

FISCAL NOTE
Requested by Legislative Council
02/08/2019

Amendment to: HB 1535

- 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.*

	2017-2019 Biennium		2019-2021 Biennium		2021-2023 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues			\$(146,000,000)			
Expenditures						
Appropriations						

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

	2017-2019 Biennium	2019-2021 Biennium	2021-2023 Biennium
Counties			
Cities			
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).*

Engrossed HB 1535 changes the individual income tax from a system with five rate brackets to a single flat tax rate.

- 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 engrossed HB 1535 creates a deduction from taxable income - similar to the federal standard deduction - based upon a taxpayer's filing status. This deduction is \$18,725 for single taxpayers and \$37,450 for married taxpayers filing a joint return.

The bill also removes the current individual income tax brackets and rates that range from 1.1% to 2.9% of taxable income. In place of these progressive rate brackets, the bill imposes a flat 2% tax on taxable income, which has been reduced by the deduction created in the bill.

(The bill also provides some statutory clean-up of obsolete references which will have no fiscal impact.)

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.*

The 2% flat rate established in the bill is expected to reduce state general fund revenues by an estimated \$146 million in the 2019-21 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 Strombeck

Agency: Office of Tax Commissioner

Telephone: 701.328.3402

Date Prepared: 02/11/2019

FISCAL NOTE
Requested by Legislative Council
01/14/2019

Bill/Resolution No.: HB 1535

- 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.*

	2017-2019 Biennium		2019-2021 Biennium		2021-2023 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues						
Expenditures						
Appropriations						

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

	2017-2019 Biennium	2019-2021 Biennium	2021-2023 Biennium
Counties			
Cities			
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 1535 changes the individual income tax from a system with five rate brackets to a single flat tax rate.

- 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 1535 creates a deduction from taxable income - similar to the federal standard deduction - based upon a taxpayer's filing status. This deduction is \$18,725 for single taxpayers and \$31,300 for married taxpayers filing a joint return.

The bill also removes the current individual income tax brackets and rates that range from 1.1% to 2.9% of taxable income. In place of these progressive rate brackets, the bill imposes a flat 2.5% tax on taxable income, which has been reduced by the newly allowed deduction amount.

(The bill also provides some statutory clean-up of obsolete references which will have no fiscal impact.)

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.*

The 2.5% flat rate established in the bill is expected to be approximately revenue-neutral. It will generate approximately the same revenue as the current individual income tax system of multiple bracketed rates.

- 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 Strombeck

Agency: Office of Tax Commissioner

Telephone: 701.328.3402

Date Prepared: 01/29/2019

2019 HOUSE FINANCE AND TAXATION COMMITTEE

HB 1535

2019 HOUSE STANDING COMMITTEE MINUTES

Finance and Taxation Committee Fort Totten Room, State Capitol

HB 1535
1/30/2019
31793

- ☐ Subcommittee
☐ Conference Committee

Committee Clerk: Mary Brucker

Explanation or reason for introduction of bill/resolution:

A bill relating to replacement of the individual, estate, and trust income tax rate schedule with a flat rate income tax.

Minutes:

No attachments

Vice Chairman Grueneich: Opened hearing on HB 1535.

Representative K. Koppelman: Introduced bill. This bill is a flat tax bill. North Dakota has a very low income tax already. The graduation really doesn't make a lot of difference. A flat tax state would simplify our tax code. I think it would also be something other people could clearly understand and it would be attractive to our taxpayers. I wanted to ensure this was revenue neutral to the state and that is was either neutral or beneficial to the people of the state. If anything, some taxpayers may even pay lower taxes. That occurs with the exemption especially for lower income taxpayers which is high enough that many of them will either pay no tax or very little tax. The same goes with higher income taxpayers because of that exemption so they will be paying a percentage on a threshold of income that's higher than that certain point. I was just informed that there is a marriage penalty in the bill but that was not my intent so we could fix that.

Vice Chairman Grueneich: The \$18.725, is that the fairness part? Where did we get to that point and how does that offset so the 2.5% isn't picking a winner or a loser?

Representative K. Koppelman: I didn't want to see winners or losers in this. If we can establish a flat tax, we are in a much better situation as a state to simplify our tax code. If we can make the exemption high enough it may result in some people paying less because I don't see anyone paying more.

Vice Chairman Grueneich: Was that your thought process mimicking that just a little bit as we increase that?

Representative K. Koppelman: It wasn't what motivated this but part of the result may be that.

Vice Chairman Grueneich: Is there further testimony in support?

Dustin Gawrylow, North Dakota Watchdog Network: We are in support of this. This is our preferred bill this session. We have supported flat tax bills as the preferred approach to tax policy the last few sessions. In 2015 on the Senate side there was a flat tax bill in the 2.5% range for rate that had a higher exemption but also eliminated a lot of other deductions and credits. I don't believe it was revenue neutral but there was a relatively low fiscal note. The goal is to create an exemption for everyone that is as high as possible. I won't advocate that you absolutely have to do revenue neutral. If it ends up being \$15 million or \$100 million cut, I think that's fairly sustainable for the long term. As long as those dollars are fed into the size of exemption so that more people at the bottom are getting that benefit it would make it easier. It's something both parties have accepted over the years. I informed the sponsor of the marriage penalty. Regardless of what you do on maximizing exemption make sure there is no marriage penalty then it would be good policy.

Representative B. Koppelman: We need to make sure the marriage is double the single then that would take care of that, is that right?

Dustin Gawrylow: Yes.

Vice Chairman Grueneich: Is there further testimony in support? Is there opposition? Are there questions for the tax department?

Vice Chairman Grueneich: On page 1 lines 20-23, could you clarify how we got there and what that means for us?

Joe Becker, Tax Department: I presume that's to help the folks on the lower end of our current graduated rate scale.

Vice Chairman Grueneich: How is that effective in helping our lower income people? What's the number?

Joe Becker: That's going to vary. Right now we have five rates running from 1.1% to 2.9% with the first three of those rates being 1.1, 2.04, and 2.27 while the tax rate here is 2.5 percent. That means that all the folks in those categories are going to get a standard deduction off of there but they are still going to be in a higher tax bracket than they were before. If you're going to do a flat tax, then dollars on that high end are going to have to shift somewhere so somebody will be picking that up.

Vice Chairman Grueneich: Who's going to get the brunt of that; what group?

Joe Becker: We'd have to run some numbers to see where that falls. We can run some comparisons through various income brackets to see what happens.

Representative Ertelt: Do you see the marriage penalty also exists in subsection c as well if you're married filing separately because that value is at \$15.650 versus the \$18.725 for single?

Joe Becker: Generally the married filing jointly is double what the single amount is and the married filing singly is generally one half of what the married filing jointly number is. You would have to adjust those numbers as well.

Representative Trottier: Do we have a state estate tax?

Joe Becker: No. Just a footnote, if you're going to build the marriage penalty into those standard deduction amounts then you may want to look at repealing the current marriage penalty credit which is not being addressed in the bill. If you have the graduated rate brackets, then it was helping. There is a marriage penalty credit relief on the books now but it's not being taken out by this bill.

Representative B. Koppelman: Does it appear there isn't a marriage penalty in here because the result of the marriage penalty less the marriage penalty credit is that there is no marriage penalty?

Joe Becker: No. The current marriage penalty credit calculation is based on graduated rate brackets. There is a fixed formula that's used to work with the lower two brackets. The current provision won't help you here.

Vice Chairman Grueneich: Is there anything further? We'll close the hearing on HB 1535.

2019 HOUSE STANDING COMMITTEE MINUTES

Finance and Taxation Committee Fort Totten Room, State Capitol

HB 1535
2/6/2019
32312

- ☐ Subcommittee
☐ Conference Committee

Committee Clerk: Mary Brucker

Explanation or reason for introduction of bill/resolution:

A bill relating to replacement of the individual, estate, and trust income tax rate schedule with a flat rate income tax.

Minutes:

Attachment 1

Representative B. Koppelman: Distributed proposed amendments, 19.0660.01001, see attachment 1. The amendments fix the marriage penalty by replacing the \$18,725 on the individual deduction amount to \$15,650 then rennumbers the bill after that. **MADE A MOTION TO ADOPT THE AMENDMENT**

Representative Steiner: SECONDED

Representative Ertelt: If changing that value down to \$15,650, that brings it in line with the married filing jointly and married filing separately but does that result in a no tax increase?

Joe Becker, Tax Department: It's really no different. There is a little bit of a change with the revenue neutrality generally still there but it really doesn't change the shifting around of the dollars. The lower end folks from about \$40,000 and down are okay but then there's an increase as it goes up.

Representative Ertelt: Is that included in this chart from HB 1319?

Joe Becker: I didn't know she included that in there. That's indicating that if we were to go into each of those AIG brackets. It presents us with a very interesting problem because everybody would have a different standard deduction. I think that's quite awkward. You'd have to come up with an interesting calculation on the tax return to deal with that.

Representative Ertelt: At the 2% rate is it clear there is no increase to any of the brackets?

Joe Becker: If we're just talking about a rate change 2.5% versus 2% no matter how we cut a flat tax it's going to shift the dollars around.

Representative Ertelt: On the individual brackets? If it was a flat 2% with these deductions would it result in an increase?

Joe Becker: There would be a fiscal impact to the 2%; \$70 million if you were going 2.5% one year and dropping it 2% the second year. It would be about \$136 million reduction if we just stepped down to two percent. It wouldn't be revenue neutral either.

Representative Kading: The math I did showed the bracket that increases the most is the \$50,000 bracket so you'd have to move the rate to 1.87% to make it the same.

Representative B. Koppelman: Not everybody has this chart but at a 2.2% rate for married filing jointly, income between \$90,000 and \$250,000 there is an average of 5% increase in tax at 2.2% rate. I think it would be very close to the bill sponsor's intent as far as it relates to individual taxpayers at a 2% rate. If we wanted something close to revenue neutral, I believe it would be at about a 2% rate and somewhere between \$100-140 million range for the fiscal note.

Representative Steiner: If we went to a flat tax rate after we went to 0% on the chairman's bill so that if we had to bring income tax back in the future then we would go to the flat tax. Have you thought about that option rather than doing one this biennium? I know you believe in the flat tax but if we can't afford it this session would it be something you would consider for the future if ever there was an income tax if we would go to zero?

Representative B. Koppelman: If things work out with the chairman's bill in the long term I think I would be in favor of eliminating the tax mechanism whenever we can afford to do it with the amount of legacy fund money. A flat tax is an easy tax to reinstall in the tax code if we need it unlike all the brackets. When you have a bracket in tax code there is a benefit to setting the rate to zero if you intend to come back to it and you want all those brackets. If you're going to have a flat tax where you're going to pay zero anyway I think that is a pretty simple bill without a lot of moving parts. If I were writing our tax policy from scratch there wouldn't be a tax deduction on the front end, it would just be a very low flat tax across the board. Simple is better. I hope we'll support this amendment. I also have another idea to run past the committee later in the discussion.

Representative Ertelt: In reviewing the numbers I'm going to resist the amendment. I believe the amendment should be increasing the married filing jointly and married filing separately to match what was listed for the single. Then move the flat rate down to 2% in order to keep it tax neutral for everyone. If you look at the values on the bracket for each individual taxpayer for single filing jointly half of that is the \$18,725. The first 50% of that bracket you're not paying tax on. If you had a tax of 2% there you'd be paying 1% tax because of the deduction of \$18,725. Then you'd have to carry that through for the married filing jointly and married filing separately to have it 50% of each one of those.

Representative B. Koppelman: We could do that. The marriage penalty has to be double of the single. I think you need to pick your rate. I just wanted to get the marriage penalty out of there.

Representative Ertelt: My concern is raising the tax on any individual taxpayer. I'd like to raise the deductions and lower the rate to ensure there isn't any additional tax for any individual taxpayer.

Representative B. Koppelman: I can change that if you like.

Representative Dockter: I can't support any amendments. We're trying to patch something up in hopes that it will work.

Representative Ertelt: I'd like to offer the amendment I was suggesting. On page 1 line 16 strike .5% to 2% and on page 2 line 7 replace \$31,300 with \$37,450. On page 2 line 15 replace \$15,650 with \$18,725. And on page 9 line 10 strike that line and renumber accordingly.

Chairman Headland: I think we are all just shooting from the hip.

Matt Peyerl, Tax Department: The 2% with the prior bill would have had a cost for one year of about \$70 million. Changing the standard deduction for married up a little will probably just add a little more to that price tag.

Representative B. Koppelman: \$70.7 million is the cost for year two. That's why I believe it would be a range of \$100-140 million.

Chairman Headland: I think that would be fairly accurate. We need to vote on Representative B. Koppelman's amendment first.

Voice vote was too close to tell so **ROLL CALL VOTE was taken: 3 YES 11 NO 0 ABSENT**
MOTION FAILED

Representative Ertelt: MADE A MOTION TO ADOPT AMENDMENT

Representative Toman: SECONDED

Chairman Headland: I've been on this committee for a while and I've seen every type of tax cut we've had in the last 20 years. I believe in reducing tax burden. I just don't know that I can go along with reducing revenue to the level that's in this bill now and tell Appropriations and the citizens of the state that we're going to have to find these types of deductions in order to balance and get out of here. As much as I want to be a tax cutter and I believe it's appropriate to reduce set burden when you can, I think the bill you supported yesterday is paid for in a way that allows us to do it. I just can't go along with this bill at this time.

Representative B. Koppelman: I hope the committee will support the amendment. It's going to cost \$100 some million to do it. We can then vote the bill out on the merits of whether or not you think we should give \$140 million tax cut or not.

Chairman Headland: I can go along with that. This is a better bill now but still unaffordable.

VOICE VOTE: MOTION PASSED

Chairman Headland: You have amended HB 1535 before you.

Representative Dockter: MADE A MOTION FOR A DO NOT PASS AS AMENDED

Representative Steiner: SECONDED

Chairman Headland: Is there anything else?

ROLL CALL VOTE: 10 YES 4 NO 0 ABSENT

MOTION CARRIED

Representative Blum will carry this bill.

****On 2-8-2019 Chairman Headland changed the bill carrier to Vice Chairman Grueneich.**

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1535

Page 1, line 3, after the semicolon insert "to repeal section 57-38-01.28 of the North Dakota Century Code, relating to the marriage penalty credit;"

Page 1, line 23, replace "\$18,725" with "\$15,650"

Page 9, line 10, overstrike "Marriage penalty credit under section 57-38-01.28."

Page 9, line 11, remove "j."

Page 9, line 12, replace "k." with "j."

Page 9, line 13, replace "l." with "k."

Page 9, line 15, replace "m." with "j."

Page 9, line 19, replace "n." with "m."

Page 9, line 21, replace "o." with "n."

Page 10, after line 25, insert:

"SECTION 2. REPEAL. Section 57-38-01.28 of the North Dakota Century Code is repealed."

Renumber accordingly

February 6, 2019

DP 2/6/19

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1535

Page 1, line 16, remove "and one-half"

Page 2, line 7, replace "\$31,300" with "\$37,450"

Page 2, line 15, replace "\$15,650" with "\$18,725"

Page 9, line 8, overstrike "i."

Page 9, overstrike line 10

Page 9, line 11, replace "j." with "i."

Page 9, line 12, replace "k." with "j."

Page 9, line 13, replace "l." with "k."

Page 9, line 15, replace "m." with "l."

Page 9, line 19, replace "n." with "m."

Page 9, line 21, replace "o." with "n."

Renumber accordingly

Date: 2-6-19
Roll Call Vote #: 1

2019 HOUSE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1535

House Finance and Taxation Committee

☐ Subcommittee

Amendment LC# or Description: \$18,725 to \$15,650

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. Steiner

Representatives	Yes	No	Representatives	Yes	No
Chairman Headland		✓	Representative Eidson		✓
Vice Chairman Grueneich		✓	Representative Mitskog		✓
Representative Blum		✓			
Representative Dockter		✓			
Representative Ertelt		✓			
Representative Fisher		✓			
Representative Hatlestad		✓			
Representative Kading	✓				
Representative Koppelman	✓				
Representative Steiner	✓				
Representative Toman		✓			
Representative Trottier		✓			

Total (Yes) 3 No 11

Absent 0

Floor Assignment _____

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

Motion failed

Date: 2-6-19
Roll Call Vote #: 2

2019 HOUSE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1535

House Finance and Taxation Committee

☐ Subcommittee

Amendment LC# or Description: p.1 line 16 strike 1/2% to 2%.

Recommendation: ☒ Adopt Amendment p.2 line 7 replace 31,300 to 37,450

☐ Do Pass ☐ Do Not Pass ☐ Without Committee Recommendation

☐ As Amended

☐ Place on Consent Calendar

Other Actions: ☐ Reconsider

☐ Rerefer to Appropriations

p.2 line 15
replace \$15,650 with \$18,725
p.9 line 10
strike line
renumber accordingly

Motion Made By Rep. Ertelt Seconded By Rep. Toman

Representatives	Yes	No	Representatives	Yes	No
Chairman Headland			Representative Eidson		
Vice Chairman Grueneich			Representative Mitskog		
Representative Blum					
Representative Dockter					
Representative Ertelt					
Representative Fisher					
Representative Hatlestad					
Representative Kading					
Representative Koppelman					
Representative Steiner					
Representative Toman					
Representative Trottier					

Total (Yes) _____ No _____

Absent _____

Floor Assignment _____

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

Voice Vote = Motion carried.

Date: 2-6-19
Roll Call Vote #: 3

2019 HOUSE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1535

House Finance and Taxation Committee

☐ Subcommittee

Amendment LC# or Description: 19.0660.01002

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. Dockter Seconded By Rep. Steiner

Representatives	Yes	No	Representatives	Yes	No
Chairman Headland	✓		Representative Eidson	✓	
Vice Chairman Grueneich	✓		Representative Mitskog	✓	
Representative Blum	✓				
Representative Dockter	✓				
Representative Ertelt		✓			
Representative Fisher	✓				
Representative Hatlestad	✓				
Representative Kading		✓			
Representative Koppelman		✓			
Representative Steiner	✓				
Representative Toman		✓			
Representative Trottier	✓				

Total (Yes) 10 No 4

Absent 0

Floor Assignment Rep. Blum - as of 2-8-19

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

Rep. Grueneich
is Floor Assignment
per Chairman.

REPORT OF STANDING COMMITTEE

HB 1535: Finance and Taxation Committee (Rep. Headland, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO NOT PASS** (10 YEAS, 4 NAYS, 0 ABSENT AND NOT VOTING). HB 1535 was placed on the Sixth order on the calendar.

Page 1, line 16, remove "and one-half"

Page 2, line 7, replace "\$31,300" with "\$37,450"

Page 2, line 15, replace "\$15,650" with "\$18,725"

Page 9, line 8, overstrike "i."

Page 9, overstrike line 10

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Page 9, line 13, replace "l." with "k."

Page 9, line 15, replace "m." with "l."

Page 9, line 19, replace "n." with "m."

Page 9, line 21, replace "o." with "n."

Renumber accordingly

2019 TESTIMONY

HB 1535

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1535

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