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OMB/RECORDS MANAGEMENT DIVISION
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ROLL NUMBER

DESCRIPTION

2311

2007 SENATE FINANCE AND TAXATION

SB 2311

2007 SENATE STANDING COMMITTEE MINUTES

Bill/Resolution No. **SB 2311**

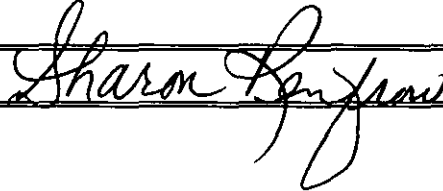
Senate Finance and Taxation Committee

Check here for Conference Committee

Hearing Date: January 23, 2007

Recorder Job Number: # 1686

Committee Clerk Signature



Minutes:

Sen. Urlacher called the committee to order and opened the hearing on SB 2311.

Sen. Krauter: prime sponsor of the bill appeared with written testimony and proposed amendments. (See attached)

Sen. Cook: is there any sales tax collected during the renting or leasing of farm machinery?

Answer: currently there is sales tax collected if the machinery has met one of these 3 exemptions, so if the piece is 3 yrs or younger, you will pay that 3% sales tax on that lease or that rent price that you pay.

Terry Steckler: resident of Bismarck and am in the business of renting farm equipment, primarily combines to growers all across the country and operate in about 33 states. Rental equipment is more of an option used around here because machinery is very expensive. I want to make a clear distinction between a true rental, a finance lease and traditional financing. When a farmer goes to buy a machine, he has a choice of taking traditional financing through the dealer, the local banker or taking a finance lease option. On a financed lease there is almost always the opportunity to own that machine at the end of that financed lease. It's just another way of financing a machine, there is some tax benefits to a financed lease. In almost all cases, they must take ownership of that machine. In a true rental

situation, the grower is never given the option of owning that particular piece of equipment, its simple a rental payment, they pay for the hours they put on the machine, they are never offered the option of ownership, so there is never a sale of the machine that has been transacted. Spot rentals – a grower can rent a combine from his local dealer, a neighbor or rent from a custom cutter. If it's a grower to grower there probably isn't an option to own it. Most dealers will lease a combine to a grower at harvest time if they have one on their lot that is available for rental. There is an opportunity to own that machine.

The situation with the tax law, this law is very difficult to manage. Most of our machines in our fleet are purchased new from dealers but there is always situations where we have purchased a machine from a dealer that might be a year old, it might have had less than 200 hours on it, it was previously owned by a farmer, we bought the machine and put it in our lease fleet. Now by ND state law, we can't rent that machine to a farmer in ND and charge him sales tax because it was previously owned by a farmer. It met one of the 3 criterions that Sen. Krauter outlined. We have to make a clear distinction between leasing and renting.\

Sen. Oehlke: If you buy a machine new and rent it our for 1 yr what would the average for 100 hrs what would the 3% be on that?

Answer: the lease or the rental payment that he would make to our company is somewhere around fifteen to eighteen thousand dollars depending on the size of that machine.

Sen. Oehlke: if that machine is rented out under this bill if it went through rented out for 1 yr, so the 3% tax of \$400 or \$800 or whatever it is, but the full price of that machine has never suffered sales tax then has it? A \$250,000 combine we're talking about because, did you have to pay that sales tax?

Answer: in some cases the sales tax has been previously paid if the machine was previously owned by a farmer. If we bought it brand new, in some cases we actually never take

ownership of these combines either. We may be making a lease payment to a dealer some where in the country. And when that machine has been in our fleet for about 3 years, it's turned back into the dealer and new lease arrangement has been established. In some cases there is no sales transaction has taken place there either. It becomes a very complicated situation. It becomes a fairness issue and this will reduce the complexity of trying to administer this program where we go from 3 yrs to 1 yr and tremendously uncomplicated the issue but doesn't solve the problem completely, either everybody pays the tax or no one pays the tax.

Sen. Cook: do you pay the sales tax on any machinery you own in any situation?

Answer: possibly, it depends I can't really answer that question.

Sen. Cook: do you know if you've paid any sales tax in the State of ND on any of the machinery in your fleet? Is it safe for me to say that most of the equipment you have was purchased out of state?

Answer: May have. Can't answer

Sen. Triplett: do you think it would be fairer if everyone should pay taxes or no one should pay taxes, do you have an opinion on that?

Answer: It would be fairer if everybody paid the tax or no one paid the tax.

Sen. Triplett: do you have an opinion as to whether we should make a distinction in the taxes as between a rental vs. a lease situation?

Answer: yes, I do because a true rental is much different than a finance leasing option, I believe a rental situation should not be subject to tax because a sale has not taken place.

Richard Schlosser: ND Farmers Union appeared in support stating this would help with situations that producers are making a change and having to look at getting newer equipment which costs a lot.

Brian Kramer: NDFB appeared in support stating they also would like some clarity and feels the 1 yr makes more sense.

Sen. Krauter: I want to clarify some questions, to my understanding, sales tax is only collected in ND and SD, when you get to the other playing states, there is no sales tax on this type of equipment.

Sen. Triplett: do you have any idea how many of these situations are rentals or leases? Half and half or?

Answer: this is why I looked at down to 1 yr vs. totally eliminating it saying if its been rented 1 time and after that you don't collect the tax on it.

Sen. Cook: you heard Mr. Steckler's explanation of this company, it's a for rental company only and if he bought a combine from a dealer in ND to rent, would he pay sales tax on the full purchase price of that combine?

Miles Vosberg: Tax Dept. I would say probably not because under the sales and use tax law, he has an option because under our existing law, if someone who purchases tangible personal property for rent or lease has an option, they can pay tax under purchase price up front and not charge tax on any of the lease or rental payment or they can buy it for retail without paying the tax and charge tax on the rental or lease payments for those first 3 years. After 3 years none of the activity would be subject to tax because of our definition of used farm machinery.

Sen. Urlacher: so if they sold it after that 3 year collection, would there be a tax on it then?

Answer: if it was 3 yrs old, No.

Sen. Cook: what if they buy it from a state and bring it into ND and the state that they purchased it from does not have any sales tax on new equipment, is there a different set of requirements for them then, still have to charge sales tax on renting the piece of equipment?

Answer: Based on our definition of used equipment, they would have to determine whether that piece of equipment has been rented or leased for less or more for 3 yrs or whether its been owned by a farmer or not in that state. If they bought it brand new from a dealer they would have the responsibility or options when they bring into ND because of use tax. They would have to either pay the tax up front or collection tax on their rental.

Sen. Cook: is there a better way to solve or remove this problem?

Answer: it's difficult for dealerships. Redoing in another matter without a fiscal note, I don't know how we could do it and change the definition of used without having to change the F.N.

Sen. Tollefson: used farm machinery is not taxable right? Correct. Suddenly it becomes usable after 1 yr vs. 3, so the revenue to the State becomes some less as you indicated in the F.N. Where is it such a nightmare that you don't think it be workable anymore?

Answer: it would ease the responsibility because they'd have 1 yr rather than 3 to track this information. Administrative by the tax dept., it really probably doesn't matter to us, 1 yr or 3 yr doesn't complicate our job in any way.

Sen. Anderson: Either the existing law or the proposed new law, will it have an effect on more sales or transactions by ND machinery & Equipment?

Answer: we didn't build that into our F.N. But did comment on it.

Sen. Cook: if I lease a combine for 2 yrs and then purchase it, I'm going to pay the sales tax or the gross receipts on the full purchase price of that combine, correct? That's correct. If I lease it for 3 yrs and purchase the equipment the day after the 3rd yr, then I pay gross receipts tax only on the amount of the lease? Correct

Sen. Triplett: I think we should explore the fact of trying to simplify this as previously suggested by Sen. Cook.

Bob Lamp: ND Implement Dealers Association appeared saying they have mixed emotions about the bill. It offers another retail opportunity, but when we put in the definitions of used equipment back in 2001 there was some basis of substance for those decisions at that time and on the leasing side of it, the principal reasons was to prevent the situation where a producer could lease a piece of equipment for a very short period of time turn around and buy out that piece of equipment at the end of that lease period with the objective of avoiding the gross receipts sales. There was some issues happening in other states where the definition was not clear and there would be monthly leases made and then purchases made for that purpose. We do not oppose the idea of going to 1 yr although I think it does offer the opportunity for a lease buyout, leased own arrangement, which is not necessarily bad.

Reference of not taxing on rentals vs. taxing on leases would be huge step in the wrong direction in my opinion.

2007 SENATE STANDING COMMITTEE MINUTES

Bill/Resolution No. **SB 2311**

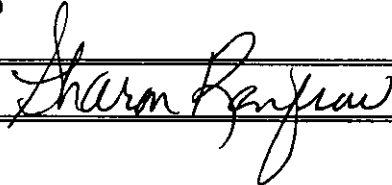
Senate Finance and Taxation Committee

Check here for Conference Committee

Hearing Date: January 29, 2007

Recorder Job Number: # 2176

Committee Clerk Signature



Minutes:

Sen. Urlacher opened discussion on SB 2311.

Sen. Tollefson asked for the amendment.

Sen. Cook asked if the amendment just adds an expiration date.

Sen. Tollefson responded yes.

Sen. Horne clarified that it adds a 2-year sunset.

Sen. Triplett commented that this is the same issue [as amendments from SB 2172] and suggested getting clarification from Legislative Council about how they interpret the sunset acts. Does it apply just to the amendment or to the whole bill? Need clarification before we can vote.

Sen. Urlacher stated that they will call Legislative Council to come down to explain the sunset.

Discussion on SB 2176 was closed.

2007 SENATE STANDING COMMITTEE MINUTES

Bill/Resolution No. **SB 2311**

Senate Finance and Taxation Committee

Check here for Conference Committee

Hearing Date: January 30, 2007

Recorder Job Number: # 2321

Committee Clerk Signature

Sharon Kenyon

Minutes:

Sen. Urlacher called the committee back to order for further discussion and action on SB 2311.

Sen. Cook: this is the bill that was introduced to deal with the renting and leasing issue on used farm machinery. I have met with several people trying to solve the issue that this is trying to address and that problem basically falls into the definition of used rental I believe, it treats rental different than leased I guess. We basically we agreed that there is not another solution out there other than changing the tax on new equipment to zero or we could change the new equipment to 1 ½ or 2% and used equipment is 1 ½ or 2% to make them all the same so there is no difference between new and used, this problem would go away. I think the consensus and Sen. Krauter said this is he would just as soon run this bill through the way it is. It changes the time period that you pay tax on your leasing from 3 yrs to 1 yr. So with that I would Move a **DO NOT PASS**, seconded by Sen. Oehlke.

Sen. Triplett: I'm not happy with this bill either the way it was explained and if we can't find a better solution but it does seem like there is an issue.

Sen. Oehlke: isn't there a resolution to study some of this tax related stuff in the next interim?

It doesn't really make it a third less of a problem it just means that we're collected a third less of the taxes, actually I think we're looking for ways for people to cheat.

Sen. Urlacher: a lot of the rentals on the smaller operators have no intention in buying it because of the quality of dollars it takes to run an operation.

Sen. Anderson: I had a problem when the fiscal note was distributed that there is a potential to structure the sale of new farm equipment under a 1 yr lease thereby eliminating the 3% which goes along with what Sen. Oehlke was saying, I'm scared of that. I think its going to make people dishonest I'm afraid.

Sen. Cook: we didn't have a problem really until I think this company came in that focuses on renting equipment, that's the one that has the problem.

Sen. Urlacher: how are car rentals handled?

Sen. Cook: same way, taxed up front on full purchase price.

Sen. Horne: Chairman Urlacher, your name is on the bill, I'm interested I your comments about the motion to DNP.

Sen. Urlacher: I'll vote accordingly.

Sen. Cook: we'll find out if he's going to shoot his own dog or just pet it.

Roll Call Vote: 4-3-0 Sen. Oehlke will carry the bill.

FISCAL NOTE
Requested by Legislative Council
01/17/2007

Bill/Resolution No.: SB 2311

1A. **State fiscal effect:** *Identify the state fiscal effect and the fiscal effect on agency appropriations compared to funding levels and appropriations anticipated under current law.*

	2005-2007 Biennium		2007-2009 Biennium		2009-2011 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues			(\$966,000)	(\$84,000)		
Expenditures						
Appropriations						

1B. **County, city, and school district fiscal effect:** *Identify the fiscal effect on the appropriate political subdivision.*

2005-2007 Biennium			2007-2009 Biennium			2009-2011 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts

2A. **Bill and fiscal impact summary:** *Provide a brief summary of the measure, including description of the provisions having fiscal impact (limited to 300 characters).*

SB 2311 redefines leasing requirements for farm machinery to be considered "used" for gross receipts tax purposes.

B. Fiscal impact sections: *Identify and provide a brief description of the sections of the measure which have fiscal impact. Include any assumptions and comments relevant to the analysis.*

The reduction in the lease time allowed in SB 2311 is expected to result in a decrease in state general fund and state aid distribution fund revenues of \$1.05 million, as shown above.

There is the potential for the provisions of SB 2311 to be utilized to structure the sale of new farm equipment under a one-year lease program, thereby eliminating the 3% gross receipts tax on new equipment. It is not known if, and to what degree, this might occur.

3. **State fiscal effect detail:** *For information shown under state fiscal effect in 1A, please:*

A. **Revenues:** *Explain the revenue amounts. Provide detail, when appropriate, for each revenue type and fund affected and any amounts included in the executive budget.*

B. **Expenditures:** *Explain the expenditure amounts. Provide detail, when appropriate, for each agency, line item, and fund affected and the number of FTE positions affected.*

C. **Appropriations:** *Explain the appropriation amounts. Provide detail, when appropriate, for each agency and fund affected. Explain the relationship between the amounts shown for expenditures and appropriations. Indicate whether the appropriation is also included in the executive budget or relates to a continuing appropriation.*

Name:	Kathryn L. Strombeck	Agency:	Office of Tax Commissioner
Phone Number:	328-3402	Date Prepared:	01/22/2007

PROPOSED AMENDMENTS TO SENATE BILL NO. 2311

Page 1, line 3, remove "and"

Page 1, line 4, after "date" insert "; and to provide an expiration date"

Page 1, line 22, after "**DATE**" insert "**- EXPIRATION DATE**"

Page 1, line 23, after "2007" insert ", and before July 1, 2009, and is thereafter ineffective"

Renumber accordingly

REPORT OF STANDING COMMITTEE

SB 2311: Finance and Taxation Committee (Sen. Urlacher, Chairman) recommends DO NOT PASS (4 YEAS, 3 NAYS, 0 ABSENT AND NOT VOTING). SB 2311 was placed on the Eleventh order on the calendar.

2007 TESTIMONY

SB 2311

SB 2311

Senate Finance & Tax Committee
Senator Urlacher, Chairman
January 23, 2007

Chairman Urlacher and members of the Senate Finance & Tax Committee, for the record my name is Aaron Krauter, State Senator from District 31, which encompasses parts of Morton and Hettinger counties and all of Grant and Sioux counties.

SB 2311 makes a change in the definition of the word "used" for rented farm machinery from three years to one year. Currently there is a tax of 3% on the gross receipts of sales of farm machinery. There are specific tax exemptions for the sale or lease of used farm machinery, farm machinery repair parts or used irrigation equipment used exclusively for agricultural purposes.

The definition of used has to meet one of three requirements to be considered used and meet the exemption.

- 1) the sales tax has been paid on a previous sale
- 2) originally purchased outside this state and previously owned by a farmer
- 3) has been under lease or rental for three years or more.

This 3rd requirement is where SB 2311 proposes to change to one year for the definition of used.

In today's farming business, the option of renting a certain piece of equipment is considered more than it was ten years ago. The reason is a combination of economics and possible newer technologies. Economics from the standpoint of tying up a large amount of capital (money) into a depreciating asset versus leasing a piece of equipment to complete the job it is needed for. The possibility of newer technologies comes at a higher price but renting allows the farmer the chance to use newer technology at less cost.

But the real issue comes with the definition of three year versus one year. The example that I use is you have farmer Ben who rents a three year old combine with 400 hours on the machine and pays no tax and then you have farmer Dwight who rents a two year old combine with 800 hours on the machine and pays the tax. It seems a little unfair for farmer Dwight who rents a machine with more wear and tear on it to pay a tax. Then we have farmer Herb who comes along and rents a machine that is one year old with 200 hours on it but was traded in to the dealer and had the sales tax paid on it originally, so Herb pays no tax.

As you can see this can get quite confusing. Lets look at this from the implement dealers point of view and record keeping. Farmer Ben's machine has been rented for it entire life so once it reaches three years it is used. Farmer Dwight's machine was mistakenly thought to be rented but was really taken in on trade last year and the dealer overcharged Dwight and it was Herb's machine that was bought at an auction in Minnesota and the dealer is not sure it was owned by farmer.

This does get confusing and a managing nightmare. These scenarios happen because we have many different type of machinery being rented; i.e. tandem disks, sprayer, loader tractor and the list goes on. Let alone if the North Dakota State Tax Department is actually going to go out to check the birth dates on farm equipment.

To simplify the definition from three years to one will help to eliminate many of these problems.

Also, I have an amendment that would put a two year sunset on this bill to address any concerns about the unknown fiscal effect of the change.

Mr. Chairman and committee members I know that there are others here to testify and I ask for your favorable support and will stand for any questions.