

Our Best Advice to Taxpayers

The department offers the following advice to taxpayers who want to have the best experience possible during tax season.

File early

Taxpayers who are expecting a refund will receive that refund faster if they file early in the tax season. The earlier taxpayers file, the better service the department can provide in getting tax returns processed and refunds issued quickly.

For example, the average number of weeks to process a paper return with a refund request is approximately 1½ weeks on February 1; 3 weeks at March 1; and 4 - 6 weeks at April 15.

Taxpayers who have taxes due are also encouraged to file early, but to pay later. Using direct debit, taxpayers can wait to pay any balance due until closer to the tax deadline. Taxpayers simply authorize the department to withdraw the amount of tax due from a checking or savings account on a date that the taxpayer chooses.

File electronically

Electronic filing is a quick and accurate way to file a state income tax return. Taxpayers who file their federal income tax return electronically can file their state income tax return at the same time. The refund will be issued quickly, usually within a week.

Last tax season, approximately 52% of Montana taxpayers filed electronically, while 48% filed on a paper return.

Choose direct deposit if you are expecting a refund

Taxpayers can reduce the wait for a refund through direct electronic deposit into a bank account. Taxpayers simply check the box indicating they want direct deposit, then provide information about their financial institution and account (routing number, account number, whether the account is checking or savings).

Last tax season, more than half (54%) of Montana taxpayers who filed electronically also used direct deposit.

Improved Forms, Instructions and Website

Tax-saving opportunities are clearly shown

The department has expanded its forms and instructions to reflect all features of Montana law, especially those that allow taxpayers to legally reduce their tax obligation. In essence, this provides a “checklist” for taxpayers to ensure that they are aware of all possible tax-saving opportunities. This also serves the right of the public to know the laws that affect them.

- In all, this year’s tax booklet details 36 more ways to reduce taxes than last year’s booklet did.
- The “catch-all” lines labeled as “Other” no longer bundle together multiple, diverse provisions of law. Instead, there are now numerous lines that clearly describe the possibilities that exist

in these categories. This change applies to reductions-to-income, tax credits, and additions-to-income. The "Other" lines that remain are available only for rare, exceptional cases.

- In the 2004 tax year, the tax return listed 9 specific reductions to income (2004 Form 2, lines 26 through 34). In 2005, there are 34 reductions to income listed (2005 Form 2A, Schedule II). Note: One reduction to income is new (2005 Form 2A, Schedule II, line 10); the remaining 24 reductions to income are not new, but were bundled on one line labeled "Other Reductions" (2004 Form 2, line 35).
- In the 2004 tax year, the tax return listed 16 specific tax credits. In 2005, there are 27 tax credits listed (2005 Form 2A, Schedule V and Form 2, line 47). Note: Five credits are new; the remaining 6 credits are not new, but were bundled on one line labeled "Other Credits" (2004 Form 2A, Schedule II, line 111).
- In the 2004 tax year, the tax return listed 2 specific additions to income (2004 Form 2, lines 21 and 22). In 2005, there are 19 additions to income listed (2005 Form 2A, Schedule I). Note: The additional 17 additions to income are not new; they were bundled on one line - labeled "Other Additions" (2004 Form 2, line 23).

Tax credits are listed in an order that gives taxpayers the maximum benefit

The tax credits have been grouped and arranged in a manner that provides taxpayers with maximum tax benefit. If taxpayers apply tax credits in this order, they will maximize tax savings.

- Non-refundable tax credits with no carryover provision are listed first. Non-refundable tax credits with a carryover provision are listed next. Refundable tax credits are listed last.

State tax forms now reflect federal forms, ending a source of confusion

The department has worked to reduce taxpayer confusion by making all federal items on the state tax form "mirror" the federal Form 1040.

Forms and instructions are more citizen-oriented

The department has significantly revised its tax forms and instructions. These materials now have a design and writing style that reflects the perspective of the taxpayer, rather than the department.

The improved design includes larger sized type and more white space. The pages appear more readable and less intimidating to the taxpayer.

The department has improved the writing in several ways. Foremost, the department revised the new forms and instructions so that taxpayers know the laws and rules that affect them. The forms and instructions now fully disclose all provisions of the law to taxpayers. The provisions are no longer hidden in catch-all "Other" lines and cryptic, fine print instructions. This approach will also yield data for lawmakers and the public on the impact of each provision of the law.

The following are other goals that guided the department as the forms and instructions were rewritten.

- **Understandable:** To help taxpayers understand our forms and letters; to give precise and clear directions on how to file; to avoid legal jargon, terms of art, and unnecessary abbreviations and acronyms; to label sections clearly and consistently; to mark clearly the

sequential steps the taxpayer should follow; to use complete sentences, rather than cryptic or telegraphic ones; to communicate in grammatically accurate sentences

- **Informative and Helpful:** To take the taxpayers' perspective, to walk in their shoes; to anticipate in advance any confusion that the taxpayer may experience; to present information and give helpful advice--rather than giving harsh directives and warnings; to tell taxpayers precisely and clearly what errors they may have made
- **Positive:** To state things positively, rather than negatively; to be polite in the effort to obtain taxpayer compliance; to sympathetically explain any bad news the department has to give; to give clear reasons for the actions the department has to take.

The new writing style resulted in the 2005 income tax booklet containing significantly more pages than in past years. While the 2004 booklet was 32 pages, the 2005 booklet is 60 pages. The bulk of the increase in pages results from an expansion of the instructions, from 11 pages in 2004 to 35 pages in 2005.

Other highlights of the forms and instructions

- A new section called Your Tax Dollars at Work was added to the tax booklet. The page shows a chart of the sources of revenue for both state and local governments in Montana for 2002, the most recent year for which totals are compiled. A second chart shows state and local spending. A table shows where income tax dollars—about 11% of total state and local revenues—were spent in 2005.
- Due to the larger number of pages in the 2005 income tax booklet, the department was unable to provide duplicate copies of forms, as was done in the past. Taxpayers are encouraged to visit the department's website to download extra copies of any needed forms. Fill-in forms are particularly handy for taxpayers for this purpose.
- Taxpayers are encouraged to use the pre-addressed, postage-paid survey card enclosed in the tax booklet to provide comments to the department.

Revamped website for income tax filing season

The department has revamped its website to gather all key individual income tax information into one place—with one-click access to all key services and forms that taxpayers need.

Montana Law Changes for Tax Year 2005

Changes from 2003 Legislative Session (Senate Bill 407)

The 2003 Legislature made several changes to Montana's income tax laws.

- **Tax Rates:**
The ten tax brackets ranging from 2% to 11% that were used in the past have been replaced with seven brackets ranging from 1% to 6.9%.
- **Capital Gains Tax Credit:**
Taxpayers reporting net capital gains in their Montana adjusted gross income are entitled to a 1% capital gains tax credit.

- **Federal Income Tax Deduction Limitation:**
For taxpayers who itemize instead of taking the standard deduction, the federal income tax deduction is now limited. Federal income tax deduction is limited to \$5,000 per taxpayer (using the filing status of single, married filing separately or head of household) and to \$10,000 if filing jointly with a spouse.

Note: With the changes in the law in 2005, taxpayers should review their filing methods. Married couples can choose whether to file separately or jointly, and all taxpayers can choose whether to itemize deductions or take the standard deduction. Some taxpayers will pay less tax if they make different choices than they made last year. Taxpayers should try both ways on each choice instead of automatically doing what they did last year.

For Military Personnel

- **Extensions available for active duty service members:**
Montana follows the Service members Civil Relief Act passed by Congress in 2003 and also follows IRC 7508, which provides a service member, and his or her spouse, who is serving in a combat zone, participating in a contingency operation, or has qualified hospitalization time, the opportunity to extend the due date of his or her return up to 180 days after being discharged from service. Although the individual income tax booklet references National Guard members, any full-time military personnel serving in a combat zone will qualify.
- **Life insurance premium reimbursement:**
A member of the Montana National Guard or Reserve who is reimbursed by the Montana Department of Military Affairs for premiums that were paid under the service members' group life insurance program can exempt these reimbursements when determining Montana adjusted gross income.

New Tax Credits Available

Biodiesel Fuel Credits

- **Oil Seed Crushing and Biodiesel Production Facility Credit:**
If a taxpayer invests in qualifying depreciable property that is used to crush oilseed crops that are used in the production of biodiesel fuel, they can qualify for a tax credit equal to 15% of the cost of the investment up to \$500,000. In addition, if a taxpayer invests in qualifying depreciable property that is used to construct and equip a facility to produce biodiesel fuel, the taxpayer can qualify for a tax credit equal to 15% of the cost of the investment up to \$500,000.
- **Biodiesel Blending and Storage Tank Credit:**
If a taxpayer is a special fuel distributor, a tax credit can be claimed equal to 15% of the cost of installing depreciable storage and blending equipment, for a maximum credit of \$52,500. If the taxpayer is an owner of a motor fuel outlet that has installed depreciable storage and blending equipment that is used to blend bio-diesel with petroleum diesel, you are entitled to a tax credit equal to 15% of the cost of installing such equipment up to \$7,500.

Film Production Credits

- **Employment Production Tax Credit:**
An owner of a film production company that produced a state-certified production is entitled to an employment production tax credit equal to 12% of the first \$50,000 of compensation that was paid to Montana employees.
- **Qualified Expenditures Tax Credit:**
An owner of a film production company that produced a state-certified production can qualify for a qualified expenditures tax credit equal to 8% of the qualified expenditures that were incurred in the state-certified production.

Changes to Credits Available in Previous Year

- **Energy Conservation Installation Credit:**
Residents of Montana can claim a credit for energy conservation investments that were made to their home or other buildings. The credit is equal to 25% of the expenses for a maximum credit of \$500. The department has revised its interpretation of this statute whereas each person owning the property may claim \$500 provided that sufficient expenses were incurred. So, a couple owning a house may claim \$500 each, or \$1,000 in total.
- **Contractor's Gross Receipts Tax Credit:**
Beginning in 2005, the contractor's gross receipts tax credit in excess of the taxpayer's liability can now be carried forward up to five subsequent years.

Late Pay Penalty and Interest

- **Interest:**
Effective July 1, 2005, interest accrues daily on any unpaid tax, at an annual rate of 12%, from the original due date of the return. Interest accruing prior to July 1, 2005 remains at 1% per calendar month or fraction of a calendar month.
- **Late Pay Penalty:**
If the full amount of the tax liability is not paid on or before April 17, 2006, a late pay penalty will be charged. Please note that an extension to file is not considered an extension to pay. Even if sufficient payments were made by April 17, 2006 to perfect an extension to file, the taxpayer is not allowed an extension to pay. The penalty remains at 1.5% a month or fraction of a calendar month, not to exceed 18%.

Federal Law Changes for Tax Year 2005

Temporary Expansion of Charitable Contribution Deductions Triggered by Hurricane Katrina

Montana follows federal provisions for the expanded deduction of contributions made between August 27 and December 31, 2005. However, Montana law does not allow the additional \$500 federal exemption for housing a person displaced by Hurricane Katrina.

Domestic Production Activities Deduction

Because Montana's deductions that are allowed in computing net income begin with the federal deductions allowed under 26 U.S.C. 161, the federal domestic production activities deduction now effective for federal purposes is allowed as a deduction for Montana purposes.

Changes to Extension

There is no longer a four-month or an additional two-month extension requirement for federal income tax purposes or, accordingly, for state purposes. The Internal Revenue Service replaced the four and two month extension with a six month extension. Upon applying for a federal extension, using federal Form 4868, taxpayers are granted an automatic six-month extension for Montana purposes.

Please note "extensions available to activity duty service members" set forth in Montana Tax Law Changes (above).

Electronic Filing

Electronic filing for individual income tax has made gigantic strides.

Tax Year	E-File Returns	Online Returns	Telefile Returns	Total E>Returns
1994	1,689			1,689
1995	11,503			11,503
1996	16,907		13,131	30,038
1997	26,258		19,724	45,982
1998	37,126	476	21,892	59,494
1999	49,703	6,889	20,663	77,255
2000	78,515	10,833	19,697	109,045
2001	104,034	17,882	18,109	140,034
2002	126,166	25,097	16,698	168,231
2003	152,210	28,204	15,474	195,888
2004	174,979	35,811	13,863	224,653

How Taxpayers Can E-file

There are three ways to e-file, including using an authorized e-file provider, using tax software to prepare your taxes or filing using the Internet.

- Utilize an authorized E-file tax professional. This involves a cost to the taxpayer.
- Use an off-the-shelf software program installed on a personal computer with Internet access. This involves a cost to the taxpayer.
- Use online software on a personal computer with Internet access. This can be done by downloading the software to a personal computer or by filing the tax return on a software vendor's website. Both options involve a cost to the taxpayer. However, some taxpayers may qualify to prepare and submit their taxes online for free, through services such as:

- MontanaFreeFile.org, a service provided by Consumer Credit Counseling Service of Montana's Tax Help Montana Project, Montana Legal Services Association, and Montana's Credit Unions. The service is supported by Governor Brian Schweitzer.
- Montana Free File Alliance, an alliance between the department and software companies to offer free on-line filing services to qualified Montana taxpayers. You can find information on the department's website at www.mt.gov/revenue.

Why Taxpayers Should E-file

There's really no good excuse not to E-file. It's accurate, secure and speedy. Taxpayers who file electronically can expect these benefits:

- Federal/state e-filing: Taxpayers can e-file their federal and state tax returns in one transmission to the IRS. The IRS forwards the state data to the Montana Department of Revenue.
- More accurate returns: Tax software does the math and checks for errors or other missing information, making e-filed returns more accurate and reducing the chance of getting an error letter.
- Quick electronic confirmation: Acknowledgements are created for both the federal and state when the return is received. This is a positive confirmation that your return was received.
- Convenient: Online filing can be completed at any time of the day. When the taxpayer selects direct deposit of the refund, the refund goes directly into the bank account – a safer, more convenient transaction.
- Speedy: Once the income tax calculations have been completed, E-filing the tax return takes about 10 minutes.
- Faster refunds: Direct Deposit can speed refunds to e-filers in as few as 4 days. The average e-file refund is issued in 7 days.

Telefile

The department has eliminated the state Telefile (phone-based) program, for the following reasons.

- Telefile serves a very small population of taxpayers. Last year, only about 2.2% of Montana taxpayers used Telefile. At its peak (tax year 1998), Telefile was used by only 3.6% of Montana taxpayers. In addition, the number of Telefile users has decreased over the years.
- The IRS discontinued its federal Telefile for tax year 2005. The department believes this will cause a further decline in the number of Montana Telefile users.
- Last year, Montana secured a new vendor (NextiraOne) for the interactive voice response portion of its telephone network. This vendor change would have required the department to

pay \$80,000 to re-program the Telefile database into the new telephone system for tax year 2005. This would have been an expense to fund a declining filing option.

Convenient Options for Former Telefile Users

Taxpayers who used Telefile in the past are encouraged to do one of the following:

- file electronically
- use the “self-calculating” Form 2S (short form) on the department’s website, or file a paper return.

Electronic Payment Options

There are two options for paying taxes electronically. With both options, taxpayers can file early and wait to pay any balance due until closer to the tax deadline.

Income Tax Express

Taxpayers may pay state taxes online using an application called Income Tax Express. Taxpayers can pay using a credit card (MasterCard, VISA) or an eCheck. Income Tax Express can be used to pay current and past year state individual income taxes, and estimated taxes. Fees are charged for this service.

Direct Debit

Using direct debit, a taxpayers who files electronically can authorize the department to withdraw the amount of tax due from a checking or savings account on a date that the taxpayer chooses.

Tax Assistance

Call Center

8 a.m. – 5 p.m., Monday – Friday
(406) 444-6900

Note: Lowest volume of calls is typically received in the midmorning (9 – 11 a.m.), so this is a good time for taxpayers to call with minimal wait. Highest volume of calls is typically received in the early afternoon (1:30 – 3:30 p.m.), and the wait for taxpayers may be several minutes during this period.

Website

www.mt.gov/revenue

The website contains a variety of filing information, and includes an e-mail function that allows taxpayers to send a message to the department. To access the e-mail function, click on Contact Us.

Note: Taxpayers who do not have Internet access at home, but want to file electronically, may want to visit their local library for free Internet use. An Internet e-mail account is required for acknowledgement of receipt of the tax return.

Walk-in Assistance

Sam W. Mitchell Building
125 North Roberts Street
Helena, Montana

Note: Taxpayer assistance is available year-round. A special taxpayer assistance room is open on the first floor of the building from March 1 – April 15.

Other Telephone Numbers

Where's My Refund - (406) 444-9840

Telephone Device for the Deaf (TDD) - (406) 444-2830

E-file Administration

Information for Practitioners, Transmitters, Developers

David Berg, Electronic Tax Program Coordinator

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Filing It Right

- **Calculation of Penalty and Interest:**
In order to ensure that penalties were not attached to any contributions to the Montana check-offs, the calculation of the penalties and interest has been re-arranged. Please refer to the instructions included in the booklet.
- **Amended Return:**
The Form 2X is no longer available on which to file an amended return. If amending your 2005 tax return, the box by "amended return" on the front of the return should be marked and the Amended Return Reconciliation on Form 2A or on the back of the Form 2S should be completed.
- **Tax Rates:**
As noted above, the tax rates have changed for tax year 2005. Due to space limitations, the rates are no longer included on the bottom of Form 2. Please refer to the rates included on page 1 and again on page 9 of the instruction booklet.

For Senior Citizens

- **Elderly Homeowner/Renter Credit:**
Montana taxpayers are eligible for the Elderly Homeowner/Renter Credit at age 62. The Elderly Homeowner/Renter credit is no longer separately identified on Form 2, Page 2. It is now included on Form 2A, Schedule V (Montana Tax Credits), line 27 as it is no longer the only refundable credit available.
- **Interest Exclusion for the Elderly:**
Remember, if you are age 65 or older you may subtract up to \$800 of interest income from your federal adjusted gross income. You can find this subtraction on Form 2A, Schedule II, line 12 "Partial interest exemption for taxpayers 65 and older."
- **Pension Income Exclusion:**
Remember, if you have taxable pension income you may be eligible to subtract up to \$3,600 of your pension income from your federal adjusted gross income. You can find this subtraction

on Form 2A, Schedule II, line 11 and on Form W, Worksheet IV, page 39 of the instruction booklet.

- **Medical Insurance Premiums:**
If you are receiving social security and if you have Medicare premiums deducted from your benefits, these premiums are described as "Medicare premium payments made in 2005" in the description box on Federal Form SSA-1042S. These premium payments, known as Medicare B, are 100 % deductible as an itemized deduction on Form 2A, Schedule III, line 4. The basic monthly premium in 2005 was \$78.20.

Errors Found in Tax Materials

To date, the Department of Revenue has identified two errors in our income tax booklet that may impact taxpayers. The downloadable income tax booklet and associated forms on the department's Internet site have been corrected. In addition, the software providers have been notified of the correction to Schedule VII as noted below. Here is a brief description of each error:

- **Form 2EC instructions:**
The first paragraph of the instructions for the Montana Homeowner/Renter Credit (Form 2EC) inadvertently refers to the age 65 instead of 62. Taxpayers are eligible for this credit if they are 62 or older. It is correct on the actual form and when referenced later in the instructions. We are also notifying impacted groups such as AARP and the Montana Society of CPA's.
- **Schedule VII:**
Credit for an Income Tax Liability Paid to Another State or Country. Part-year resident only:
On lines 1 and 3, it should refer to line 16 of Schedule IV instead of line 17. Both lines 1 and 3 correctly refer to "Montana" source income but inadvertently reference the wrong line number that must be transferred from Schedule IV. As noted above, the software providers have been notified of this error. There are approximately 19,000 part year resident filers each year and consideration will be given to any taxpayer that completes this schedule in error.