

FISCAL NOTE
Requested by Legislative Council
01/10/2017

Bill/Resolution No.: HB 1224

- 1 A. **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.*

	2015-2017 Biennium		2017-2019 Biennium		2019-2021 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues			\$(40,400,000)	\$(3,850,000)		
Expenditures						
Appropriations						

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

	2015-2017 Biennium	2017-2019 Biennium	2019-2021 Biennium
Counties			
Cities		\$(2,900,000)	
School Districts			
Townships			

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

HB 1224 creates a sales and use tax exemption for purchases made on behalf of an exempt entity.

- 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.*

Section 1 of HB 1224 deals with a sales tax exemption and Section 2 deals with a use tax exemption for materials acquired by a contractor on behalf of an exempt entity.

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.*

If enacted, HB 1224 is expected to reduce state general fund and state aid distribution fund revenues by an estimated \$44.25 million in the 2017-19 biennium. Additionally there will be a reduction in locally imposed sales and use taxes estimated to total \$2.9 million for the 2017-19 biennium.

- 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 or a part of the appropriation is included in the executive budget or relates to a continuing appropriation.*

Name: Kathryn L. Strombeck

Agency: Office of Tax Commissioner

Telephone: 701.328.3402

Date Prepared: 01/16/2017

2017 HOUSE FINANCE AND TAXATION

HB 1224

2017 HOUSE STANDING COMMITTEE MINUTES

Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1224
1/17/2017
26966

- Subcommittee
 Conference Committee

Committee Clerk Signature

Mary Brucher

Explanation or reason for introduction of bill/resolution:

A bill relating to a sales and use tax exemption for purchases made by a contractor, subcontractor, or builder on behalf of an exempt entity and relating to use tax on contractors.

Minutes:

Attachment 1, 2

Chairman Headland: Opened hearing on HB 1224.

Representative Weisz: Introduced bill. Our current law has some quirks that should be addressed. In reality the state is taxing tax exempt entities by the use tax that is currently in place. Our political subdivisions and hospitals are tax exempt. We are not technically charging them sales tax; we charge the contractor the use tax who performs work for these political entities. I think that is wrong because it is a tax shift for these political subdivisions. In a local county or township if they hire someone to haul gravel on the road the contractor doesn't pay use tax as long as he doesn't do anything with the gravel but only dumps it on the road. If he is also contracted to use his blade to spread the gravel on the road now the contractor is subject to use tax. He then charges more to the city, township, or county so in effect is paying the tax. If a contractor digs a ditch to put in a culvert, as long as the township or county drops the culvert in the ground and covers it up, there is no use tax but if he covers it up he pays the 5% use tax; same with a nonprofit hospital. If a hospital needed to put a new furnace in they purchase a furnace and install it themselves, then they don't pay any tax. If they purchase the furnace and hire the contractor to install the furnace, even though he didn't purchase it, he will pay the use tax on the furnace. He will then pass that cost on to the nonprofit who is tax exempt. I don't think that is fair because we've spent millions of dollars in the state off of property tax relief then we turn around and charge our cities, townships, and counties the 5% sales tax. It has the effect of shifting.

Chairman Headland: Are there any questions?

Representative Hogan: Do you have any sense on what the percentage is on the loss of \$40 million would be in the political subs versus the nonprofit?

Representative Weisz: On the hospital end it is pretty small.

Representative Hogan: So it's mostly on the political subdivisions?

Representative Weisz: Yes. The net cost, the loss of federal funds coming in on projects and the hospitals was roughly \$4.5 million. That included both federal and the hospital.

Chairman Headland: Any other questions? Is there testimony in support of HB 1224?

Larry Syverson, Chairman of the Board of Supervisors of Roseville Township of Traill County: Distributed written testimony in support. See attachment #1. Also distributed a proposed amendment. See attachment #2. Ended testimony at 9:52.

Chairman Headland: Have you talked to a committee member about carrying your amendment for you? We generally don't take amendments from the audience.

Larry Syverson: It was just given to me this morning.

Chairman Headland: If you wouldn't mind working with a committee member to try and get someone to carry your amendment for you? It would be appreciated. Do you have any idea how to make up the \$48 million loss of revenue that is in this fiscal note?

Larry Syverson: I'm not aware of how much it costs our townships but I don't believe the fiscal note would be that large if we just limit it to road materials.

Representative Ertelt: Do you expect that contractors will reduce their charges by that amount going forward if this bill were to pass?

Larry Syverson: I'm sure that many contractors are not even aware until they are audited that they are responsible for this. Once they do find out they will be increasing. We'd like to stay ahead of that and prevent those increases.

Representative B. Koppelman: Do you know if any of the political subdivisions have plans for reductions in costs they have as a result of this bill to lower property taxes?

Larry Syverson: We apply for a levy to our county auditor based on the dollars required. If this bill results in a lower dollar required that is what we will tax.

Chairman Headland: Is there further testimony in support?

Terry Traynor, Association of Counties: This certainly affects the townships more than the counties but it isn't exclusive. If they are in a position for a contractor to put that material in place the contractor will hopefully know but then they get audited and get penalized for not paying the use tax. It's a complicating thing that increases costs to local government. It is really just converting property tax into sales tax. We would support an amendment that limits it to construction materials at least to see what impact that would have.

Chairman Headland: Further testimony in support? Is there any opposition to HB 1224? Myles, can you take a look at the amendment and see if you could come up with a fiscal note?

Myles Vosberg, Tax Commissioner's Office: I haven't seen the amendment but I can certainly look at it. We prepared the fiscal note during the study in the interim and broke it down between contracts. We could pull that apart a bit and come up with an estimate. If it says highway materials or road materials, we might want to define that a bit so it's clear as to what is included in that.

Chairman Headland: The way we collect use tax has been done for decades. Do you think that most contractors now building the cost of the tax into their bids?

Myles Vosberg: It has been going on for a long time. I wouldn't say everyone knows. All contractors are subject to tax regardless of whether the owner of that project is exempt or subject to tax.

Representative B. Koppelman: Do you have any breakdowns on the use tax portion of it versus the sales tax portion? The fiscal note appears to include both.

Myles Vosberg: I don't know if we can break that apart or not. We tried to identify a reasonable amount of contracts that we could anticipate in the next biennium. We assumed 30% of that was materials and applied a 5% tax on that. Under normal circumstances I would say the contractor purchases the materials and pays their tax at the time of purchase. If this bill were to pass you would probably push more of those arrangements to the exempt entity buying the materials whenever possible. I don't know how much of the materials would be purchased by the exempt entity versus those that would be purchased by the contractor.

Representative B. Koppelman: Would you be able to provide how those taxes are paid and how much is paid in use tax on those projects?

Myles Vosberg: From the sales and use tax returns by contractors we could look at how much tax is remitted on purchases. We really wouldn't know how much is being paid to the retailers.

Representative Olson: Could you also provide data on how much contractors are being stung for these taxes they didn't collect that was found in an audit?

Myles Vosberg: We could look back at our audit. It wouldn't necessarily reflect exempt entity jobs though.

Representative Olson: If we can't figure that out then it's not worth looking into.

Chairman Headland: This is a bill we struggled with during the interim, the past two prior sessions, and we'll be struggling again.

Representative Ertelt: Is there some other chain of events where other political subdivisions or tax exempt entities could make that purchase directly so they don't have this problem?

Chairman Headland: They do make the purchases currently. It's only when they hire an independent contractor to do the work for them is the time when they pay the use tax for the nonprofits and the political subdivisions.

Representative Ertelt: Is the issue about the use only and not about the purchase of materials?

Chairman Headland: It would be but in some cases the independent contractor is probably making the purchase in which the sales tax would be due at that point.

Representative Hatlestad: The only difference is the sales tax when you buy it and the use tax is when you spread it on the road. You're paying the same amount of money whether it's sales tax or use tax, correct?

Representative B. Koppelman: At some point it would be nice to see us head away from the practice of use tax, putting the contractor in an impossible position, and then let the chips fall where they may. I think it would take care of a lot of the circumstances that they are asking us to take care of and probably not in one lump sum like this fiscal note suggests. To get to that point might be creating a bill from whole cloth. This could put government in competition with private sector with unequal yoke terms under our current practice. There are a lot of good merits to this concept but I don't think this bill form could take it to where it needs to be with the time frame we have and probably not with the tax atmosphere we have right now either. I'm probably going to be in opposition of this bill and I'm not interested in proposing an amendment.

Chairman Headland: We need to have a mechanism to follow the money which we could achieve with the REMI software in dynamic fiscal notes. We tried to get the software during the interim specifically for this bill to help us figure it out. If you do the math the true cost of this is probably only \$2 or \$3 million versus the \$48 that we have to deal with while we're looking at this bill. Maybe next session if we get the REMI software through we will have a mechanism to deal with this, today I don't believe we do. I'm in agreement with Representative B. Koppelman.

Representative B. Koppelman: MADE A MOTION FOR A DO NOT PASS

Representative Hogan: SECONDED

Chairman Headland: Is there any discussion?

**ROLL CALL VOTE: 9 YES 5 NO 0 ABSENT
MOTION CARRIED**

Representative B. Koppelman will carry this bill.

Date: 1-17-17
 Roll Call Vote #: 1

**2017 HOUSE STANDING COMMITTEE
 ROLL CALL VOTES
 BILL/RESOLUTION NO. 1224**

House Finance and Taxation Committee

Subcommittee

Amendment LC# or Description: _____

- Recommendation: Adopt Amendment
 Do Pass Do Not Pass Without Committee Recommendation
 As Amended Rerefer to Appropriations
 Place on Consent Calendar
 Other Actions: Reconsider _____

Motion Made By Rep. Koppelman Seconded By Rep. Hogan

Representatives	Yes	No	Representatives	Yes	No
Chairman Headland	✓		Representative Hogan	✓	
Vice Chairman Dockter		✓	Representative Mitskog		✓
Representative Ertelt	✓				
Representative Grueneich	✓				
Representative Hatlestad		✓			
Representative Howe	✓				
Representative Koppelman	✓				
Representative Olson	✓				
Representative Schobinger	✓				
Representative Steiner	✓				
Representative Toman		✓			
Representative Trottier		✓			

Total (Yes) 9 No 5

Absent 0

Floor Assignment Rep. Koppelman

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE

HB 1224: Finance and Taxation Committee (Rep. Headland, Chairman) recommends **DO NOT PASS** (9 YEAS, 5 NAYS, 0 ABSENT AND NOT VOTING). HB 1224 was placed on the Eleventh order on the calendar.

2017 TESTIMONY

HB 1224

#1
1-17-17
HB 1224

Support HB 1224

House Finance and Tax Committee

January 17, 2017

Chairman Headland and Committee members,

I am Larry Syverson from Mayville, I raise soybeans on my farm in Traill County, I am the Chairman of the Board of Supervisors of Roseville Township of Traill County and I am the Executive Secretary of the North Dakota Township Officers Association. NDTOA represents the 5,600 Township Officers that serve in more than 1,100 dues paying member townships.

It is difficult to even guess how much the sales and use tax on contractors is costing township tax payers. It is a hidden tax, the contractor cannot charge a township the tax, but we know very well it is added into the bill.

Unlike counties, many townships do rely heavily on contractors to furnish and apply gravel, install culverts and such.

A township can purchase a culvert from a supplier or the county, tax exempt, but the contractor that is hired to install it has to pay use tax to install it so the township actually ends up paying that tax anyway. I believe it is wrong to make the taxpayers of a township pay tax on their property to pay sales or use tax.

I understand there is an amendment coming to make this bill only apply to road materials such as culverts, signs, gravel or other road surface treatments. We would welcome and support such an amendment.

Chairman Headland and Committee members I am grateful for this chance to again support eliminating this tax on townships. Please give HB 1224 your favorable recommendation.

#2
1-17-17
HB 1224

PROPOSED AMENDMENTS TO HOUSE BILL No. 1224

Page 2, line 6, after the period insert "For the purposes of this section, tangible personal property means road construction materials."

Renumber accordingly