporting error.

Montana-Source Income Passed Through to Owners, 2014 Net of Distributions from First-Tier to Second-Tier Pass-Throughs ($ million)											
	S-Corporations										
	Natural Resources & Mining	Construction	Manufacturing	Trade, Transportation & Utilities	Information	Financial Activities	Professional & Business Services	Education & Health Services	Leisure & Hospitality	Other Services	Unknown / Public Admin
Returns	3,104	5,791	1,171	4,915	408	4,219	5,507	1,722	2,346	1,644	325
Income Items											
Salaries and Other Fixed Payments to Owners	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Ordinary Business Income	$263.2	$348.6	-$3.1	-$7,792.1	$12.7	$165.6	-$7,924.1	$142.9	$96.6	$92.8	$3.5
Rental Income											
Real Estate	$10.8	-$2.6	$0.5	$6.3	$0.3	-$134.2	$3.1	$0.6	$1.5	$0.3	-$0.1
Other	$6.8	$0.0	$0.6	$14.8	$0.0	$6.1	$0.1	$0.0	$0.3	$0.1	$0.0
Interest	$5.2	$3.5	$4.6	$2.0	$0.4	$32.6	-$1.0	$1.7	$1.8	$1.7	$0.1
Dividends	$2.0	$0.9	$2.5	$6.7	$0.2	$87.1	-$7.7	$0.3	$0.3	$2.7	$0.0
Royalties	$22.6	$0.2	$0.2	$0.3	$0.0	$12.8	$0.6	$0.0	$0.5	$0.2	$0.0
Capital Gains	$15.5	$12.5	$5.2	-$2.6	$0.2	$258.3	-$13.2	$1.6	$5.3	$62.8	$0.6
Gains Taxed as Ordinary Income	$99.1	$3.3	$7.8	$21.1	$0.7	-$36.1	$12.7	$3.6	$18.9	$1.1	$0.0
Other Income	$9.0	$1.1	$4.1	$1.5	$0.0	$16.6	$1.0	$0.0	$0.2	$0.1	$0.0
Total	$434.2	$367.7	$22.6	-$7,742.0	$14.5	$408.8	-$7,928.6	$150.8	$125.3	$161.9	$4.1
Montana Additions to Federal Income											
Interest on Non-Montana Municipal Bonds	$0.7	$0.2	$0.0	-$1.2	$0.0	$1.5	-$3.5	$0.0	$0.0	$0.0	$0.0
State and Local Income Taxes	$0.3	$0.5	$0.2	$0.4	$0.0	$2.0	$0.9	$3.5	$0.1	$0.0	$0.0
Other	$0.3	$0.9	$0.1	$0.6	$0.5	$0.5	$1.2	$0.3	$0.2	$0.3	$0.0
Total	$1.3	$1.6	$0.3	-$0.2	$0.5	$4.0	-$1.5	$3.8	$0.3	$0.3	$0.0
Montana Subtractions from Federal Income											
Interest on Federal Bonds	$0.0	$0.2	$0.1	$0.0	$0.0	$0.4	$4.5	$0.0	$0.0	$0.3	$0.0
Purchases of Recycled Materials	$0.0	$0.1	$0.3	$0.1	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Other	$6.9	$1.2	$2.5	-$7,687.6	$0.2	-$146.5	-$8,457.5	$0.1	$2.4	$0.1	$0.0
Total	$6.9	$1.5	$2.9	-$7,687.6	$0.2	-$146.1	-$8,453.0	$0.1	$2.4	$0.4	$0.0
Deductions											
Expensing of Capital Purchases	$132.3	$74.0	$14.7	$60.9	$2.2	$32.3	$245.6	$12.1	$16.7	$12.1	$0.4
Contributions	$7.1	$6.5	$1.9	-$54.2	$0.5	$5.3	-$58.5	$1.9	$1.7	$1.1	$0.1
Interest on Funds Borrowed to Make Investments	$0.1	$0.3	$0.0	$0.2	$0.0	$20.6	$7.7	$0.0	$0.1	$0.0	$0.0
Other	$8.0	$0.8	$0.1	-$564.8	$0.0	$88.7	$10.5	$0.5	$0.4	$1.3	$0.1
Total	$147.4	$81.6	$16.7	-$557.9	$2.7	$146.9	$205.2	$14.4	$18.9	$14.5	$0.6
Total Net Montana Source Income	**$281.2**	**$286.2**	**$3.3**	**$503.3**	**$12.2**	**$412.0**	**$317.7**	**$140.1**	**$104.3**	**$147.3**	**$3.5**

As the next table shows, the amount of pass-through income also varies significantly for Montana's pass-through partnerships. In tax year 2014, the Financial Activity partnerships generated slightly more than $64 billion in income within Montana, which is significantly higher than the income generated by any other pass-through industry sector. Unlike S corporations, one partnership sector reported negative pass-through income for their owners. In 2014, the Trade, Transportation and Utilities sector reported a net income loss of $266 million.

Montana-Source Income Passed Through to Owners, 2014 Net of Distributions from First-Tier to Second-Tier Pass-Throughs ($ million)											
	Partnerships										
	Natural Resources & Mining	Construction	Manufacturing	Trade, Transportation & Utilities	Information	Financial Activities	Professional & Business Services	Education & Health Services	Leisure & Hospitality	Other Services	Unknown / Public Admin
Returns	3,896	1,312	495	1,828	285	14,586	1,929	417	1,327	632	381
Income Items											
Salaries and Other Fixed Payments to Owners	$22.4	$16.2	$8.8	$22.0	$781.3	$822.1	$46.7	$34.8	$8.9	$5.6	$0.4
Ordinary Business Income	$220.1	$39.2	-$6.3	-$338.3	$598.5	$5,341.2	$1,040.9	$126.0	$34.2	$14.7	$5.2
Rental Income											
Real Estate	$16.3	$1.0	$0.7	$7.5	$0.2	-$74.3	-$49.6	$1.8	-$0.7	$1.1	$0.3
Other	$3.9	$0.1	$0.2	-$35.9	$115.8	$18.2	$59.1	$0.0	$0.3	$0.5	$0.1
Interest	$4.8	$0.5	$8.1	$11.2	$110.0	$5,033.0	$162.7	$0.7	$5.7	$0.2	$0.3
Dividends	$3.6	$0.1	$1.6	$1.0	$38.8	$5,562.2	$271.9	$0.0	$6.2	$0.3	$0.9
Royalties	$174.5	$0.3	$2.3	$0.1	$276.9	$295.8	$158.0	$0.1	$0.2	$1.8	$0.5
Capital Gains	$30.3	$4.3	$0.4	$37.8	-$26.5	$42,999.5	$226.7	$0.9	-$4.2	$0.9	$5.1
Gains Taxed as Ordinary Income	$214.1	$2.0	$3.8	$3.5	-$4.6	$5,671.1	$134.0	$0.7	$54.1	$0.5	$3.1
Other Income	$16.3	$3.3	$0.0	$19.7	$128.9	$12,511.5	$132.4	$0.0	-$2.2	$0.0	$1.3
Total	$706.2	$67.0	$19.7	-$271.4	$2,019.3	$78,180.4	$2,182.9	$165.2	$102.5	$25.5	$17.0
Montana Additions to Federal Income											
Interest on Non-Montana Municipal Bonds	$0.7	$0.1	$0.0	$0.0	$0.0	$80.6	$0.4	$0.0	$0.0	$0.2	$0.0
State and Local Income Taxes	$0.3	$0.0	$0.1	$2.1	$9.7	$32.3	$3.1	$0.0	$0.1	$0.0	$0.0
Other	$1.3	$0.0	$0.0	$37.4	$2.6	$116.6	$4.5	$0.0	$0.1	$0.0	$0.0
Total	$2.3	$0.1	$0.1	$39.6	$12.4	$229.6	$8.1	$0.0	$0.1	$0.2	$0.0
Montana Subtractions from Federal Income											
Interest on Federal Bonds	$0.0	$0.0	$0.0	$0.0	$0.0	$90.2	$0.0	$0.0	$0.0	$0.0	$0.0
Purchases of Recycled Materials	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Other	$142.7	$0.1	$0.0	$4.5	$3.6	-$869.2	$235.8	$0.1	$0.8	$0.0	-$0.8
Total	$142.7	$0.1	$0.0	$4.5	$3.6	-$779.1	$235.8	$0.1	$0.8	$0.0	-$0.8
Deductions											
Expensing of Capital Purchases	$231.0	$9.7	$4.6	$9.8	$0.8	$3,883.2	$133.7	$4.2	$5.8	$2.0	$1.0
Contributions	$3.7	$0.3	$1.3	$1.0	$13.8	$136.1	$13.4	$0.4	$0.7	$0.2	$0.1
Interest on Funds Borrowed to Make Investments	$1.0	$0.0	$1.1	$0.9	$0.0	$2,675.6	$21.0	$2.8	$0.6	$0.1	$0.1
Other	$76.8	$2.5	$13.3	$18.0	$873.4	$8,365.9	$751.1	$4.7	$3.8	$0.9	$1.6
Total	$312.5	$12.6	$20.3	$29.6	$887.9	$15,060.7	$919.2	$12.2	$10.9	$3.1	$2.7
Total Net Montana Source Income	**$253.3**	**$54.4**	**-$0.5**	**-$266.0**	**$1,140.1**	**$64,128.4**	**$1,036.0**	**$152.9**	**$90.8**	**$22.6**	**$15.1**

The following two tables provide an industry-level breakdown of the credits claimed by Montana's S corporations and partnerships. For some credits, there is not a significant amount of variation in the use of credits by each industry sector. Nearly every pass-through industry sector claimed the Insure Montana, Health Insurance for Uninsured Montanans, and College Contributions credits. At the same time, no pass-through claimed the Mineral Exploration, Empowerment Zone, or Temporary Emergency Lodging credits. Some other credits were utilized, but only within a couple of industries. For example, nearly every S corporation industry sector had at least one pass-through claim the College Contribution credit, while only four of the 11 partnership industry sectors made a claim for this credit. At the same time, the Infrastructure Users Fee and Historic Building Preservation credits were only claimed by pass-throughs in one industry sector.

Tax Credits Passed Through to Owners, 2014, Net of Distributions from First-Tier to Second-Tier Pass Throughs											
	S Corporations										
Credit	Natural Resources & Mining	Construction	Manufacturing	Trade, Transportation & Utilities	Information	Financial Activities	Professional & Business Services	Education & Health Services	Leisure & Hospitality	Other Services	Unknown / Public Admin
Dependent Care Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
College Contribution Credit	$800	$1,281	$418	$3,167	$200	$1,973	$5,730	$408	$208	$0	$0
Insurance for Uninsured Montanans Credit	$1,950	$12,912	$1,411	$7,052	$1,513	$5,567	$13,426	$7,830	$650	$5,978	$7,126
Credit for Investment in Recycling Equipment	$0	$0	$78,604	$299,832	$0	$0	$53,328	$0	$0	$200,486	$0
Alternative Energy Production Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Real Estate	$8,801	$4,125,258	$25,962	$34,233	$0	$537	$134,934	$0	$11,421	$21,082	$0
Other	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Infrastructure Users Fee Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Historic Building Preservation Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Mineral Exploration Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Empowerment Zone Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Film Production Credit	$0	$0	$0	$0	$63,608	$0	$31,536	$0	$11,827	$0	$0
Biodiesel Blending Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Oilseed Crushing Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Insure Montana Credit	$74,662	$229,728	$41,561	$265,957	$15,768	$95,466	$301,622	$118,370	$56,051	$132,347	$5,580
Temporary Emergency Lodging Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Total	**$86,213**	**$4,369,179**	**$147,956**	**$610,241**	**$81,089**	**$103,543**	**$540,576**	**$126,608**	**$80,157**	**$359,893**	**$12,706**

Tax Credits Passed Through to Owners, 2014, Net of Distributions from First-Tier to Second-Tier Pass Throughs											
	Partnerships										
Credit	Natural Resources & Mining	Construction	Manufacturing	Trade, Transportation & Utilities	Information	Financial Activities	Professional & Business Services	Education & Health Services	Leisure & Hospitality	Other Services	Unknown / Public Admin
Dependent Care Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
College Contribution Credit	$0	$0	$0	$525	$0	$885	$25	$75	$0	$0	$0
Insurance for Uninsured Montanans Credit	$0	$0	$0	$2,100	$0	$1,160	$3,741	$1,845	$0	$0	$0
Credit for Investment in Recycling Equipment	$0	$0	$88,833	$60,068	$0	$1,042	$0	$0	$0	$0	$0
Real Estate	$0	$0	$0	$0	$0	$5,643	$0	$0	$0	$0	$0
Other	$0	$75,070	$2,196	$0	$0	$0	$10,400	$0	$0	$0	$0
Alternative Fuel Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Infrastructure Users Fee Credit	$0	$0	$0	$0	$0	$35,548	$0	$0	$0	$0	$0
Historic Building Preservation Credit	$0	$0	$0	$0	$0	$86,081	$0	$0	$0	$0	$0
Mineral Exploration Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Empowerment Zone Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Film Production Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Biodiesel Blending Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Oilseed Crushing Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Insure Montana Credit	$34,533	$6,287	$8,091	$26,211	$0	$21,034	$18,363	$4,186	$8,482	$5,580	$0
Temporary Emergency Lodging Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Total	**$34,533**	**$81,357**	**$99,120**	**$88,904**	**$0**	**$151,393**	**$32,529**	**$6,106**	**$8,482**	**$5,580**	**$0**

Pass-Through Entities by Size - Number of Owners

Pass-through entities vary greatly in size. Approximately 48 percent of Montana's S corporation pass-throughs reported a single owner and 69 percent of partnerships with Montana source income had two to three owners. Overall, pass-throughs that operate in multiple states tend to have more owners than pass-throughs that only operate in Montana. Less than 10 percent of the S corporations that only operated in Montana in 2014 had more than eight reported owners, while nearly 14 percent of multi-state S corporations had at least nine owners. At the same time, 29 percent of Montana's multi-state partnerships had more than eight owners, which is approximately five times higher than the proportion of Montana-only partnerships with at least nine reported owners.

Pass-Through Entities - Number of Owners								
	S Corporations				Partnerships			
Number of Reported	Montana		Multi-State		Montana		Multi-State	
Owners	Number	%	Number	%	Number	%	Number	%
1	12,625	47.7%	448	9.9%	1,536	7.2%	98	1.7%
2 to 3	9,932	37.5%	2,432	53.8%	14,718	69.4%	2,554	44.0%
4 to 8	1,387	5.2%	1,024	22.6%	3,705	17.5%	1,479	25.5%
9 to 20	196	0.7%	374	8.3%	634	3.0%	605	10.4%
Over 20	2,314	8.7%	244	5.4%	620	2.9%	1,062	18.3%

Pass-Through Entities by Size - Montana Source Income

The following table shows the number and percentages of pass-through entities in six groups based on the entity's Montana source income. As can be seen from the following table, many S corporations and approximately 40 percent of all partnerships reported zero, or negative, Montana-source income on their returns. And while S corporations and partnerships tend to be used as business structures for smaller businesses, there are some partnerships and S corporations that have substantial Montana source income – falling into the over $5 million category. Forty-seven S corporations and 991 partnerships reported more than $5 million in Montana source income.

Number of Pass Through Entities by Amount of Montana Source Income								
	S Corporations				Partnerships			
	Montana		Multi-State		Montana		Multi-State	
Montana - Source Income	Number	%	Number	%	Number	%	Number	%
$0 or Negative	7,312	30.0%	2,766	40.7%	9,267	43.2%	2,139	37.5%
$1 to $10,000	3,734	15.3%	2,237	32.9%	3,362	15.7%	1,214	21.3%
$10,001 to $100,000	9,743	39.9%	1,148	16.9%	5,751	26.8%	920	16.1%
$100,001 to $1,000,000	3,391	13.9%	555	8.2%	2,184	10.2%	619	10.9%
$1,000,001 to $5,000,000	197	0.8%	82	1.2%	378	1.8%	320	5.6%
Over $5,000,000	32	0.1%	15	0.2%	500	2.3%	491	8.6%

The next table shows Montana source income reported by pass-through entities for the same groups provided in the previous table. Most of the income generated by pass-through entities was from entities with over $5 million in Montana source income. S corporations with over $5 million in Montana source income generated approximately $694 million in 2014, which is 31 percent of all the Montana source income generated by Montana's S corporations. Partnerships with over $5 million in Montana source income generated $69 billion in Montana source income in 2014.

Montana Source Income by Size of Pass-Through								
	S Corporations				Partnerships			
	Montana		Multi-State		Montana		Multi-State	
Montana - Source Income	$ million	%	$ million	%	$ million	%	$ million	%
$0 or Negative	-$384	-24.5%	-$69	-10.0%	-$2,962	-7.8%	-$2,391	-8.3%
$1 to $10,000	$16	1.0%	$5	0.8%	$13	0.0%	$3	0.0%
$10,001 to $100,000	$390	24.9%	$41	5.9%	$221	0.6%	$35	0.1%
$100,001 to $1,000,000	$854	54.5%	$171	24.8%	$594	1.6%	$223	0.8%
$1,000,001 to $5,000,000	$377	24.1%	$162	23.5%	$865	2.3%	$797	2.8%
Over $5,000,000	$314	20.0%	$380	55.1%	$39,120	103.4%	$30,308	104.6%

Taxation of Estates and Trusts

Estates and trusts are legal arrangements where one party holds assets on behalf of or for the benefit of one or more other parties. The details of these legal arrangements vary widely, because trusts can be set up to serve many purposes and because estates and trusts are created under state laws, which vary between states.

A trust generally is managed by one or more trustees. The estate of a decedent is managed by an executor. The manager of a bankruptcy estate is called a trustee or a debtor in possession depending on whether the estate is created under Chapter 7 or Chapter 11 of the bankruptcy code. Managers of trusts and estates are referred to as fiduciaries because of their legal obligation to act in the interest of another party rather than in their own interest.

When an estate or trust earns income, it may distribute part or all of the income to one or more beneficiaries or it may retain part or all of the income. Beneficiaries are taxed on income distributed to them, and the estate or trust is taxed on income that it retains.

A trust may also distribute part of the principal to one or more beneficiaries. All estates and many trusts are created with the intention of ultimately distributing all their assets. Distributions from the principal of an estate or trust are not taxable.

Montana taxes the income of a trust or estate as if the trust or estate were an individual, with the exception that a trust or estate is allowed a deduction for income distributed to beneficiaries. Some trusts are created for the purpose of providing funds for charity, and estates and trusts are allowed a deduction for charitable contributions.

Estates and trusts may file on a tax year that is different from the calendar year. In this section, information is reported based on the calendar year when the estate or trust's tax year started. Tax years numbered 2014 may have ended any time between December 30, 2014 and December 29, 2015. Returns are due by the 15th day of the fourth month after the end of the tax year, but taxpayers may receive a six-month filing extension. Thus, 2014 is the latest tax year for which all returns had been filed and processed by the time of publication.

Types of Estates and Trusts

The Montana return asks the fiduciary to indicate that the return is for one of eleven types of estate or trust. The table to the right shows the number of returns in each category for 2013 and 2014.

Number of Estate and Trust Returns	2013	2014
Simple Trust	2,598	2,625
Complex Trust	4,565	4,702
Decedent's Estate	1,476	1,521
Grantor Trust	834	847
Electing Small Business Trust	61	18
Qualified Disability Trust	47	60
Bankruptcy Estate (Chapter 7)	23	22
Bankruptcy Estate (Chapter 11)	5	7
Qualified Funeral Trust	4	3
Pooled Income Fund	3	1
Other	203	271
Total	9,819	10,077

A simple trust is a trust where all income is to be distributed to the beneficiaries, no income is to be used for charitable purposes, none of the principal is to be distributed, and capital gains are to be allocated to the principal. A complex trust is a trust that does not qualify as a simple trust and does not fall into one of the other categories. A decedent's estate is charged with distributing assets in accordance with the decedent's will or state law and preserving assets until they are distributed.

A grantor trust is a trust where the person who created the trust retains control of or an ownership interest in the trust's assets. For both federal and Montana taxes, a grantor trust is treated as a disregarded entity: Its income is treated as belonging to the grantor and its income and deduction line items should be reported on the grantor's tax return.

An electing small business trust is a trust that holds shares in an S corporation and for which the trustee has made an election to be taxed under a different section of federal law than generally applies to trusts.

Montana taxes an electing small business trust in the same manner as other trusts.

A qualified disability trust is a trust whose beneficiaries are one or more disabled persons under the age of 65. A bankruptcy estate holds the assets of a bankrupt individual or business and is charged either with liquidating those assets to repay debts (Chapter 7) or with reorganizing the business (Chapter 11).

A qualified funeral trust is a type of grantor trust set up to pay the beneficiary's funeral expenses. A pooled income fund is an arrangement where individuals or businesses donate assets to a charity with the provision that the donor is to receive part or all of the earnings from the assets for a fixed period or for life.

Income of Estates and Trusts

Montana law considers a trust to be a resident trust if Montana is the primary place where the business of the trust is administered. If a primary place of business is not identifiable, the trust is a resident trust if the principal trustee's residence or usual place of business is in the state. A trust is classified as a part-year resident trust if the primary place of administration moves into or out of the state during a year. A trust or estate that is created during a year has a short tax year, but is considered either resident or nonresident, unless it moves.

All of a resident trust's income is taxable by Montana, but a trust with income that has its source in another state may claim a credit against Montana tax for tax paid to another state. Montana source income of a non-resident trust is taxable by Montana. As with a nonresident individual, a nonresident trust calculates tax on all its income and then multiplies this calculated tax by the share of its income that has a Montana source.

The following table shows the different types of income reported by trusts and estates. It shows income of resident estates and trusts and nonresident and part-year resident estates and trusts separately. For nonresident and part-year resident estates and trusts, it shows the average apportionment factor used in calculating their tax. This is the ratio of total Montana source income to total income from all sources.

Income Reported on Estate and Trust Returns ($ million)

	2013		2014	
Type of Income	Resident	Nonresident and Part-Year	Resident	Nonresident and Part-Year
Interest	$13.533	$208.039	$12.607	$156.666
Dividends	$41.716	$431.752	$51.426	$409.431
Sole Proprietor Business Income	$4.767	-$53.815	$5.551	-$8.647
Pass-Through Business, Rents, Royalties	$63.303	$126.030	$73.452	$224.425
Gain or Loss on Asset Sales				
Taxed as Capital Gains	$97.891	$1,497.484	$79.715	$1,917.130
Taxed as Ordinary Income	-$0.874	$57.219	-$2.453	$36.910
Other	$14.876	$27.373	$16.022	$103.279
Total	$235.212	$2,294.082	$236.320	$2,839.193
Average Apportionment Factor for Nonresident and Part-Year Resident Estates and Trusts		3.32%		0.71%

Deductions for Charitable Contributions and Distributions to Beneficiaries

Income earned by a trust or estate generally is put to one of four uses: it may be used to pay costs of the trust, it may be donated to charity, it may be distributed to a beneficiary, or it may be retained and added to the principal of the trust. In calculating taxable income, an estate or trust is allowed an itemized deduction for charitable contributions in the same way an individual is. Unlike an individual, an estate or trust is allowed a deduction for income distributed to a beneficiary. An estate or trust may also distribute part of the principal, but this is not deductible for the trust or taxable for the beneficiary. The following table shows deductions for charitable contributions and for distributions to beneficiaries.

Deductions for Charitable Contributions and Distributions to Beneficiaries

	2013		2014	
	Entities with Deduction	$ million	Entities with Deduction	$ million
Charitable Constributions				
Resident Estates and Trusts	229	$5.628	229	$6.006
Nonresident and Part-Year	469	$304.547	517	$533.785
Distributions from Income				
Resident Estates and Trusts	3,463	$123.930	3,371	$127.350
Nonresident and Part-Year	1,006	$305.362	1,035	$344.918

Tax Paid by Estates and Trusts

Trusts and estates directly pay about $5 million in tax per year. The following table shows tax paid by type of trust or estate. Categories with few returns are combined to protect taxpayer confidentiality.

Tax After Capital Gains Credit and Apportionment ($ million)

Entity Type	2013	2014
Bankruptcy Estates	$0.000	$0.007
Decedent Estates		
Resident	$0.491	$0.651
Nonresident and Part-Year	$0.019	$0.011
Electing Small Business Trusts		
Resident	$0.002	$0.000
Nonresident and Part-Year	$0.000	$0.015
Grantor Trusts	$0.000	$0.000
Simple Trusts		
Resident	$0.485	$0.554
Nonresident and Part-Year	$0.020	$0.021
Disability, Funeral, Pooled Income, and Other	$0.001	$0.019
Complex Trust Not in Another Category		
Resident	$2.092	$1.673
Nonresident and Part-Year	$1.807	$0.541
All Estates and Trusts	$4.917	$3.494

Montana's corporate income tax is a tax levied on C corporations for the "privilege of carrying on business in this state for the tax year in which the income was earned" (15-31-101(3), MCA). A corporation includes:

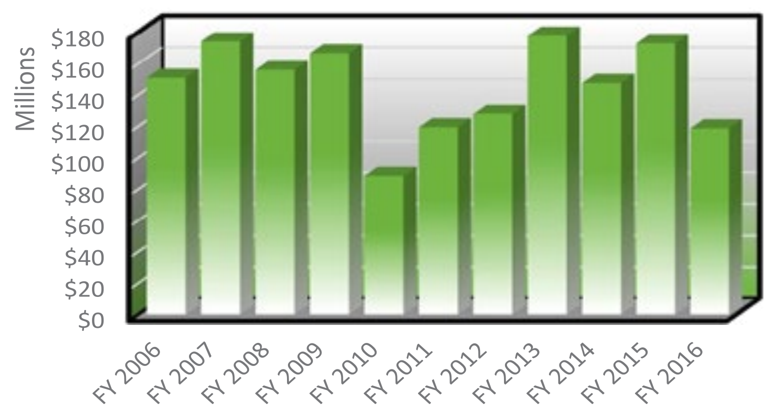
> an association, joint-stock company, common-law trust or business trust that does business in an organized capacity, all other corporations whether created, organized, or existing under and pursuant to the laws, agreements, or declarations of trust of any state, country or the United States, and any limited liability company, limited liability partnership, partnership or other entity that is treated as an association for federal income tax purposes and that is not a disregarded entity (15-31-101(1), MCA).
>
> Every bank organized under the laws of the state of Montana, of any other state, or of the United States and a savings and loan association organized under the laws of this state or of the United States is subject to the Montana corporate income tax (15-31-101(4), MCA).

In the 2013 Legislature, SB 361 was passed revising the name of the corporate license tax to the corporate income tax. The change applies to tax years beginning after December 31, 2013.

The table below shows total corporate income tax collections for fiscal years 2006 through 2016 as recorded in the state accounting system. As a rule, corporate income tax collections in Montana follow the general national economy. Total collections in FY 2006 (which started on July 1, 2005) were $150.8 million, increasing to $173.9 million in FY 2007 and declining to $87.9 million in FY 2010. Corporate tax revenues for FY 2015 and FY 2016 were $172.7 million and $118.4 million, respectively.

Corporate Income Tax

Fiscal Year	Total Revenue
FY 2006	$150,801,693
FY 2007	$173,896,433
FY 2008	$155,890,705
FY 2009	$166,352,453
FY 2010	$87,906,411
FY 2011	$119,045,890
FY 2012	$127,774,092
FY 2013	$177,500,421
FY 2014	$147,550,091
FY 2015	$172,731,561
FY 2016	$118,386,603



Corporate income taxes are deposited in the state general fund. However, the 2013 Legislature passed HB 354, which established a wildfire suppression fund and authorized certain general fund transfers to the fund. HB 354 required transfer of corporate tax revenues in excess of $152.0 million in FY 2013 to the wildfire suppression account. The transfers are required by August 15th, after the end of the fiscal year. In FY 2013, total corporate income tax collections were $177.5 million, which is over the $152 million threshold, so the difference was transferred to the wildfire suppression account. HB 354 also required FY 2014 and FY 2015 revenues in excess of $156.2 million and $157.5 million, respectively, be transferred to the wildfire suppression account. FY 2014 revenues were below the threshold so no transfer was made. FY 2015 revenues exceeded the $157.5 million threshold and the difference was transferred to the wildfire suppression account.

The following table provides a breakdown for the last seven years of revenues deposited in the general fund by how they are collected and also shows refunds.

As the table shows, estimated quarterly payments are by far the largest source of corporate income tax collections, followed by payments with returns.

Average estimated payments over the past seven years were $112.5 million. Average annual revenue for payments with returns over the same period was $30.4 million. The seven-year average of revenues from audits, penalties, and interest was $19.9 million. Refunds averaged about $26.8 million per year.

Corporate Income Tax Collections and Refunds - General Fund

Fiscal Year	Payments With Returns	Estimated Payments	Audits, Penalties, and Interest	Refunds	Total Collections
FY 2010	$36,909,143	$72,732,614	$15,380,337	($37,121,182)	$87,900,911
FY 2011	$23,747,579	$98,979,556	$26,116,467	($29,799,712)	$119,043,890
FY 2012	$27,777,649	$110,864,886	$27,885,386	($38,757,329)	$127,770,592
FY 2013	$35,894,922	$135,790,121	$16,811,485	($10,999,107)	$177,497,421
FY 2014	$28,136,519	$130,352,294	$10,765,481	($21,706,704)	$147,547,591
FY 2015	$31,109,657	$129,923,853	$28,775,440	($17,972,938)	$171,836,012
FY 2016	$29,079,903	$108,541,034	$13,308,491	($31,390,463)	$119,538,965
Average	$30,379,339	$112,454,908	$19,863,298	($26,821,062)	$135,876,483

Over the past seven years, total corporate tax collections averaged about $135.9 million annually. However, there was wide variation in annual collections over that time period.

Who pays Corporate Income Taxes?

Only C corporations pay corporate income taxes. Corporations that elect to file as a subchapter S corporation for federal tax purposes are also required to file as a subchapter S corporation for Montana income tax purposes. Despite the filing requirement, subchapter S corporations do not pay Montana corporate income taxes. Instead the owners or shareholders of the S corporation are subject to income tax on income received through the S corporation. The owner/shareholder therefore reports any taxable income on their individual income tax form. S corporations are discussed more in the section on pass-through entities.

Exemptions

Organizations exempt from the tax include corporations or associations organized and operated exclusively for religious, charitable, scientific, or educational purposes, and whose income does not benefit any stockholder or individual. Other entities exempt from corporate income tax include labor, agricultural or horticultural organizations; civic organizations operated exclusively for the promotion of social welfare; clubs or corporations organized and operated exclusively for pleasure, recreation or other nonprofit purposes and who do not have any income that benefits any private stockholder or member; and similar nonprofit organizations.

Unrelated business taxable income, as defined by federal law, of exempt organizations that creates more than $100 of federal tax liability is taxable as corporate income in the same manner as other taxable corporate income.

To receive treatment as exempt from state corporation taxes, the corporation must prove it is in compliance with all statutory conditions (15-31-102, MCA and ARM 42.23.103). Research and development (R&D) firms organized to engage in business for the first time in Montana do not have to pay the corporate income tax for the first five years of operation. In order to receive this tax exemption, the firm must apply to the Department of Revenue and be approved as meeting legal requirements (15-31-103, MCA).

Returns Filed for Tax Year 2014	
Regular C Corporations	16,571
S Corporations	31,152
Total Corporations	47,723
C Corporations Paying Minimum Tax*	10,380
C Corporations Paying More Than Minimum Tax	6,191
Total C Corporations	16,571

* Includes corporations filing a tax return, but claiming zero or negative taxable income

Distribution of Corporate Income Taxes

The following table shows the distribution by Montana tax liability of the 16,572 corporate returns with a Montana tax liability filed in calendar years 2015 and 2016 reporting on tax year 2014. Note that the revenues from the return data will not match the fiscal year revenues in earlier tables because fiscal year revenue is based upon payments, including estimated payments and payments with returns, recorded in the state accounting system.

Altogether the top 100 returns constituted about 68 percent of total tax liability for the entire group of taxpayers. The top 500 returns accounted for 87 percent of total Montana tax liability for the group. The other 16,072 returns accounted for only 13 percent of the total Montana tax liability.

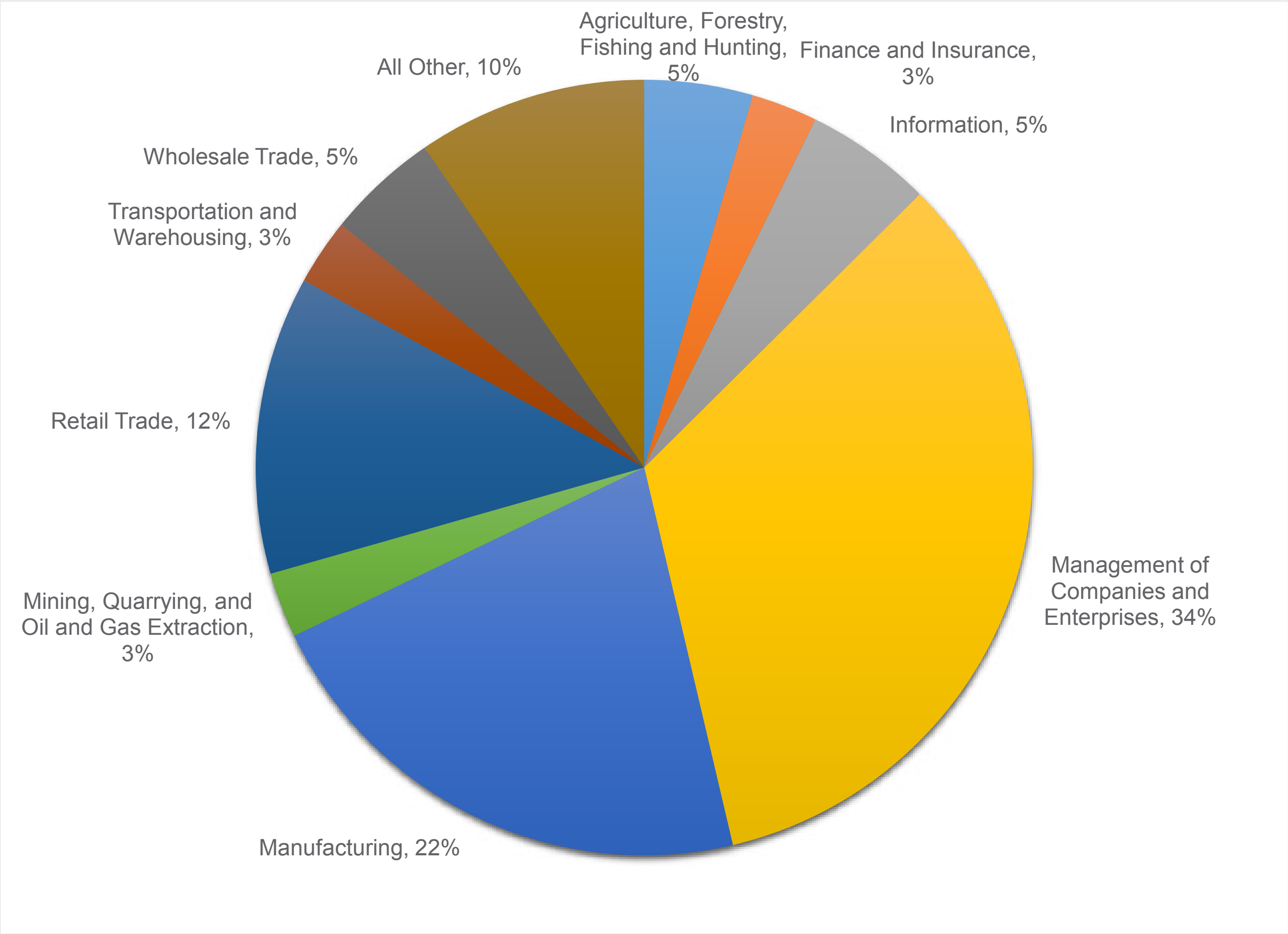
Corporate Returns Filed in CY 2015 - CY 2016 for Tax Year 2014
Distribution of Montana Tax Liability

Regular Corporation Returns	Number	Tax Liability	Percent of Total Liability	Cumulative Percent of Total Liability
Top 100 returns	100	$98,925,275	68%	68%
Second 100 returns	100	$13,414,200	9%	77%
Third 100 returns	100	$7,269,022	5%	82%
Fourth 100 returns	100	$4,722,386	3%	85%
Fifth 100 returns	100	$3,543,943	2%	87%
All other returns	16,072	$18,352,335	13%	100%
Total	16,572	$146,227,161	100%	n/a

Another way to look at the distribution of corporate income taxes is by economic sector. Starting with the 2009 tax returns, corporate taxpayers were asked to identify their primary industry just as identified on their federal tax forms. The following graph on the next page shows the distribution of corporate income taxes for the largest sectors.

The largest sector in terms of tax year 2014 tax liability was management of companies and enterprises. Corporations involved in the management of companies and enterprises that includes bank and other holding companies and corporate or regional headquarters paid about 34 percent of all the corporate income taxes.

Manufacturing was the second largest sector with 22 percent of all corporate income taxes in tax year 2014. The Census Bureau list of manufacturing activities includes food manufacturing, which includes



grain, oilseed, fruit and dairy processing; bakeries; beverages. Others include sawmills, millwork, and paper manufacturing; petroleum and chemical manufacturing; cement and concrete; and other activities.

Corporations primarily involved in retail trade paid 12 percent of corporate income taxes followed by all other (10 percent); information (5 percent); agriculture, forestry, fishing and hunting (5 percent); and wholesale trade (5 percent). Mining, quarrying, and oil and gas extraction, transportation and warehousing, and finance and insurance each made up 3 percent.

When looking at the graph it is important to remember that only businesses organized as C corporations pay corporate income taxes. Businesses can also be organized as partnerships, S corporations, or sole proprietorships. These businesses are called pass-through entities because the income from the business is passed through to the owners or shareholders of these businesses, who then must report the income on their own tax returns. Businesses in certain industries, such as agriculture or legal services, may be more likely to be structured as a pass-through entity, rather than as a C corporation.

Taxable Income and the Tax Rate

The starting point for calculating Montana corporate income tax is the corporation's federal taxable income. In order to determine net income taxable by Montana, certain adjustments to federal taxable income must be made. For example, municipal bond interest is taxable and must be added to income. Also, Montana allows certain reductions to income, such as a portion of the cost of energy conservation investments made in a building used for the corporation's business.

After the additions and reductions to federal taxable income required by Montana law, income is then apportioned to Montana to produce Montana taxable income.

If the corporation conducts business that is taxable only in Montana, then all of the net taxable income from that business is Montana taxable income. The tax is levied at a rate of 6.75 percent on net income earned in Montana.

Multi-state corporations with net taxable income generated by doing business both inside and outside the state are required to apportion income to Montana based on an equally weighted, three-factor apportionment formula.

Sales, property, and payroll comprise the three factors used in the apportionment formula. The payroll factor is the ratio of payroll paid in compensation attributable to the production of business income during the tax period in Montana to all payroll paid. Similarly, the property factor is based on the ratio of Montana property to all property and the sales factor is based on the ratio of Montana sales to all sales. Once the three factors are calculated, they are averaged together to create the overall apportionment factor. That factor is applied against adjusted federal taxable income to produce the net income apportioned to Montana, or Montana taxable income.

The tax is normally levied at a rate of 6.75 percent on net income apportioned to Montana, with exceptions explained below.

Following is an example of how a multi-state corporation doing business in Montana would calculate its Montana source income assuming the following facts:

- The corporation has $1 million in payroll in Montana out of total payroll of $10 million dollars.
- It has $2 million of property in Montana out of total property owned by the corporation of $125 million.
- The corporation has sales in Montana of $4 million out of total sales for the firm of $100 million during the tax year.

These facts result in an apportionment factor of 0.052 (see the calculations in the table to the right).

If this corporation had total taxable income of $10,000,000, then its Montana taxable income is $520,000 ($10 million times 0.052 equals $520,000), and its state income tax is $35,100 before credits ($520,000 times 6.75 percent).

Relying on an apportionment formula simplifies the calculation of taxable income by state for the multistate taxpayer and for the state tax administrator, but there can still be issues. A simple

Example of Apportionment Factor Calculation for Multi-State Corporation

Payroll In Montana		Total Payroll		Payroll Factor
$1,000,000	÷	$10,000,000	=	0.100
Property In Montana		**Total Property**		**Property Factor**
$2,000,000	÷	$125,000,000	=	0.016
Sales In Montana		**Total Sales**		**Sales Factor**
$4,000,000	÷	$100,000,000	=	0.040
Apportionment Factor (Avg.)				**0.052**

example is that of a multistate taxpayer who over-apportions or shifts one or more of the factors - property, payroll or sales - to a state that does not tax corporate income. Apportioning too much in sales or property or payroll to a non-income tax state reduces other states' apportionment factors and so reduces the income taxable in those states.

Montana is a worldwide, combined unitary state. A business is unitary when the operations of that business within the state depend on or contribute to the operations of that business outside the state. However, in Montana corporations can elect to have primarily their United States income included in the apportionment process. Corporations taking this election, called a "water's edge" election, pay the tax at a rate of 7 percent instead of 6.75 percent. For corporations electing to file as water's edge corporations, there are some limits on exclusions under the water's edge election (see 15-31-322 and 15-31-324, MCA).

Multinational unitary corporations wishing to file under the water's edge method are required to file a written election within the first 90 days of the tax period for which the election is to become effective. The Department of Revenue must approve the election before the corporation uses it and the election is binding for three consecutive taxable periods.

Corporations whose only activity in Montana consists of making sales, and who do not own or rent real estate or tangible personal property, and whose annual gross income from sales in Montana does not exceed $100,000 may elect to pay an alternative tax equal to ½ of 1 percent of gross sales.

There is a minimum tax of $50 for any corporation doing business in the state. The table on returns filed for tax year 2013 earlier in this section shows that for those returns filed in tax year 2014 by corporations, the minimum tax or less was paid on 10,783 returns or 64 percent. If the corporation has no property, sales, or payroll in the state during the tax period, it is exempt from the minimum tax.

All states with a corporate income tax allow corporations a carry forward of net operating losses. These losses can be deducted against net taxable income in future years, although all states limit the number of years a corporation can carry forward losses. Some states, including Montana, allow carryback of net operating losses.

Montana net operating losses (NOL) of a corporation may be carried back for a period of three years and used to reduce prior years' taxable income, and may be carried forward for up to seven years to reduce taxable income in those future years. The table on the next page provides a comparison of Montana treatment of net operating loss deductions with that in other states.

In Montana, if a corporation has net operating losses, it can file an amended return and claim a refund of previously-paid taxes for any or all of the prior three years.

For example, a hypothetical Montana corporation had net taxable income of $50,000 each year in years 1, 2, and 3. In year 4 it had losses of $160,000 and in year 5 it is back to profitability and has taxable income of $60,000. Based upon these assumptions, the corporation would have paid $3,375 in corporate income taxes ($50,000 times 0.0675) each year in years 1, 2, and 3. In year 4, it had net losses of $160,000 so it paid no corporate income tax (actually it would likely pay the $50 minimum tax unless it had credits). In year 4, the corporation could file amended returns for years 1, 2, and 3. On the amended returns, the taxpayer could claim $150,000 of year 4 losses against income earned in those prior years, and obtain refunds of taxes paid, or $10,125 (3 times $3,375). The remaining $10,000 of losses would be used as a deduction against year 5 income of $60,000, reducing taxable income from $60,000 to $50,000, and reducing the corporation's tax liability by $675.

Twenty-nine states do not allow carryback of net operating losses, but do allow carryforward of losses, from 5 years up to 20 years. Fourteen states allow the same carryforward and carryback periods as federal tax law has historically allowed (2 years back and 20 years forward). Louisiana, Montana, and Utah allow corporations with net operating losses to carry back these losses against the three prior years of income.

States with Corporate Income Taxes
Allowed Carryback and Carryforward Periods for Net Operating Losses

Allowed years of carryback	Allowed years of carryforward					
	5 years forward	7 years forward	10 years forward	12 years forward	15 years forward	20 years forward
0 years back	Arkansas Rhode Island		Kansas Michigan New Hampshire 6/ Vermont	Illinois 4/	Alabama Minnesota North Carolina Oregon Tennessee	Arizona Colorado Connecticut 11/ District of Columbia Florida Indiana Iowa Kentucky 11/ Maine 5/ Massachusetts Nebraska New Jersey New Mexico North Dakota Ohio Pennsylvania 8/ South Carolina Wisconsin
2 years back						Alaska California 1/ Delaware 2/ Georgia Hawaii Idaho 3/ Maryland Mississippi Missouri Oklahoma Virginia West Virginia 10/
3 years back		Montana			Louisiana Utah 9/	New York 7/

1/ California limited loss carrybacks to a percent of income in tax years 2013 and 2014.
2/ Delaware has a $30,000 per year limit on carrybacks.
3/ Idaho limits carrybacks to $100,000 in the preceding 2 years.
4/ Illinois suspended use of NOLs for tax years beginning in 2011-2012.
5/ Maine suspended certain carryforwards for tax years 2009-2011.
6/ New Hampshire limits carryforward of losses generated per year to $10 million for tax years beginning in CY 2013.
7/ New York reformed corp tax for 2015 on; from 2014 NOLs cannot be carried back before 2015.
8/ Pennsylvania limits NOL deductions to the larger of $5 million or 30% of Pennsylvania taxable income.
9/ Utah has a $1 million limit on carrybacks.
10/ West Virginia limits carrybacks to $300,000.
11/ Limits NOLs to 50% of a taxpayer's net income.

Source: *2015 State Tax Handbook* , CCH, 2014.

As can be seen in the footnotes to the Net Operating Loss table, a number of states have restricted the amounts of losses that can be carried back and used to obtain refunds or carried forward in any one year. For example, like Montana, Utah provides a three year carryback of net operating losses, but has a limit of $1 million on carryback losses.

Idaho allows losses to be carried back against income for up to 2 years, but limits carryback losses to $100,000. Idaho allows carry forward of losses for up to 20 years.

North Dakota allows carry forward of losses for up to 20 years, but does not allow carryback of losses.

Credits

As with individual income tax, corporations with expenditures that qualify under state law can claim tax credits. Tax credits are applied against the corporation's tax liability to reduce the amount the corporation owes.

For example, a corporation with Montana taxable income (income after deductions and additions) of $3,000 has a tax liability of $202.50 ($3,000 times 6.75 percent). However if the corporation has expenditures that qualify under state law for a credit of $150, its tax liability is reduced to $52.50 from $202.50. The table below shows what credits have been claimed in the last two tax years and the number of corporations claiming those credits. If the number of credits claimed on returns is less than 10, then the number is represented by an asterisk.

Montana Corporation Tax Credits

	--- Tax Year 2013 ---		--- Tax Year 2014 ---	
Credit	Number of Credits	Total Credit Amounts	Number of Credits	Total Credit Amounts
Contractors Gross Receipts Tax Credit	103	$613,274	96	$645,615
Charitable Endowment Credit	26	$50,704	17	$32,561
Montana Recycling Credit	*	$40,379	*	$114,755
Credit for Increasing Research Activities	*	$16,264	*	$1,627
Credit for Contribution to MT University or Private College	28	$6,173	31	$19,300
Temporary Emergency Lodging Credit	0	$0	0	$0
Health Insurance for Uninsured Montanans Credit	15	$11,741	*	$5,581
Credit for Alternative Fuel Motor Vehicle Conversion	*	$379	*	$4,000
Alternative Energy Production Credit	*	$100	0	$0
Dependent Care Assistance Credit	0	$0	0	$0
New/Expanded Industry Credit	0	$0	*	$4,221
Historical Building Credit	0	$0	*	$85,520
Infrastructure Users Fee Credit	*	$472,732	*	$741,261
Mineral Exploration Incentive Credit	*	$534	*	$25
Film Production Credit	0	$0	0	$0
Film Employment Refundable Credit	0	$0	*	$25,468
Biodiesel Blending and Storage Credit	0	$0	0	$0
Oilseed Crushing and Biodiesel Production Credit	0	$0	0	$0
Geothermal System Credit	*	$1,500	0	$0
Insure Montana Credit	141	$691,185	111	$546,204
Empowerment Zone Credit	0	$0	0	$0
Total Credits	**338**	**$1,904,965**	**284**	**$2,226,138**

Some of the above credits are claimed on returns that have not been audited yet. The amount of credit claimed may change once these returns are audited. In addition, some of the above numbers represent a carryback of some credits claimed on amended returns received during the fiscal year. Credits claimed on less than 10 returns are indicated by a *.

Filing Requirements and Estimated Payments

Corporate Income Tax Tax Year 2014		
Tax Year Period Ending	Number of Taxpayers	Percent
12/31/2014	11,197	68%
1/31/2015	370	2%
2/28/2015	254	2%
3/31/2015	804	5%
4/30/2015	228	5%
5/31/2015	235	5%
6/30/2015	902	5%
7/31/2015	158	5%
8/31/2015	216	5%
9/30/2015	823	5%
10/31/2015	864	5%
11/30/2015	520	5%
Total	16,571	100%

Unlike individual income taxpayers who must file their federal and state returns based upon a calendar year, corporate taxpayers must file tax returns based upon their fiscal year. Corporate income taxpayers must use the same tax period for their state return as was used for the federal tax return (15-31-112, MCA).

As can be seen in the table to the right, about two-thirds of corporate taxpayers (68 percent) have a fiscal year/tax year that is based upon the calendar year. Tax returns for taxpayers using a calendar year as their fiscal year are due May 15th or November 15th under an automatic extension.

The next most-used fiscal year/tax year is the twelve months ending at the end of June; about 5 percent of corporate taxpayers filing in Montana used a fiscal year ending at the end of June. Tax returns for taxpayers using another period as their fiscal year are due the 15th day of the fifth month after close of the taxable year. So if a taxpayer's fiscal year ends at the end of June, the tax return is due November 15th or May 15th under an automatic extension.

Automatic extensions are allowed for up to six months following the prescribed filing date.

For example, a taxpayer with a fiscal year/tax year that is also a calendar year can use the automatic extension moving the due date of their return from May 15th to November 15th. So the TY 2014 return for a taxpayer whose fiscal year is calendar year 2014 would be due May 15th, 2015, but the taxpayer would have until November 15th to file under the automatic extension.

A taxpayer whose fiscal year/tax year ends June 30th can obtain an automatic six-month extension that moves the due date for its return from November 15th to May 15th of the following year. So the tax year 2014 return for a taxpayer whose fiscal year starts July 1st (in 2014) and goes through June 30th (of 2015) is due November 15th, 2015 but the taxpayer would have until May 15th, 2016 to file under automatic extension.

Companies with a tax liability of $5,000 or more must make quarterly estimated payments. For a corporation operating with a calendar year as its fiscal year/tax year, the due dates for quarterly payments are April 15th, June 15th, September 15th, and December 15th. For a corporation using another 12-month period as its fiscal/tax year, the due dates for quarterly installments are the 15th day of the 4th month, the 15th day of the 6th month, the 15th day of the 9th month, and the 15th day of the 12th month (15-31-502, MCA).

Penalties and Interest

Corporations that do not pay taxes when due may be charged a late payment penalty of 1.2 percent per month on the unpaid tax, up to a maximum penalty of 12 percent of the tax due. Interest on unpaid tax accrues at a rate of 12 percent per year, or at 1 percent per month or fraction of a month on the unpaid tax.

Maximum Corporate Tax Rate By State		
Rank	**State**	**Maximum Tax Rate**
1	Iowa*	12.00%
2	Pennsylvania	9.99%
3	Minnesota	9.80%
4	District of Columbia	9.40%
4	Alaska*	9.40%
5	New Jersey	9.00%
6	Maine *	8.93%
7	California	8.84%
8	Delaware	8.70%
9	New Hampshire	8.50%
9	Vermont *	8.50%
10	Maryland	8.25%
11	Louisiana *	8.00%
11	Massachusetts	8.00%
12	Wisconsin	7.90%
13	Nebraska *	7.81%
14	Illinois	7.75%
15	Oregon	7.60%
16	Connecticut	7.50%
17	Idaho	7.40%
18	Rhode Island	7.00%
19	**Montana**	**6.75%**
20	New Mexico*	6.60%
21	Indiana	6.50%
21	New York	6.50%
21	West Virginia	6.50%
21	Alabama	6.50%
21	Arkansas *	6.50%
21	Tennessee	6.50%
22	Hawaii *	6.40%
23	Missouri	6.25%
24	Kentucky *	6.00%
24	Georgia	6.00%
24	Michigan	6.00%
24	Oklahoma	6.00%
24	Virginia	6.00%
25	Arizona	5.50%
25	Florida	5.50%
26	Mississippi *	5.00%
26	South Carolina	5.00%
26	Utah	5.00%
27	Colorado	4.63%
28	North Dakota*	4.31%
29	North Carolina	4.00%
29	Kansas	4.00%

* Graduated income tax
As of Jan. 1, 2016, Federation of Tax Administrators

Comparison of Corporate Tax Rate with Other States

Forty-four states and the District of Columbia have a tax on corporate income. The comparison table in this section uses data from the Federation of Tax Administrators (as of January 1, 2016) to show the maximum rates for states that have a corporate tax. These go from 12 percent down to 4 percent. A number of states have a graduated income tax which is indicated by an asterisk next to the state. The ranking is done by rate, so states with the same tax rate have the same ranking.

Of course, what is shown in the table is only the maximum rate for each state. The effective or average tax rate in different states can vary substantially, depending upon what the lower rates are and what income they apply to. Furthermore, state tax deductions, exemptions and credits, and other aspects of state taxation policy can substantially reduce the effective tax rate.

Nevada and Wyoming do not have corporate income taxes.

Texas does not have a corporate income tax, but imposes a franchise tax based on gross revenues.

Ohio has adopted a commercial activity tax which is a tax on gross receipts. Washington has a business and occupation tax which also is a tax on gross receipts.

Montana's tax rate is 6.75 percent. Idaho's tax rate is 7.4 percent and North Dakota's top corporate income tax rate is 4.31 percent.

South Dakota does not have a general corporate income tax, but does have an excise tax on financial institutions which starts at 6 percent on net income of $400 million or less. The percentage tax declines in steps on net income over that amount.

As noted earlier, Wyoming does not have a corporate income tax, but does have a corporate franchise tax or license tax of 0.0002, which applies to the sum of capital, property, and assets located in Wyoming (in addition to a general property tax), and also has a relatively broad-based sales tax.

Select History of Corporate Income (License) Tax

The corporate license tax was established in 1917. The tax rate was 1 percent and there was no minimum tax.

In 1933, the rate was raised to 2 percent with a minimum tax of $5. In 1937, the rate was raised to 3 percent; the minimum tax remained $5. Twenty years later in 1957, the rate was raised to 5 percent and the minimum tax changed to $10. The tax rate was changed several times in the years between 1960 and 1971 and the minimum tax was increased from $10 to $50.

In 1987, the water's edge election, which includes a tax rate of 7 percent for corporations that elect to file as water's edge companies, was added.

Corporate Income Tax
Historic Tax Rates and Minimum Tax

Year	Tax Rate	Minimum Tax	Water's Edge
1987	6.75%	$50	7%
1971	6.75%	$50	--
1969	6.25%	$50	--
1965	5.25%	$10	--
1960	4.5%	$10	--
1957	5%	$10	--
1937	3%	$5	--
1933	2%	$5	--
1917	1%	--	--