Timber in Transition: Legislation Aims to Close Tax Loopholes

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Trout Creek resident Jim Elliott lives in Plum Creek territory and enjoys the returns on personal investments he's made in the timber company. But he's also a state legislator in charge of a powerful committee - the Senate Taxation Committee - looking for tax loopholes to close. He and others think he's found one. Elliott is sponsoring Senate Bill 120, a bill inspired by Plum Creek but that also affects other real estate investment trusts operating in Montana. When a fire breaks out on Plum Creek property, the company gets help from local and state fire departments, Elliott said. Plum Creek uses Montana roads and services, including its courts, licensing bureaus and environmental agencies. Yet the company, because of unique deductions that real estate investment trusts - or REITs - enjoy under federal law, pays virtually no taxes on income earned in Montana. And that's the loophole Elliott wants to close. “I just don't think they are paying their fair share,” said Elliott, a Democrat who serves Senate District 7, which includes Mineral and Sanders counties, and the Frenchtown, Ninemile, Huson and Wye areas of Missoula County. “Real estate investment trusts get deductions that nobody else gets.” “Companies operate in the state of Montana with the permission of the state,” he said. “Along with that goes the responsibility to pay your own way.”

Here's the simplified version of how the bill would work: SB120 would require REITs to pay taxes on income earned in Montana. Congress set up REITs in 1960, specifically to give small investors a chance to invest in commercial real-estate markets. REITs own property that generates rent or payment from leases. By federal law, REITs are required to pass on at least 90 percent of their income - essentially the rent and lease payments - to their shareholders. Shareholders receive the dividends and pay taxes on those dividends in their home states. Problem is, Elliott said, most REIT shareholders don't live in Montana. That means whatever money the companies make in the state transfers out across the country, benefiting other states' tax coffers. Companies that aren't owned by REITs don't get that benefit, which gives REITs unfair advantage, according to Elliott's view.

Local owners of Missoula's Southgate Mall, for instance, pay state taxes on their corporate income, while the profits of Billings' Rimrock Mall, owned by a REIT, go to shareholders across the country. Tax the Montana profit in Montana, and let Montana benefit from it, Elliott argues. His proposed bill attempts to deal with concern over double taxation by exempting dividends paid to Montana taxpayers by REITs operating in Montana. That's a simplistic explanation of a complex, many-layered tax bill. It was proposed last session as part of a much larger bill and probably died because it was too complex, Elliott said. Now, Montanans ears perk up when Plum Creek is mentioned, he said. Had SB120 been in effect in 2004, the state would have received an additional $3.3 million in income tax revenues, according to one analysis of the legislative proposal. If approved, SB120 could bring in nearly $33 million to the state's general coffers in the next four years, based on the 21 percent income growth REITs enjoyed in Montana from 2002-04, again according to estimates from the state. There are, however, naysayers. The revenue estimates are overly optimistic and Montana will actually suffer if SB120 passes, predicted Tony

Edwards, executive vice president and general counsel for the National Association of Real Estate Investment Trusts, based in Washington, D.C. First, it would make Montana a lone ranger. “Four or five other states have looked at this issue and decided it doesn't make sense,” he said. “After learning about it, they've always dropped it.”

From a practical standpoint, REITs don't know where investors file their tax returns, so they can't tease out just the Montana investors and Montana profits for special tax treatment. But more importantly, it would make Montana “very noncompetitive,” he said. REITs would simply sell or stop improving their Montana properties, and invest elsewhere. Plum Creek is not the only REIT in the state: NAREIT lists 12 others, including the Macerich Co., which owns the Billings mall, and the Apartment Investment and Management Co. (AIMCo.), whose Web site lists two apartment complexes in Butte. These companies hire local people, pay local real-estate taxes, buy local goods and have subsidiary companies that pay millions of dollars in Montana taxes, according to NAREIT. Philosophically, SB120 gets away from the original congressional intent behind REITs, Edwards said. REIT profits are supposed to go to individual investors, not to governments. Elliott is unfazed. Surely, the paperwork questions can be fixed, he said. And he dubs the anti-business argument bogus. REITs shift the tax burden to other businesses and taxpayers, who must cover the cost of government. “Essentially, my question is: Why are these folks given an exemption that no other company in the state gets? The answer is: I don't know.” Elliott is carrying the bill. But he's not the only well-placed person backing it. SB120 came from the state Department of Revenue and its chief, Dan Bucks. And Gov. Brian Schweitzer is behind it, too. It's a fairness issue, the governor said. “The bottom line is that there are a whole lot of individuals and companies that are getting a competitive advantage in Montana because they don't pay Montana taxes,” he said. “It gives a competitive advantage to out-of-staters.” “It's pretty common sense here,” Schweitzer said. “Here are some folks by Montana law who ought to be paying taxes. We've identified the gate that they are getting out of. We just want to close that gate.”

Two more bills could affect Plum Creek Two other bills awaiting action by the 2007 Montana Legislature could affect Plum Creek Timber Co. lands. They are: Protecting land: Sen. Carol Williams, D-Missoula, plans to introduce a bill in the next few weeks to create a “Montana Working Forests, Ranches, Farms and Watershed Program.” The legislation would create a state commission appointed by the governor to establish criteria for purchasing land, conservation easements and public access on land important to Montana's public, culture, history, wildlife, water or beauty. “The idea is to get private, public, tribal and federal money into the fund so that when projects come open and there is land available, we are ready,” Williams said. The potential of Plum Creek developing big chunks of its 1.3 million acres in Montana sparked the bill, but it has wider appeal, she said. “It could work in Scobey if there is a farm or ranch along a river that has important habitat issues or access issues,” she said. “It would be of value to the whole state, not just around the Seeley Lake and Swan Valley where Plum Creek has so much land.” How to fund the program isn't clear yet, and the House will handle the money angle, Williams said. The Montana Department of Natural Resources and Conservation would administer the program, and commission members would represent conservation, timber, fish and wildlife, agriculture and public interests. “We don't have a lot of time to make decisions about a lot of this property out there,” she said. “This is really a gift to future generations.” Paying for fire: Sen. Bob Hawks, D-Bozeman, has introduced Senate Bill 167 at the request of the DNRC. It's a legislative club to get counties to set development standards for the wildlandurban interface - areas where subdivisions and homes are sprouting up next to undeveloped wildlands, forests and remote areas. With human development comes more human-caused wildfires and different firefighting priorities that emphasize saving people and structures instead of trees - the former much more expensive than the latter, according to the DNRC. The state ends up footing the bill. The DNRC spent about $30 million in the past five wildfire seasons fighting fires for Montana's 56 counties, according to a state analysis. If counties choose not to designate interface zones and set standards and zoning for them, they'd have to reimburse the DNRC for fire suppression in those areas - a huge financial burden for counties. SB167 would prod counties to get moving on planning and zoning efforts and setting standards for buildings and subdivisions in these wildland areas, thereby forcing zoning on thousands of acres owned by the state's largest owner of private land, Plum Creek Timber Co.