INDIVIDUAL AND CORPORATE INCOME TAX
BIENNIAL REPORT - THE MONTANA DEPARTMENT OF REVENUE

Montana Department of
REVENUE

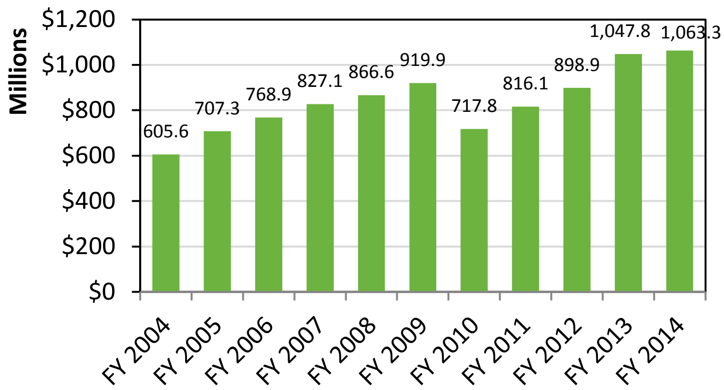
Overview of Individual Income Tax

The individual income tax is the largest source of state tax revenue. All income tax revenue is allocated to the state general fund, accounting for 51 percent of general fund revenue for FY 2014. 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 and in returns for 2009 is due to the national recession.

Individual Income Tax Collections

Fiscal Year	Total Revenue
FY 2004	$605,582,309
FY 2005	$707,343,333
FY 2006	$768,911,933
FY 2007	$827,095,302
FY 2008	$866,638,122
FY 2009	$919,896,762
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



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

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 married couples find their tax is lower if they file a joint federal return and separate Montana returns.

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 2011 Legislature affected the individual income tax:
House Bill 44 eliminated obsolete statutory language relating to tax credits for certain investments made before 1995.

House Bill 467 clarified that the contributions to the endowment funds of community colleges, tribal colleges, and technical colleges are eligible for the college contribution credit. The department had previously interpreted the law as allowing a credit for these contributions. However, the law did not explicitly list these institutions, and some donors may not have taken the credit because they did not think they were eligible.

Senate Bill 11 corrected an omission in Senate Bill 407, passed by the 2003 Legislature. SB 407 reduced income tax rates, but did not make the corresponding reduction in the withholding rate for lottery winnings. This resulted in lottery winners having income tax over-withheld and then refunded when they filed their returns. Senate Bill 11 reduced the withholding rate for lottery winnings to 6.9%, which is the top income tax rate.

Senate Bill 166 created a threshold of $200 of income tax liability before taxpayers who file a tax return and pay tax due by the extension deadline (generally October 15) owe penalty and interest for late filing, late payment, or underpayment through withholding or estimated payments.

Senate Bill 413 makes the due date for income tax returns and estimated payments the same as the IRS due date when the IRS due date is affected by a federal or District of Columbia holiday. The IRS deadline in April occasionally is affected by Emancipation Day, which is a holiday in the District of Columbia.

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 to the public. The credit is $500 per grant of access, with a maximum credit of $2,000 per taxpayer. This credit will first be 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.

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 subtracted.

The values of the taxpayer's exemptions and either itemized or standard deductions are subtracted 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 2010	$2,130	$1,770	$3,990	$3,540	$7,980
TY 2011	$2,190	$1,820	$4,110	$3,640	$8,220
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

Tax liability is calculated from the rate table. The rate table is adjusted for inflation each year:

Marginal Tax Rate Structure

Year	TY 2010	TY 2011	TY 2012	TY 2013	TY 2014
1% of the first	$2,600	$2,700	$2,700	$2,800	$2,800
2% of the next	$2,000	$2,000	$2,100	$2,100	$2,200
3% of the next	$2,300	$2,500	$2,500	$2,500	$2,600
4% of the next	$2,500	$2,500	$2,600	$2,700	$2,700
5% of the next	$2,700	$2,800	$2,800	$2,900	$3,000
6% of the next	$3,500	$3,500	$3,700	$3,700	$3,800
6.9% of remaining	NA	NA	NA	NA	NA

Marginal Tax Rate Income Limits

Year	TY 2010	TY 2011	TY 2012	TY 2013	TY 2014
1.0%	$2,600	$2,700	$2,700	$2,800	$2,800
2.0%	$4,600	$4,700	$4,800	$4,900	$5,000
3.0%	$6,900	$7,200	$7,300	$7,400	$7,600
4.0%	$9,400	$9,700	$9,900	$10,100	$10,300
5.0%	$12,100	$12,500	$12,700	$13,000	$13,300
6.0%	$15,600	$16,000	$16,400	$16,700	$17,100
6.9%	Unlimited	Unlimited	Unlimited	Unlimited	Unlimited

Any credits the taxpayer may claim are subtracted from the tax liability to give the net tax. Taxpayers with capital gains income are allowed a 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 2012 and 2013. 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 in 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
2012 and 2013

	2012		2013	
	Count	**Total**	**Count**	**Total**
Income Items				
Wage and salary income	425,171	$14,686,234,302	430,895	$15,189,765,954
Taxable interest income	210,367	$313,116,530	199,058	$294,150,425
Ordinary dividend income	115,986	$627,611,683	117,539	$550,135,312
Taxable refunds of state/local income taxes	99,170	$90,148,991	100,817	$89,267,424
Alimony received	850	$13,225,614	870	$15,065,175
Business income (Schedule C)	74,421	$740,893,800	76,294	$820,124,595
Capital gains income	105,833	$1,491,198,437	114,250	$1,314,178,279
Supplemental gains income	15,673	$53,107,823	16,672	$87,794,529
IRA distributions - Taxable amount	50,217	$618,963,597	51,581	$623,888,183
Pension and annuity income - Taxable amount	98,355	$1,840,957,494	100,330	$1,945,505,600
Rent, royalty, partnership, etc. income	98,670	$2,340,910,723	103,996	$2,554,830,019
Farm income	18,537	-$135,868,886	18,870	-$138,639,876
Unemployment compensation	36,502	$158,526,968	32,991	$129,933,369
Taxable social security benefits	75,231	$721,660,925	80,470	$803,830,707
Other income	43,954	-$552,854,708	43,391	-$523,590,495
Total income	535,648	$23,007,833,293	546,167	$23,756,239,200
Federal Adjustments to Income				
Educator expenses	10,909	$2,543,254	11,162	$2,674,808
Business expenses	640	$2,092,264	675	$1,945,823
Health savings account deduction	8,260	$25,616,255	8,592	$28,425,705
Moving expenses	3,230	$4,960,850	3,502	$5,789,550
One-half self-employment tax	60,276	$77,679,329	62,427	$84,415,172
Self-employed SEP, SIMPLE, and qual. plans	2,551	$41,584,610	2,758	$47,762,885
Self-employed health insurance deduction	22,225	$116,803,202	23,892	$132,130,435
Penalty on early withdrawal of savings	3,193	$2,107,438	2,761	$417,775
Alimony paid	1,199	$15,398,290	1,222	$16,013,124
IRA deduction	14,563	$56,077,309	15,113	$62,060,697
Student loan interest deduction	46,304	$38,303,590	48,245	$41,374,226
Tuition & fees deduction	6,164	$13,060,037	5,747	$12,198,697
Domestic production activities deduction	6,687	$47,736,036	7,306	$50,133,423
Federal write-ins	324	$1,554,002	335	$2,430,892
Total adjustments to income	139,849	$445,516,466	144,872	$487,773,212
Federal Adjusted Gross Income	535,699	$22,562,316,827	546,225	$23,268,465,988

Montana Individual Income Tax Additions Reported on Full Year Residents' Returns 2012 and 2013				
	2012		2013	
	Count	Total	Count	Total
Montana Additions to Federal Adjusted Gross Income				
Interest on other states' municipal bonds	16,391	$81,026,411	17,231	$91,030,099
Dividends not included in FAGI	3,589	$9,204,757	4,024	$10,455,799
Taxable federal refunds	90,651	$125,864,217	87,814	$119,788,229
Recoveries of amounts deducted in earlier years	173	$451,396	174	$267,044
Additions to federal taxable social security or railroad retirement	8,219	$13,655,410	8,935	$14,844,146
Allocation of compensation to spouse	477	$8,049,850	505	$8,032,567
Medical savings account nonqualified withdrawals	107	$144,311	84	$129,693
First-time homebuyer's account nonqualified withdrawals	*	$8,053	*	$50,177
Farm and ranch risk management account taxable distributions	*	$5,043	*	$1,003
Dependent care assistance credit adjustment	45	$66,238	35	$30,755
Smaller federal estate and trust taxable distributions	97	$544,475	85	$585,412
Federal net operating loss carryover	4,477	$433,483,298	4,365	$388,352,723
Federal taxes paid by your S. corporation	37	$93,491	35	$62,675
Title plant depreciation	*	$7,341	*	$1,607
Group health premiums reimbursed by Insure Montana credit	792	$3,669,598	705	$3,914,375
Other additions	4,204	$158,298,705	4,004	$166,060,653
Total Montana Additions	117,119	$834,572,594	115,622	$803,606,957

Montana Individual Income Tax Subtractions Reported on Full Year Residents' Returns 2012 and 2013				
	2012		2013	
	Count	Total	Count	Total
Montana Subtractions from Federal Adjusted Gross Income				
Federal bonds exempt interest	19,299	$22,275,353	19,022	$19,330,263
Exempt tribal income	7,023	$221,787,087	5,685	$170,919,136
Exempt unemployment compensation	36,502	$158,526,968	32,991	$129,933,369
Exempt worker's comp benefits	140	$918,240	138	$1,009,272
Capital gains from small business investment companies	16	$47,868	17	$173,389
State tax refunds included in FAGI	106,258	$95,200,093	107,642	$94,089,431
Recoveries of amounts deducted in earlier years	15	$33,272	14	$47,254
Exempt active duty military salary	4,565	$158,404,853	4,571	$164,472,809
Nonresident exempt military income	111	$3,862,257	127	$4,235,016
Exempt life insurance premiums reimbursement (National Guard)	41	$17,001	46	$28,091
Exempt pension income	45,185	$154,378,099	45,486	$158,597,172
Elderly interest exclusion	70,617	$33,021,476	71,577	$31,301,899
Exempt retirement disability income (under age 65)	60	$276,606	50	$226,388
Exempt tip income	15,410	$52,275,624	16,702	$56,390,533
Exempt income of child taxed to parent	109	$211,627	111	$264,493
Exempt health insurance premiums taxed to employee	193	$597,413	169	$791,972
Student loan repayments taxed to health care professional	283	$789,081	306	$880,391
Medical care savings account exempt deposits	7,647	$18,791,602	7,963	$19,801,670
First-time homebuyer exempt savings account deposits	187	$501,379	173	$501,702
Family education savings account exempt deposits	2,874	$6,838,715	4,017	$9,385,280
Farm and ranch risk management accounts exempt deposits	*	$0	*	$0
Subtraction to federal taxable social security/Tier 1 railroad retirement	36,365	$145,233,244	37,800	$156,201,788
Subtraction for federal taxable Tier II railroad retirement	3,037	$40,918,763	3,100	$43,719,325
Subtraction for spouse filing joint return: passive loss carryover	44	$255,077	43	$173,173
Subtraction for spouse filing joint return: capital loss adjustment	1,622	$3,168,626	1,508	$2,882,217
Allocation of compensation to spouse	491	$8,243,923	517	$8,175,290
Montana net operating loss carryover	3,978	$411,198,411	3,769	$353,739,856
40% capital gain exclusion on pre-1987 installment sales	55	$884,971	44	$148,686
Business expense of recycled material	113	$242,946	100	$366,958
Sales of land to beginning farmers	*	$6,796	*	$56,687
Larger federal estate and trust taxable distributions	141	$587,026	175	$623,005
Wage deduction reduced by federal targeted jobs credit	46	$264,065	54	$319,522
Certain gains recognized by liquidating corporation	*	$42,404	*	$4,616
Other subtractions	4,393	$166,239,698	4,591	$165,328,529
Total Montana Subtractions	251,206	$1,706,040,564	252,829	$1,594,119,182

Montana Individual Income Tax Deductions Reported on Full Year Residents' Returns 2012 and 2013				
	2012		2013	
	Count	Total	Count	Total
Deductions				
Deductible medical expenses	67,212	$296,883,350	58,740	$289,800,477
Medical insurance premiums not deducted elsewhere	103,705	$368,422,012	105,675	$388,204,675
Long-term care insurance premiums	13,344	$27,571,088	13,559	$29,433,415
Federal Income Tax				
Federal income tax withheld*	265,622	$1,763,740,518	270,808	$1,812,863,700
Federal income tax estimated payments*	46,692	$541,066,505	49,500	$710,451,220
Last year's federal income tax paid (e.g. with return)*	53,157	$308,648,524	59,658	$444,295,392
Federal income tax from previous years*	4,722	$18,611,381	4,395	$30,040,657
Total federal income tax deduction	292,377	$1,154,479,513	299,583	$1,206,778,981
State or local sales tax	400	$346,741	366	$404,334
Local income taxes	233	$102,533	199	$136,620
Real estate taxes	208,472	$407,127,118	212,292	$427,375,562
Personal property taxes	166,662	$52,294,545	170,827	$54,011,758
Other deductible taxes	24,184	$8,398,699	23,103	$8,636,652
Home mortgage interest	184,880	$958,035,238	162,335	$907,275,526
Qualified mortgage insurance premiums	19,282	$20,286,561	23,762	$29,921,640
Investment interest	7,929	$25,707,920	8,763	$30,659,925
Contributions by cash or check	167,727	$458,318,428	170,729	$487,024,879
Contributions other than cash or check	73,904	$68,366,539	77,610	$75,236,737
Carryover of contributions from previous years	3,466	$40,198,253	3,522	$36,604,717
Child and dependent care expenses	771	$1,452,494	748	$1,447,271
Casualty and theft losses	355	$7,131,478	530	$5,869,942
Business Expenses				
Unreimbursed employee business expenses*	58,698	$196,756,052	57,994	$197,814,067
Other business expenses*	145,558	$125,972,713	148,396	$148,307,298
Total business expenses*	165,844	$322,728,765	168,609	$346,121,365
Net deductible unreimbursed business expenses	58,266	$223,212,369	59,412	$239,109,524
Political contributions	11,563	$1,082,429	6,927	$643,188
All other miscellaneous deductions not subject to 2% floor	2,408	$5,892,109	2,572	$5,102,567
Gambling losses	1,248	$12,064,570	1,512	$17,520,929
Total itemized deductions	317,344	$4,137,373,987	324,165	$4,241,199,319
Unallowed itemized deductions (due to income over threshold)	0	$0	8,564	$52,237,202
Allowable itemized deductions	317,344	$4,137,373,987	324,165	$4,188,962,117
Standard deductions	199,049	$741,401,666	202,137	$775,951,691
Total deductions	531,230	$4,878,775,653	541,845	$4,964,913,808

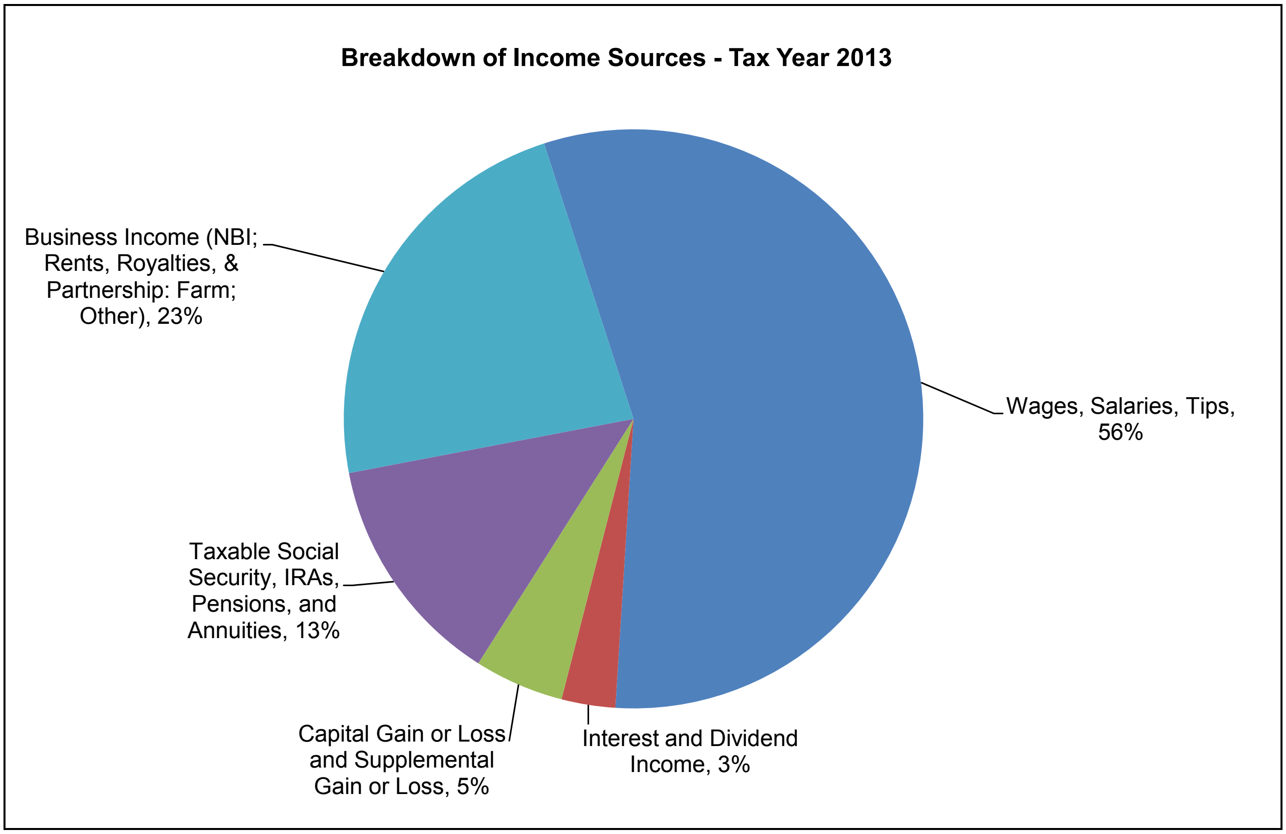
* Items either are part of another line or include another line. They are not part of the total.

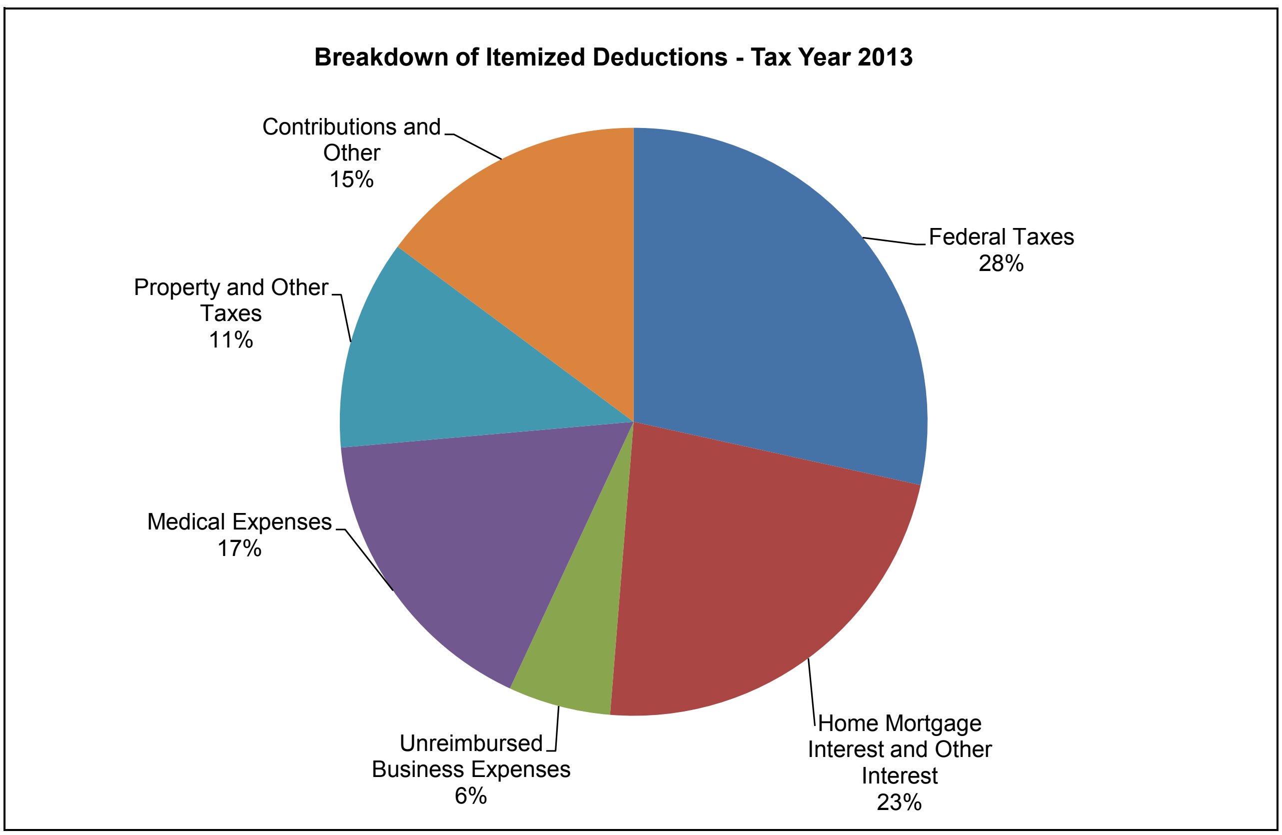
Montana Individual Income Tax Exemptions, Taxable Income, Tax, and Payments Reported on Full Year Residents' Returns 2012 and 2013				
	2012		2013	
	Count	Total	Count	Total
Exemptions *				
Self Exemption		537,294		547,927
Self 65 and Over Exemption		97,094		102,482
Self Blind Exemption		1,173		1,109
Total Taxpayer Exemptions	537,294	635,561	547,927	651,518
Spouse Exemption		181,682		84,303
Spouse 65 and Over Exemption		35,040		22,435
Spouse Blind Exemption		319		251
Total Spouse Exemptions	83,794	105,719	84,303	106,989
Dependent Exemptions	128,776	230,927	130,181	233,612
Total Exemptions	537,294	972,207	547,927	992,119
Value of Exemptions		$2,177,221,760		$2,261,782,800
Taxable Income				
Federal Adjusted Gross Income	535,699	$22,562,316,827	546,225	$23,268,465,988
+Montana Additions	117,119	$834,572,594	115,622	$803,606,957
-Montana Subtractions	251,206	$1,706,040,564	252,829	$1,594,119,182
-Deductions	531,230	$4,878,775,653	541,845	$4,964,913,808
-Value of Exemptions	537,077	$2,177,221,760	547,822	$2,261,782,800
Montana Taxable Income	446,210	$15,975,258,728	547,770	$16,500,226,913
Tax from Tax Table	445,539	$903,587,007	458,181	$929,255,001
Capital Gains Credit	61,723	$31,235,460	77,329	$27,523,134
Tax before Credits & Adjustments	442,375	$874,592,487	453,770	$903,838,419
Tax on Lump Sum Distributions	49	$2,949	56	$8,147
Recapture of Credits Claimed Previously	16	$7,304	9	$4,770
Total Tax		$874,602,740		$903,851,336
Payments				
Montana income tax withheld from wages	423,801	$686,918,324	433,206	$721,350,171
Tax withheld from mineral royalties	2,563	$3,403,373	2,819	$4,812,094
Tax withheld by pass-through entities	175	$324,289	245	$545,243
Estimated tax payments	44,916	$173,262,163	48,515	$197,361,333
Extension payments	4,995	$30,495,081	6,040	$32,051,015
Total Payments		$894,403,230		$956,119,856

* 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. Only the total number of taxpayer and spouse exemptions was recorded. 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
2012 and 2013

	2012		2013	
	Count	Total	Count	Total
Credits				
Non-Refundable and No Carryover				
Other states' income tax credit	11,316	$23,668,111	13,106	$27,082,006
College contribution tax credit	2,969	$246,495	3,131	$269,473
Qualified endowment tax credit	664	$2,049,386	671	$2,073,344
Energy conservation tax credit	12,887	$4,510,918	12,287	$4,536,016
Alternative fuel tax credit	23	$14,778	20	$8,183
Insurance for uninsured Montanan's credit	192	$171,365	180	$165,558
Elderly care tax credit	48	$52,714	45	$74,466
Recycling tax credit	93	$368,940	92	$289,907
Oil seed crushing/biodiesel facility credit	*	$0	*	$0
Biodiesel blending/storage tank credit	*	$0	*	$2,250
Non-Refundable but with Carryover				
Contractor's gross receipts tax credit	691	$4,743,249	665	$5,099,858
Geothermal systems tax credit	298	$344,548	249	$313,920
Alternative energy systems credit	626	$347,322	1,159	$632,607
Alternative energy production tax credit	*	$11,684	*	$56
Dependent care assistance credit	10	$95,590	12	$13,525
Historic property preservation tax credit	28	$199,776	37	$492,477
Infrastructure user fee credit	*	$20,990	*	$21,203
Empowerment zone credit	*	$0	*	$0
Research activities tax credit	*	$125,170	*	$73,983
Mineral exploration tax credit	*	$0	*	$0
Film production employment tax credit	*	$0	*	$0
Adoption credit	229	$189,721	244	$210,765
Total Non-Refundable Credits	29,156	$37,160,757	30,390	$41,359,597
Refundable Credits				
Elderly homeowner/renter tax credit				
Claimed with Income Tax Return	15,025	$7,183,795	13,875	$6,610,064
Claimed without Income Tax Return	5,599	$2,352,376	4,707	$1,786,064
Film production employment tax credit	*	$23,924	*	$55,391
Film qualified expenditure tax credit	*	$0	*	$15,150
Insure Montana small business health insurance credit	782	$1,876,550	701	$2,028,400
Emergency lodging credit	*	$0	*	$0
Total Refundable Credits	15,804	$11,436,645	14,577	$10,495,069
Total Credits	43,631	$48,597,402	43,662	$51,854,666


Breakdown of Income Sources - Tax Year 2013
Business Income (NBI; Rents, Royalties, & Partnership: Farm; Other), 23%
Wages, Salaries, Tips, 56%
Taxable Social Security, IRAs, Pensions, and Annuities, 13%
Capital Gain or Loss and Supplemental Gain or Loss, 5%
Interest and Dividend Income, 3%


Breakdown of Itemized Deductions - Tax Year 2013
Contributions and Other 15%
Federal Taxes 28%
Property and Other Taxes 11%
Medical Expenses 17%
Unreimbursed Business Expenses 6%
Home Mortgage Interest and Other Interest 23%

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
2012 and 2013

	2012				2013			
Decile Group	Returns	Income Range	Montana Adjusted Gross Income $ million	% of total	Returns	Income Range	Montana Adjusted Gross Income $ million	% of total
1	53,729	less than $3,721	-$656.2	-3%	54,792	less than $4,051	-$556.4	-2%
2	53,729	$3,721 to $8,976	$342.6	2%	54,793	$4,051 to $9,458	$371.0	2%
3	53,730	$8,977 to $14,212	$621.4	3%	54,793	$9,459 to $14,898	$665.9	3%
4	53,729	$14,213 to $19,876	$913.0	4%	54,792	$14,899 to $20,748	$973.5	4%
5	53,730	$19,877 to $26,162	$1,233.0	6%	54,793	$20,749 to $27,276	$1,311.0	6%
6	53,729	$26,163 to $33,944	$1,607.2	7%	54,793	$27,277 to $35,263	$1,706.5	8%
7	53,729	$33,945 to $43,062	$2,060.0	9%	54,792	$35,264 to $44,678	$2,180.6	10%
8	53,730	$43,063 to $55,197	$2,619.7	12%	54,793	$44,679 to $57,302	$2,771.8	12%
9	53,729	$55,198 to $77,702	$3,484.0	16%	54,793	$57,303 to $80,880	$3,697.5	16%
10	53,730	more than $77,702	$9,466.3	44%	54,793	more than $80,880	$9,356.6	42%
All	537,294		$21,690.8		547,927		$22,478.0	

Deductions by Decile Group
Full Year Residents
2012 and 2013

	2012					2013				
Decile Group	% Returns Itemize	Itemized Deductions $ million	Itemized Deductions average	Standard Deductions $ million	Standard Deductions average	% Returns Itemize	Itemized Deductions $ million	Itemized Deductions average	Standard Deductions $ million	Standard Deductions average
1	34%	$140.4	$7,728	$79.4	$2,233	34%	$139.4	$7,466	$81.4	$2,252
2	29%	$97.1	$6,322	$82.8	$2,157	29%	$100.9	$6,324	$85.7	$2,206
3	38%	$138.1	$6,798	$88.2	$2,638	38%	$141.7	$6,808	$93.3	$2,747
4	42%	$172.7	$7,701	$108.9	$3,480	42%	$177.3	$7,792	$116.0	$3,621
5	47%	$211.7	$8,331	$121.2	$4,279	47%	$211.2	$8,271	$128.5	$4,392
6	60%	$297.7	$9,240	$101.7	$4,728	60%	$295.1	$8,993	$106.9	$4,863
7	77%	$438.8	$10,543	$69.6	$5,750	78%	$473.8	$11,036	$71.0	$5,982
8	87%	$588.0	$12,621	$47.1	$6,594	87%	$596.3	$12,551	$49.1	$6,740
9	92%	$747.5	$15,151	$29.5	$6,710	92%	$761.9	$15,141	$31.0	$6,921
10	96%	$1,305.3	$25,225	$13.1	$6,582	96%	$1,291.4	$24,440	$13.1	$6,725
All	60%	$4,137.4	$11,533	$741.4	$3,463	60%	$4,189.0	$11,437	$776.0	$3,563

Deductions as Percent of Montana Adjusted Gross Income Full Year Residents 2012 and 2013						
	2012			2013		
Decile Group	Itemized Deductions	Standard Deductions	All	Itemized Deductions	Standard Deductions	All
1	-27%	-56%	-33%	-33%	-62%	-40%
2	96%	34%	53%	91%	33%	50%
3	58%	23%	36%	56%	23%	35%
4	45%	21%	31%	44%	20%	30%
5	36%	19%	27%	34%	18%	26%
6	31%	16%	25%	29%	16%	24%
7	27%	15%	25%	28%	15%	25%
8	26%	14%	24%	25%	13%	23%
9	23%	10%	22%	22%	10%	21%
10	14%	5%	14%	14%	5%	14%
All	23%	20%	22%	23%	20%	22%

Taxable Income and Tax Full Year Residents 2012 and 2013												
	2012						2013					
Decile Group	Taxable Income			Tax Liability			Taxable Income			Tax Liability		
	$ million	Average	% of Total	$ million	Average	% of Total	$ million	Average	% of Total	$ million	Average	% of Total
1	$0.4	$7	0%	$0.0	$0	0%	$0.4	$8	0%	$0.0	$0	0%
2	$80.8	$1,504	1%	$1.0	$18	0%	$93.6	$1,708	1%	$1.1	$20	0%
3	$254.4	$4,735	2%	$4.7	$88	1%	$279.5	$5,101	2%	$5.3	$97	1%
4	$458.4	$8,531	3%	$12.0	$223	1%	$500.0	$9,125	3%	$13.3	$243	1%
5	$712.7	$13,265	4%	$24.6	$458	3%	$775.3	$14,149	5%	$27.4	$499	3%
6	$1,020.3	$18,990	6%	$43.3	$806	5%	$1,100.1	$20,078	7%	$47.4	$865	5%
7	$1,343.0	$24,997	8%	$64.5	$1,201	7%	$1,440.9	$26,297	9%	$69.9	$1,276	8%
8	$1,765.6	$32,861	11%	$93.0	$1,731	11%	$1,894.8	$34,582	11%	$100.5	$1,833	11%
9	$2,466.4	$45,905	15%	$140.5	$2,615	16%	$2,654.0	$48,437	16%	$151.8	$2,771	17%
10	$7,873.3	$146,534	49%	$490.9	$9,136	56%	$7,761.6	$141,653	47%	$487.1	$8,890	54%
All	$15,975.3	$29,733		$874.6	$1,628		$16,500.2	$30,114		$903.8	$1,650	

Tax As Percent of Adjusted Gross Income Full Year Residents 2012 and 2013						
	2012			2013		
Decile Group	Montana Adjusted Gross Income	Tax Liability	Tax / Income	Montana Adjusted Gross Income	Tax Liability	Tax / Income
	$ million	$ million	%	$ million	$ million	%
1	-$656.2	$0.0	0.0%	-$556.4	$0.0	0.0%
2	$342.6	$1.0	0.3%	$371.0	$1.1	0.3%
3	$621.4	$4.7	0.8%	$665.9	$5.3	0.8%
4	$913.0	$12.0	1.3%	$973.5	$13.3	1.4%
5	$1,233.0	$24.6	2.0%	$1,311.0	$27.4	2.1%
6	$1,607.2	$43.3	2.7%	$1,706.5	$47.4	2.8%
7	$2,060.0	$64.5	3.1%	$2,180.6	$69.9	3.2%
8	$2,619.7	$93.0	3.6%	$2,771.8	$100.5	3.6%
9	$3,484.0	$140.5	4.0%	$3,697.5	$151.8	4.1%
10	$9,466.3	$490.9	5.2%	$9,356.6	$487.1	5.2%
All	$21,690.8	$874.6	4.0%	$22,478.0	$903.8	4.0%

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 income has its source in that jurisdiction. For example, suppose a company harvests timber and mills it into lumber in Montana and

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.

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[2] 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 called a *water's-edge election.* When a group makes this election, it is only required to include affiliates in its combined

2 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.

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%.

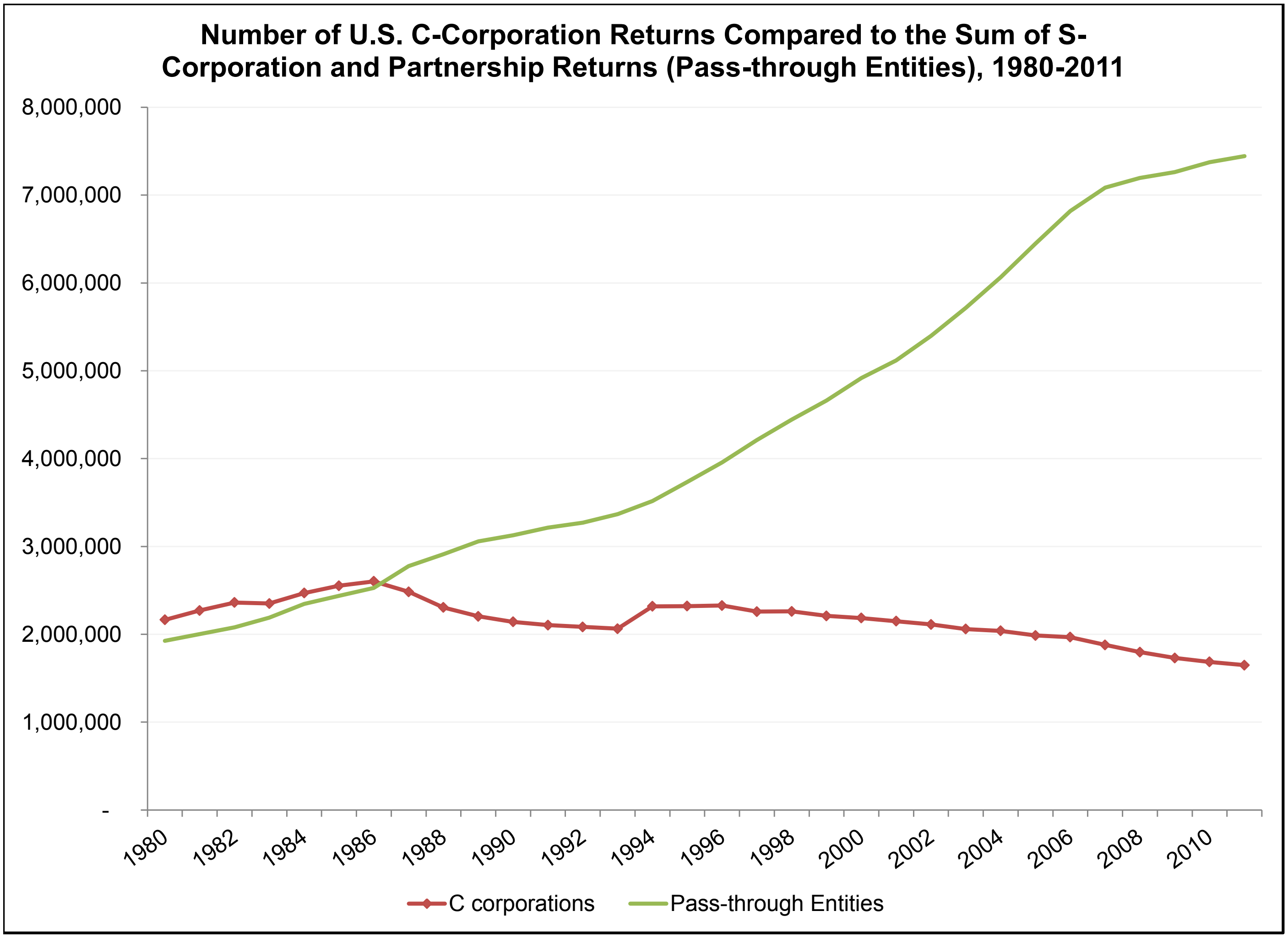
Abusive tax shelters are arrangements where taxpayers mischaracterize either income or gains and losses in order to avoid taxes. While nothing about pass-through entities or tiered business ownership creates abusive tax shelters, individuals and corporations wanting to evade taxes have used the complexity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

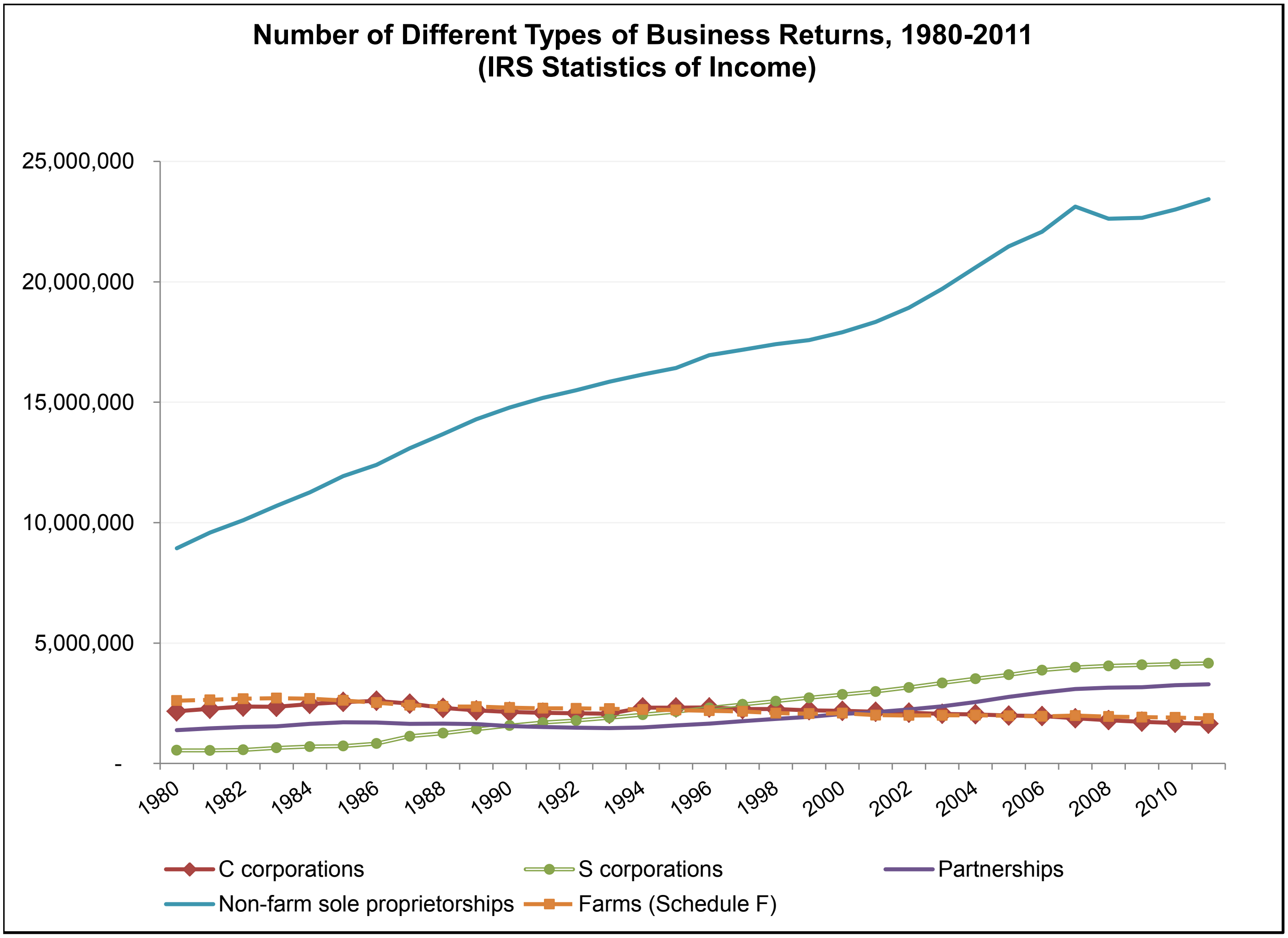
U.S. courts have consistently ruled that these types of sham transactions with no economic purpose other than evading taxes should be ignored for U.S. tax purposes.

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 and S corporations) from 1980 through 2010 (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 and 2011 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, 1980–2011, 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 just over 23.4 million in 2011.

Sole proprietorships, just 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, 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 went from 2.6 million in 1980 to 1.8 million in 2011. 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 1.65 million in 2011. One thing to note is that C corporations in Montana seem to vary greatly in terms of size – there are large or very 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 million in 2011, an annual growth rate of 7 percent. Partnerships grew more slowly – increasing from 1.4 million in 1980 to 3.4 million in 2011.

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, going from 1,691 returns in 1980 to 15,022 returns in 2010.

Businesses of all sizes can be C corporations or pass-through entities. Sole proprietor businesses generally are small. For 2008, the IRS reports that average receipts were $4.9 million for C corporations, $1.9 million for partnerships, and $1.5 million for S corporations, but only $58,000 for sole proprietor businesses. Many sole-proprietor businesses are part-time or a sideline for the owner. For 2013, 75% of taxpayers whose Montana income tax returns showed income or loss from a sole-proprietor business reported more income from other sources.

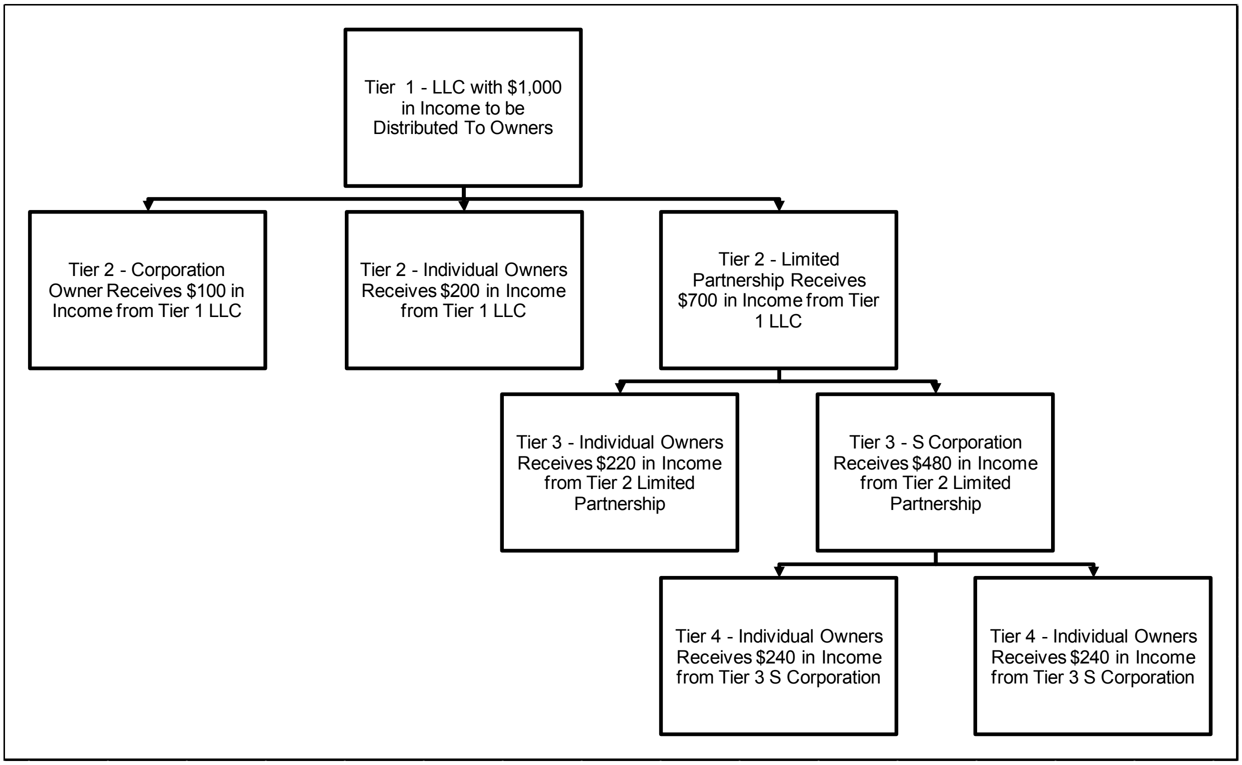
Ownership, Income, Deductions and Credits Reported on Montana Pass-Through Returns

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, or 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 are generally treated as partnerships, although LLCs with two or more members can elect to be treated as S corporations. Any single member LLC can elect to be 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, a tiered business structure is created.

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, an 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 classified as S corporations or partnerships with Montana source income are required to file an information return each year. If this entity has a partner, shareholder, member or other owner who is a non-resident individual, foreign C corporation, or a pass-through entity with an owner, or shareholder, that is a non-resident individual or foreign C corporation, the pass-through entity is also required to file with the state an agreement with the individual non-resident 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. If this agreement is not met, the pass-through entity must in all subsequent tax years withhold the appropriate amount and remit the tax payment directly to the state (15-30-3313, MCA).

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 source 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. However, some types of pass-through entities that can be owned by other business entities can elect to be treated as S corporations for tax purposes. The table to the right shows the number of owners associated with Montana's pass-throughs 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.

Shares of Pass-Through Owners by Residency Status

Type of Owner	Number	%
Resident Individuals	80,748	31%
Non-Resident Individuals	119,777	46%
Montana Business Entities	5,755	2%
Non-Montana Business Entities	56,822	22%
Total	263,102	100%

Of the approximately 263,000 pass-throughs filing informational returns in Montana during 2012, nearly 31 percent reported having individual residents of Montana as pass-through owners. Non-resident individuals are the largest group of Montana's pass-through owners, with 119,777 reported owners. Just over 5,750 Montana business entities were listed as owners of pass-throughs according to informational tax returns. More than 56,000 non-Montana business entities were owners of pass-throughs with Montana source income. Overall, individuals comprised 76 percent of the owners associated with Montana's pass-throughs, which is a slight decrease from the previous year's 78 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	37,753	88%	1,555	6%	40,377	44%	1,063	1%
Non-Resident Individuals	4,410	10%	19,615	81%	30,805	33%	64,947	63%
Montana Business Entities	668	2%	48	0%	4,784	5%	255	0%
Non-Montana Business Entities	236	1%	3,130	13%	16,144	18%	37,312	36%
Total	43,067	100%	24,348	100%	92,110	100%	103,577	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 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 2012. Income and other items passed through to two or more entities are only counted once.

Montana-Source Income Passed Through To Owners, 2012 Net of Distributions from First-Tier to Second-Tier Pass-Throughs				
	S Corporations		**Partnerships**	
	Montana	Multi-State	Montana	Multi-State
Returns	23,949	5,893	20,110	4,690
Income Items				
Salaries and Other Fixed Payments to Owners	-$15,209,085	-$2,776,139	$307,900,209	$249,138,535
Ordinary Business Income	$1,396,036,984	$479,691,120	$777,850,325	$1,092,294,449
Rental Income				
Real Estate	$37,303,473	$9,244,419	-$77,137,526	-$77,422,455
Other	-$3,976,255	$1,488,819	$10,050,975	$28,869,034
Interest	$29,326,357	$13,207,630	$2,092,602,056	$1,147,975,331
Dividends	$15,691,596	$55,507,698	$2,308,848,598	$1,127,430,131
Royalties	$9,223,964	$13,310,917	$206,151,637	$79,358,538
Capital Gains	$47,750,591	$123,524,883	$10,016,932,453	$5,049,324,003
Gains Taxed as Ordinary Income	$190,832,933	$69,075,944	$1,311,610,695	$1,215,537,222
Other Income	-$2,521,581	$6,291,220	$3,092,956,056	$2,276,768,246
Total	$1,704,458,978	$768,566,511	$20,047,765,476	$12,189,273,035
Montana Additions to Federal Income				
Interest on Non-Montana Municipal Bonds	$1,844,697	$479,034	$17,176,862	$17,163,656
State and Local Income Taxes	$2,630,933	$1,408,042	$1,229,464	$12,871,412
Other	$3,434,826	$1,652,637	$66,084,155	$5,154,936
Total	$7,910,457	$3,539,712	$84,490,481	$35,190,004
Montana Subtractions from Federal Income				
Interest on Federal Bonds	$5,379,674	$1,501,033	$32,577,530	$28,203,969
Purchases of Recycled Materials	$518,486	$363,249	$12,546	$751
Other	$72,969,832	$24,420,512	$450,615,066	$131,545,685
Total	$78,867,992	$26,284,794	$483,205,143	$159,750,406
Deductions				
Expensing of Capital Purchases	$298,544,483	$65,123,402	$892,998,013	$612,546,904
Contributions	$21,553,633	$7,094,587	$44,852,484	$53,215,952
Interest on Funds Borrowed to Make Investments	$11,835,049	$4,296,457	$1,301,985,769	$518,904,543
Other	$26,624,370	$41,069,116	$2,905,530,295	$1,428,576,624
Total	$358,557,535	$117,583,562	$5,145,366,561	$2,613,244,022
Total Net Montana Source Income	**$1,274,943,907**	**$628,237,868**	**$14,503,684,254**	**$9,451,468,610**

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 2012. Credits actually claimed by owners are included in the credits claimed against individual income tax and corporation income tax.

Tax Credits Passed Through To Owners, 2012 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	$9,893	$1,380	$2,137	$510
Insurance for Uninsured Montanans Credit	$112,941	$4,955	$20,268	$4,920
Credit for Investment in Recycling Equipment	$331,399	$28,827	$147,030	$6,250
Alternative Energy Production Credit	$14,288	$0	$14,590	$0
Contractors' Gross Receipts Credit	$2,495,745	$1,069,911	$193,444	$7,969
Alternative Fuel Credit	$0	$0	$1,000	$0
Infrastructure Users Fee Credit	$0	$0	$35,609	$0
Charitable Endowment Contribution Credit	$0	$0	$0	$0
Historic Building Preservation Credit	$7,020	$0	$178,162	$0
Increased Research Activity Credit	$0	$0	$0	$0
Mineral Exploration Credit	$0	$0	$0	$0
Empowerment Zone Credit	$0	$0	$0	$0
Film Production Credit	$31,816	$47,848	$0	$0
Biodiesel Blending Credit	$0	$0	$0	$0
Oilseed Crushing Credit	$0	$0	$0	$0
Insure Montana Credit	$1,351,347	$52,646	$173,692	$0
Temporary Emergency Lodging Credit	$0	$0	$0	$0
Total	**$4,354,448**	**$1,205,567**	**$765,932**	**$19,649**

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 is engaged in.[1] The next table provides a list of the Montana source income that was distributed by Montana's S corporations in 2012, broken down by industry sector type. As can be seen from the tax return information, 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 $490 million in 2012. The Financial Activities and Professional and Business Services S corporations also provided a significant amount of income to their owners, passing through $293.2 million and $284.9 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, 2012 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	2,941	5,579	1,128	4,810	398	3,979	5,096	1,622	2,257	1,588	444
Income Items											
Salaries and Other Fixed Payments to Owners	-$0.2	-$0.3	-$0.1	-$4.9	$0.0	-$4.4	-$3.0	-$4.8	-$0.2	-$0.2	$0.0
Ordinary Business Income	$208.7	$245.1	$73.6	$495.1	$22.2	$146.4	$400.4	$113.0	$88.2	$78.9	$4.1
Rental Income											
Real Estate	$10.7	$0.6	$0.5	$5.9	$0.1	$22.9	$4.4	$0.5	$0.7	$0.2	-$0.1
Other	-$3.4	$0.5	$1.6	$5.3	$0.0	-$6.5	$0.0	$0.0	$0.3	-$0.2	$0.0
Interest	$3.9	$3.7	$1.2	$7.6	$0.3	$9.2	$10.4	$1.2	$2.3	$2.6	$0.1
Dividends	$1.4	$0.6	$6.3	$4.0	$0.1	$51.4	$3.5	$0.1	$0.2	$3.5	$0.0
Royalties	$10.3	$0.1	$0.6	$0.2	$0.1	$10.3	$0.7	$0.0	$0.3	$0.0	$0.0
Capital Gains	$16.5	$5.9	$5.0	$21.5	$0.5	$79.7	$23.6	$3.7	$3.3	$11.4	$0.3
Gains Taxed as Ordinary Income	$103.5	$1.3	$11.5	$27.0	$4.1	$72.2	$28.1	$0.5	$9.6	$2.0	$0.1
Other Income	$8.7	$1.4	$0.1	-$16.2	$0.0	$7.6	$1.9	$0.0	$0.1	$0.1	$0.0
Total	$360.0	$259.0	$100.4	$545.4	$27.5	$389.0	$470.0	$114.1	$104.8	$98.4	$4.4
Montana Additions to Federal Income											
Interest on Non-Montana Municipal Bonds	$0.2	$0.2	$0.0	$0.1	$0.0	$0.4	$1.4	$0.0	$0.0	$0.0	$0.0
State and Local Income Taxes	$0.5	$0.3	$0.2	$0.3	$0.1	$2.1	$0.5	$0.0	$0.1	$0.0	$0.0
Other	$0.6	$0.7	$0.1	$1.3	$0.5	$0.5	$0.9	$0.2	$0.1	$0.3	$0.0
Total	$1.3	$1.2	$0.3	$1.6	$0.6	$2.9	$2.8	$0.2	$0.2	$0.3	$0.0
Montana Subtractions from Federal Income											
Interest on Federal Bonds	$0.0	$0.1	$0.0	$0.0	$0.0	$0.6	$4.8	$0.0	$0.0	$1.3	$0.0
Purchases of Recycled Materials	$0.2	$0.1	$0.4	$0.1	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Other	$10.9	$1.8	$0.3	$3.1	$0.2	$32.9	$46.5	$0.3	$1.1	$0.3	$0.0
Total	$11.2	$2.0	$0.7	$3.2	$0.2	$33.5	$51.3	$0.3	$1.2	$1.5	$0.0
Deductions											
Expensing of Capital Purchases	$102.7	$49.4	$9.3	$46.0	$1.0	$12.3	$106.8	$10.2	$16.0	$9.3	$0.6
Contributions	$2.4	$4.3	$1.3	$6.9	$0.4	$4.9	$4.5	$1.6	$1.5	$0.9	$0.0
Interest on Funds Borrowed to Make Investments	$0.0	$0.7	$0.0	$0.2	$0.0	$6.0	$9.0	$0.0	$0.1	$0.1	$0.0
Other	$5.8	-$0.1	$0.1	$0.7	$0.1	$41.9	$16.3	$0.3	$0.4	$2.3	$0.0
Total	$111.0	$54.3	$10.7	$53.8	$1.5	$65.1	$136.6	$12.0	$17.9	$12.6	$0.7
Total Net Montana Source Income	**$239.2**	**$203.9**	**$89.3**	**$490.1**	**$26.3**	**$293.2**	**$284.9**	**$102.0**	**$85.9**	**$84.5**	**$3.7**

As can be seen in the next table, the amount of pass-through income also varies significantly for Montana's pass-through partnerships. In 2012, the Financial Activity partnerships generated a little more than $23 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 pass-through sector reported negative pass-through income for their owners. In 2012, the Unknown/Public Administration sector reported a net income loss of $37.8 million.

Montana-Source Income Passed Through to Owners, 2012
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	3,611	1,278	454	1,718	245	13,141	1,697	413	1,210	589	444
Income Items											
Salaries and Other Fixed Payments to Owners	$17.8	$14.5	$3.6	$23.4	$2.0	$410.2	$38.6	$31.3	$11.0	$4.1	$0.5
Ordinary Business Income	$214.6	$13.0	$45.8	$105.1	$70.7	$1,513.6	-$182.3	$97.5	$25.9	$9.3	-$43.2
Rental Income											
Real Estate	$19.7	-$0.1	$0.2	$1.0	$0.2	-$180.4	$1.6	$0.0	$2.5	$0.8	-$0.1
Other	$3.7	$0.2	$0.2	$0.8	-$1.0	$37.1	-$2.6	$0.0	$0.4	$0.1	$0.2
Interest	$5.6	$0.6	$2.7	$2.2	$2.5	$3,145.6	$75.0	$0.5	$5.3	$0.1	$0.3
Dividends	$1.7	$0.1	$28.8	$2.4	-$0.1	$3,215.7	$181.2	$0.0	$5.5	$0.3	$0.7
Royalties	$60.8	$0.0	$7.0	$0.1	-$1.8	$214.0	$0.3	$0.1	$0.0	$4.1	$0.8
Capital Gains	-$25.7	$0.8	$4.6	$12.1	-$9.0	$14,916.7	$152.2	$6.3	$3.5	$2.1	$2.7
Gains Taxed as Ordinary Income	$109.4	$0.9	$4.2	-$28.3	$0.6	$2,398.2	$26.0	$10.2	$3.7	$0.6	$1.6
Other Income	$8.2	$2.7	$0.1	$129.8	-$0.6	$5,207.4	$22.8	$0.5	-$1.4	$0.3	$0.0
Total	$415.8	$32.6	$97.3	$248.6	$63.6	$30,878.0	$312.8	$146.3	$56.4	$21.8	-$36.4
Montana Additions to Federal Income											
Interest on Non-Montana Municipal Bonds	$0.6	$0.0	$0.2	$0.0	$0.0	$32.9	$0.3	$0.0	$0.0	$0.1	$0.0
State and Local Income Taxes	$0.1	$0.1	$0.1	$0.1	$0.1	$16.8	-$3.4	$0.1	$0.0	$0.1	$0.0
Other	$0.1	$0.0	$0.0	$0.2	$0.4	$65.9	$4.5	$0.0	$0.1	$0.0	$0.0
Total	$0.9	$0.1	$0.4	$0.3	$0.6	$115.6	$1.4	$0.1	$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	$61.6	-$0.9	$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	$20.8	$0.0	$1.4	$0.7	$0.0	$553.4	$5.0	$0.0	$0.7	$0.0	$0.0
Total	$20.9	$0.0	$1.4	$0.7	$0.0	$615.0	$4.1	$0.0	$0.7	$0.0	$0.0
Deductions											
Expensing of Capital Purchases	$204.4	$5.2	$3.2	$8.8	$1.3	$1,266.2	$7.5	$3.3	$3.6	$1.8	$0.2
Contributions	$6.0	$0.4	$0.2	$1.1	$0.2	$81.2	$6.2	$0.3	$1.5	$0.8	$0.0
Interest on Funds Borrowed to Make Investments	$2.9	$0.0	$0.0	$0.1	$0.0	$1,799.7	$17.2	$0.1	$0.9	$0.0	$0.0
Other	$51.4	$13.6	$2.1	$5.5	$21.3	$4,205.0	$26.2	$3.8	$3.5	$0.5	$1.1
Total	$264.8	$19.2	$5.5	$15.5	$22.9	$7,352.1	$57.2	$7.4	$9.5	$3.2	$1.4
Total Net Montana Source Income	**$131.1**	**$13.4**	**$90.8**	**$232.7**	**$41.3**	**$23,026.6**	**$253.0**	**$139.0**	**$46.3**	**$18.8**	**-$37.8**

The following two tables provide an industry level breakdown of the credits claimed by Montana's S corporation and partnership pass-throughs. 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 Charitable Endowment Contribution, Increased Research Activity or Temporary Emergency Lodging credits. However, there are some credits that 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 Film Production, Infrastructure Users Fee and Historic Building Preservation credits were only claimed by pass-throughs in one, or two, industry sectors.

Tax Credits Passed Through to Owners, 2012, 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	$500	$989	$398	$2,155	$200	$1,800	$3,170	$904	$897	$260	$0
Insurance for Uninsured Montanans Credit	$600	$17,211	$7,552	$17,414	$1,572	$10,789	$33,387	$20,696	$125	$5,127	$3,423
Credit for Investment in Recycling Equipment	$0	$0	$52,904	$211,095	$1,139	$0	$84,919	$0	$10,169	$0	$0
Alternative Energy Production Credit	$0	$430	$0	$0	$0	$0	$0	$0	$13,858	$0	$0
Real Estate	$124,428	$3,367,980	$1,023	$59,274	$0	$146	$6,472	$0	$3,066	$3,267	$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
Charitable Endowment Contribution Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Historic Building Preservation Credit	$0	$0	$0	$0	$0	$7,020	$0	$0	$0	$0	$0
Increased Research Activity 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	$79,664	$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	$84,780	$259,739	$30,456	$288,199	$6,772	$87,258	$308,611	$113,315	$86,886	$133,703	$4,274
Temporary Emergency Lodging Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Total	**$210,308**	**$3,646,349**	**$92,333**	**$578,137**	**$89,347**	**$107,013**	**$436,559**	**$134,915**	**$115,001**	**$142,357**	**$7,697**

Tax Credits Passed Through to Owners, 2012, 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	$960	$0	$0	$30	$0	$1,572	$0	$85	$0	$0	$0
Insurance for Uninsured Montanans Credit	$165	$1,091	$0	$1,540	$3,116	$900	$14,953	$2,043	$480	$900	$0
Credit for Investment in Recycling Equipment	$0	$0	$21,913	$116,405	$14,962	$0	$0	$0	$0	$0	$0
Real Estate	$0	$0	$0	$0	$0	$13,090	$0	$1,500	$0	$0	$0
Other	$0	$201,008	$0	$0	$0	$0	$405	$0	$0	$0	$0
Alternative Fuel Credit	$0	$0	$0	$1,000	$0	$0	$0	$0	$0	$0	$0
Infrastructure Users Fee Credit	$0	$0	$0	$0	$0	$35,547	$62	$0	$0	$0	$0
Charitable Endowment Contribution Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Historic Building Preservation Credit	$0	$0	$0	$0	$0	$178,162	$0	$0	$0	$0	$0
Increased Research Activity 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	$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	$35,760	$12,041	$8,069	$30,390	$0	$22,313	$42,914	$5,672	$12,132	$4,401	$0
Temporary Emergency Lodging Credit	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Total	**$36,885**	**$214,140**	**$29,982**	**$149,365**	**$18,078**	**$251,584**	**$58,334**	**$9,300**	**$12,612**	**$5,301**	**$0**

Pass-Through Entities by Size - Number of Owners

Pass-through entities vary greatly in size. Approximately 51 percent of Montana's S corporation pass-throughs reported a single owner and 73.6 percent of partnership pass-throughs with Montana source income had two or three owners. Overall, pass-throughs that operate in multiple states tend to have more owners than pass-throughs that only operate in Montana. For S corporations, less than 1 percent of pass-throughs that only operated in Montana in 2012 had more than eight reported owners, while 8.6 percent of multi-state S corporations had at least nine owners. At the same time, 29 percent of Montana's multi-state partnership pass-throughs 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			
	Montana		Multi-State		Montana		Multi-State	
Number of Reported Owners	Number	%	Number	%	Number	%	Number	%
1	12,021	50.8%	2,247	38.4%	109	0.5%	11	0.2%
2 to 3	9,968	42.1%	2,112	36.1%	14,665	73.6%	2,068	44.4%
4 to 8	1,473	6.2%	993	17.0%	3,970	19.9%	1,222	26.2%
9 to 20	190	0.8%	330	5.6%	733	3.7%	505	10.8%
Over 20	28	0.1%	173	3.0%	443	2.2%	853	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 nearly half 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-one S corporations and 553 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	7,814	32.6%	2,346	39.8%	9,156	45.4%	1,876	39.9%
$1 to $10,000	3,843	16.0%	1,957	33.2%	3,231	16.0%	1,188	25.3%
$10,001 to $100,000	9,252	38.6%	1,005	17.0%	5,246	26.0%	766	16.3%
$100,001 to $1,000,000	2,872	12.0%	483	8.2%	1,938	9.6%	425	9.0%
$1,000,001 to $5,000,000	189	0.8%	91	1.5%	284	1.4%	198	4.2%
Over $5,000,000	24	0.1%	17	0.3%	305	1.5%	248	5.3%

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. For S corporation pass-throughs, entities with over $5 million in Montana source income generated approximately $736 million in 2012, which is 34 percent of all the Montana source income generated by Montana's S corporation pass-throughs. Partnership pass-throughs with over $5 million in Montana source income generated $27.2 billion in Montana source income in 2012.

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	-$347	-23.0%	-$80	-12.1%	-$2,108	-13.1%	-$674	-6.5%
$1 to $10,000	$16	1.1%	$5	0.7%	$13	0.1%	$3	0.0%
$10,001 to $100,000	$363	24.1%	$37	5.6%	$204	1.3%	$28	0.3%
$100,001 to $1,000,000	$713	47.2%	$154	23.4%	$543	3.4%	$149	1.4%
$1,000,001 to $5,000,000	$361	23.9%	$207	31.6%	$655	4.1%	$481	4.6%
Over $5,000,000	$402	26.6%	$334	50.9%	$16,829	104.3%	$10,400	100.1%

Overview of Corporate Income Tax

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).**

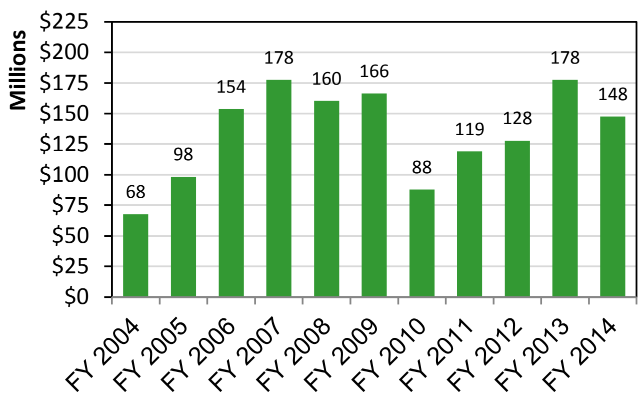
Every bank organized under the laws of Montana or another state or under the United States and every savings and loan organized under state law or United States law is also subject to corporate income tax (15-31-101(4), MCA).

In the 2013 Legislature, SB 361 was passed revising the name of the corporate income tax to 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 2004 through 2014 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 2004 (which started on July 1, 2003) were $67.7 million, increasing to $177.5 million in FY 2007 and declining to $87.9 million in FY 2010. FY 2013 and FY 2014 corporate tax revenues were $177.5 million and $147.5 million, respectively.

Corporate Income Tax

Fiscal Year	Total Revenue
FY 2004	$67,722,940
FY 2005	$98,213,717
FY 2006	$153,675,069
FY 2007	$177,503,707
FY 2008	$160,351,862
FY 2009	$166,357,514
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



Corporate income taxes, other than the fees for applications for film production credits, 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 corporate tax revenues 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 requires 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.

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.

Corporate Income Tax Collections and Refunds - General Fund					
Fiscal Year	Payments With Returns	Estimated Payments	Audits, Penalties, and Interest	Refunds	Total Collections
FY 2008	$39,473,130	$127,433,439	$16,874,522	($23,439,304)	$160,341,787
FY 2009	$45,608,755	$109,585,667	$31,041,454	($19,881,362)	$166,354,514
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
Average	$33,935,385	$112,248,368	$20,696,447	($25,957,814)	$140,922,387

As can be seen from the table, 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 $112.2 million. Average annual revenue for payments with returns over the same period was $33.9 million. The seven-year average of revenues from audits, penalties and interest was $20.7 million. Refunds averaged about $26.0 million per year.

Over the past seven years, total corporate tax collections averaged about $141 million annually. However, there was wide variation in annual collections over that time period.

In 2005 the legislature passed the Big Sky on the Big Screen Act which provides tax credits that can be used to reduce income taxes for certain costs of production of motion pictures, documentaries, television programs, commercials and magazine advertising.

Corporate Income Tax Collections - Film Production Credit Application Fee	
Fiscal Year	Application Fees
FY 2008	$10,075
FY 2009	$3,000
FY 2010	$5,500
FY 2011	$2,000
FY 2012	$3,500
FY 2013	$3,000
FY 2014	$2,500

In order to receive the Big Sky on the Big Screen tax credit, a production company must apply to the department and pay an application fee. The fee is $500 and is deposited in a special revenue account. The revenue in the special revenue account is statutorily appropriated (17-7-502, MCA) - half to the Department of Revenue and half to the Department of Commerce for administration of the provisions associated with the tax credit. The Act terminates on January 1, 2015.

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 flowed through the S corporation to the owner or shareholder. Then the owner/shareholder reports any taxable income on their individual income tax form. S corporations are discussed more in the section on pass-through entities.

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.

Returns Filed for Tax Year 2012	
Regular C Corporations	**16,790**
S Corporations	**29,842**
Total Corporations	**46,632**
C Corporations Paying Minimum Tax*	**11,127**
C Corporations Paying More Than Minimum Tax	**5,663**
Total C Corporations	**16,790**

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

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 non-profit 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.

In order 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 are not subject to the corporate income tax for the first five years of operation. In order to receive this tax treatment the firm must apply to the Department of Revenue and be approved as meeting legislative requirements (15-31-103, MCA).

Distribution of Corporate income Taxes

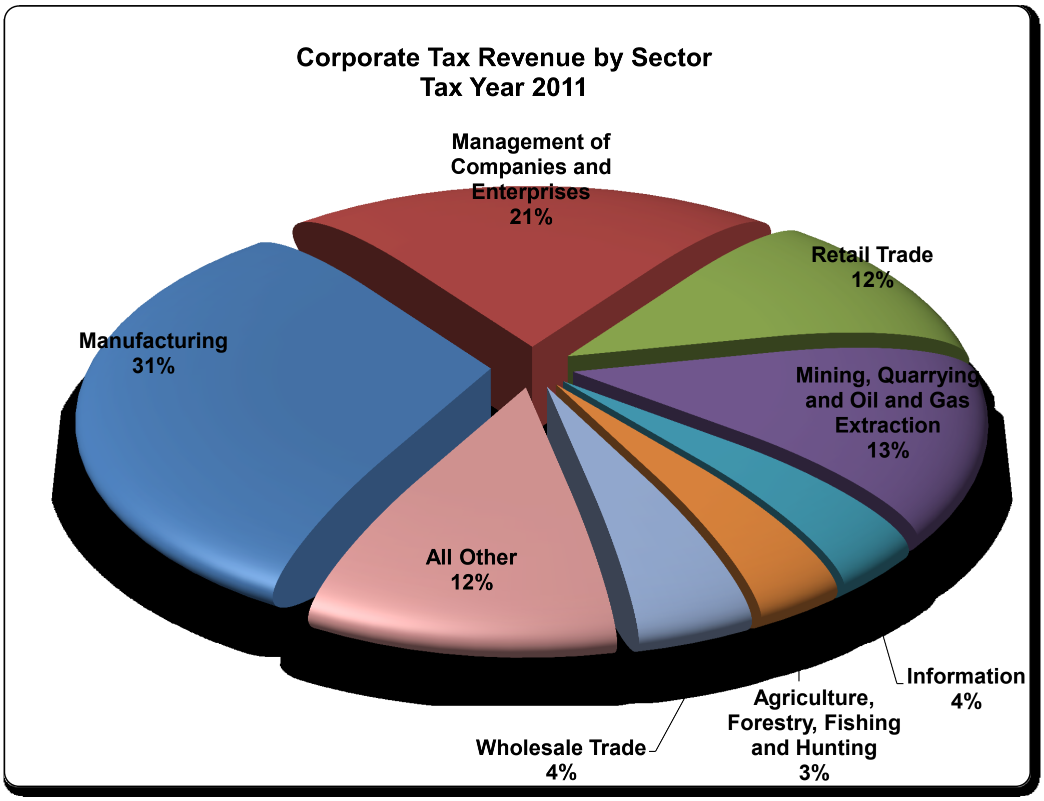
The following table shows the distribution by Montana tax liability of the 16,790 corporate returns with a Montana tax liability filed in calendar years 2013 and 2014 reporting on tax year 2012. Please note that the revenues from the return data will not match the fiscal year revenues in earlier tables because fiscal year revenue is based upon payments, including estimated payments and payments with returns, recorded in the state accounting system.

Corporate Returns Filed in CY 2013 - CY 2014 for Tax Year 2012
Distribution of Montana Tax Liability

Regular Corporation Returns	Number	Tax Liability	Percent of Total Liability	Cumulative Percent of Total Liability
Top 100 returns	100	$101,427,528	69%	69%
Second 100 returns	100	$13,788,101	9%	78%
Third 100 returns	100	$7,321,895	5%	83%
Fourth 100 returns	100	$4,482,351	3%	86%
Fifth 100 returns	100	$3,222,303	2%	88%
All other returns	16,290	$17,326,906	12%	100%
Total	16,790	$147,569,084	100%	n/a

Altogether the top 100 returns constituted about 69% of total tax liability for the entire group of taxpayers. The top 500 returns accounted for 88% of total Montana tax liability for the group. The other 16,290 returns accounted for only 12% of the total Montana tax liability.

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 shows the distribution of corporate income taxes for the largest sectors.



The largest sector in terms of tax year 2011 tax liability was manufacturing, with 31% of all the corporate income taxes. The Census Bureau list of manufacturing activities includes food manufacturing, including grain, oilseed, fruit and dairy processing; bakeries; beverages; sawmills, millwork and paper manufacturing; petroleum and chemical manufacturing; cement and concrete; and other activities.

Corporations involved in the management of companies and enterprises that include bank and other holding companies and corporate or regional headquarters paid about 21% of all corporate income taxes in tax year 2011. Corporations primarily involved in mining, quarrying and oil and gas extraction, paid 13% of TY 2011 corporate income taxes, followed by retail trade (12%), all other (12%), information (4%), wholesale trade (4%) and agriculture, forestry, fishing and hunting (3%).

When looking at the graph above 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 corporation 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% 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% 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).

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**

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 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 15-31-323, 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 2012 earlier in this section shows that for those returns filed in tax year 2012 by corporations, the minimum tax was paid on 11,127 returns or almost 66 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 to 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 year's 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 carryforward					
		5 years forward	7 years forward	10 years forward	12 years forward	15 years forward	20 years forward
Allowed years of carryback	0 years back	Arizona Arkansas New Mexico Rhode Island		Kansas Michigan New Hampshire 6/ Vermont	Illinois 4/	Alabama Minnesota North Carolina Oregon Tennessee Wisconsin	Colorado Connecticut District of Columbia Florida Iowa Kentucky Maine 5/ Massachusetts Nebraska New Jersey North Dakota Ohio Pennsylvania 8/ South Carolina
	2 years back						Alaska California 1/ Delaware 2/ Georgia Hawaii Idaho 3/ Indiana Maryland Mississippi Missouri New York 7/ Oklahoma Virginia West Virginia 10/
	3 years back		Montana			Louisiana Utah 9/	

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 has suspended use of NOLs for tax years beginning in 2011-2014.
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 limits carrybacks to the first $10,000 of losses.
8/ Pennsylvania limits NOL deductions to the larger of $3 million or 20% of Pennsylvania taxable income.
9/ Utah has a $1 million limit on carrybacks.
10/ West Virginia limits carrybacks to $300,000.

Source: *2014 State Tax Handbook* , CCH, 2013.

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.

Montana Corporate Income Tax Credits

	--- Tax Year 2011 ---		--- Tax Year 2012 ---	
Credit	Number of Credits	Total Credit Amounts	Number of Credits	Total Credit Amounts
Non-Refundable Credits				
Contractors Gross Receipts Tax Credit	110	$531,807	104	$763,534
Charitable Endowment Credit	15	$45,913	20	$60,406
Montana Recycling Credit	*	$112,359	*	$79,815
Credit for Increasing Research Activities	18	$365,643	14	$47,394
Credit for Contribution to MT University or Private College	24	$5,874	28	$9,020
Empowerment Zone Credit	-	-	-	-
Health Insurance for Uninsured Montanans Credit	28	$29,619	19	$15,220
Credit for Alternative Fuel Motor Vehicle Conversion	*	$6,479	-	-
Alternative Energy Production Credit	*	$50	*	$50
Dependent Care Assistance Credit	-	-	-	-
New/Expanded Industry Credit	-	-	-	-
Historical Building Credit	-	-	-	-
Infrastructure Users Fee Credit	*	$45,913	*	$305,304
Mineral Exploration Incentive Credit	*	$2,767	*	$25
Film Employment Credit - Non-Refundable	*	-	-	-
Biodiesel Blending and Storage Credit	-	-	-	-
Oilseed Crushing and Biodiesel Production Credit	-	-	-	-
Geothermal System Credit	-	-	-	-
Refundable Credits				
Temporary Emergency Lodging Credit	-	-	-	-
Film Employment Credit - Refundable	*	$12,693	*	$33,862
Film Production Credit	*	$25,865	*	$49,491
Insure Montana Credit	167	$753,856	156	$667,413
Total Credits	**375**	**$1,938,838**	**353**	**$2,031,534**

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. Also if the taxpayer's tax liability is less than the credit amount and the credit is not refundable, the actual reduction of tax liability due to the credit is limited to the tax liability. In addition, some of the above numbers may represent a carryback of some credits claimed on amended returns.

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 in this section 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.

Filing Requirements and Estimated Payments

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).

Corporate Income Tax Tax Year 2011		
Tax Year Period Ending:	Number of Taxpayers	Percent
12/31/2011	10,854	67%
1/31/2012	333	2%
2/29/2012	244	2%
3/31/2012	824	5%
4/30/2012	231	1%
5/31/2012	218	1%
6/30/2012	912	6%
7/31/2012	164	1%
8/31/2012	202	1%
9/30/2012	847	5%
10/31/2012	877	5%
11/30/2012	498	3%
Total	16,204	100%

As can be seen in the table in this section, about two-thirds of corporate taxpayers (67 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 6% 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 utilize the automatic extension moving the due date of their return from May 15th to November 15th. So the TY 2011 return for a taxpayer whose fiscal year is calendar year 2011 would be due May 15th, 2012, but the taxpayer would have until November 15th to file under the automatic extension.

A taxpayer whose fiscal year/tax year ends June 30th has 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 2011 return for a taxpayer whose fiscal year starts July 1st (in 2011) and goes through June 30th (of 2012) is due November 15th, 2012 but the taxpayer would have until May 15th, 2013 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 who do not pay taxes when due may be assessed a late payment penalty of 1.2% per month on the unpaid tax, up to a maximum penalty of 12% of the tax due. Interest on unpaid tax accrues at a rate of 12% per year, or at 1% per month or fraction of a month on the unpaid tax.

Maximum Corporate Tax Rate By State From Highest to Lowest

Rank	State	Maximum Tax Rate
1	Iowa *	12.00%
2	Pennsylvania	9.99%
3	District of Columbia	9.975%
4	Minnesota	9.80%
5	Illinois	9.50%
6	Alaska *	9.40%
7	New Jersey	9.00%
7	Rhode Island	9.00%
8	Maine *	8.93%
9	California	8.84%
10	Delaware	8.70%
11	New Hampshire	8.50%
11	Vermont *	8.50%
12	Maryland	8.25%
13	Louisiana *	8.00%
13	Massachusetts	8.00%
14	Wisconsin	7.90%
15	Nebraska *	7.81%
16	Oregon	7.60%
17	Connecticut	7.50%
17	Indiana	7.50%
18	Idaho	7.40%
19	New Mexico*	7.30%
20	New York	7.10%
21	**Montana**	**6.75%**
22	West Virginia	6.50%
22	Arizona	6.50%
22	Alabama	6.50%
22	Arkansas *	6.50%
22	Tennessee	6.50%
23	Hawaii *	6.40%
24	Missouri	6.25%
25	Kentucky *	6.00%
25	North Carolina	6.00%
25	Georgia	6.00%
25	Michigan	6.00%
25	Oklahoma	6.00%
25	Virginia	6.00%
26	Florida	5.50%
27	Mississippi *	5.00%
27	South Carolina	5.00%
27	Utah	5.00%
28	Colorado	4.63%
29	North Dakota*	4.53%
30	Kansas	4.00%

As of Jan. 1, 2014, 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, 2014) to show the maximum rates for states that have a corporate tax. These go from 12% down to 4%. A number of states have a graduated income tax which is indicated by an asterisk next to the state.

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%, which is in the lower half of top rates for states that have an income tax.

Idaho's tax rate is 7.4% and North Dakota's top corporate income tax rate is 4.53%.

South Dakota does not have a general corporation income tax, but does have an excise tax on financial institutions which starts at 6% 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% and there was no minimum tax.

In 1933 the rate was raised to 2% with a minimum tax of $5.00. In 1937 the rate was raised to 3%; the minimum tax remained $5.00. Twenty years later in 1957, the rate was raised to 5% and the minimum tax changed to $10.00. 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% for corporations who 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%	--	--