Prepared by the North Dakota Legislative Council staff for the Taxation Committee
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SPECIAL ASSESSMENTS - BACKGROUND MEMORANDUM

STUDY DIRECTIVES

Two separate directives call for study of special assessments. Section 2 of 2011 Senate Bill No. 2356 directs study of "use of special assessments for public improvements, use and administration of special assessments across the state, and alternative funding mechanisms available **and possible processes and procedures that would facilitate a transition to any recommended alternative funding mechanisms** (emphasis supplied)." Section 3 of 2011 House Bill No. 1322 calls for study of "use of special assessments for public improvements, use and administration of special assessments across the state, and alternative funding mechanisms available, **with emphasis on imposition and relative rate of special assessments against agricultural property, and including examination of agricultural property tax classification and assessment issues, with emphasis on these issues within and near city boundaries** (emphasis supplied)." The study directives are very similar with the exception of the emphasized language.

STATUTORY AUTHORITY FOR SPECIAL ASSESSMENT IMPOSITION

Under North Dakota law, cities have had authority to levy special assessments for improvements since 1897, recreation service districts have had that authority since 1975, water resource districts have had that authority since 1981, counties have had that authority since 1983, and townships were given that authority in 2001 legislation.

Thirteen chapters of Title 40 of the North Dakota Century Code govern improvements by special assessment in cities. Recreation service district and county authority for improvements by special assessments simply adopts the city provisions by reference. Water resource district special assessment levy authority and procedures are contained in Chapter 61-16.1. Township special assessment levy authority is governed by an abbreviated statutory procedure provided under Chapter 58-18. Because the provisions governing improvements by special assessments in cities are the oldest and most detailed and were the focus of 2011 legislative consideration, this memorandum reviews the stages of the special assessment process in cities and then briefly reviews the statutory provisions for special assessment levies by recreation service districts, water resource districts, counties, and townships.

INITIATION OF PROCESS FOR IMPROVEMENTS BY SPECIAL ASSESSMENT

An improvement district must be created as a jurisdictional prerequisite before a public improvement to be paid for by special assessments may be undertaken (*Merchant's Nat. Bank of Fargo v. City of Devils Lake*, 173 N.W. 748 (1919); Section 40-22-08). A special improvement district may be created by ordinance or resolution adopted by a city governing body by a majority vote, except a two-thirds vote of the governing body is required to establish a sewerage system (Sections 40-22-08 and 40-22-02).

Although there is no statutory provision for initiation of improvements by special assessment through a petition process, it appears from discussions with city officials that special assessment districts are almost universally initiated by petition of property owners. After a petition is received or the governing body decides to proceed, the city generally schedules an informal meeting with property owners or notifies them by mail that a project will be considered. The size and the form of a special assessment district is a matter to be decided entirely by the city governing body after consultation with the city engineer (*Robertson Lbr. Co. v. City of Grand Forks*, 147 N.W. 249 (1914); Section 40-22-09).

A city may create a water district, sewer district, water and sewer district, street improvement district, boulevard improvement district, flood protection district, parking district, or business improvement district. After a special improvement district has been created, the city governing body must direct the city engineer to prepare a report as to the nature, purpose, and feasibility of the improvement and an estimate of the probable cost of the project (Section 40-22-10). The city governing body must direct the city engineer to prepare detailed plans, specifications, and cost estimates for construction of the improvement (Sections 40-22-10 and 40-22-11).

The city engineer's report is required to include a separate statement of the estimated cost of the work for which bids will be accepted and a separate statement of all other items of estimated cost not included in the cost of the improvement under the contract (Section 40-22-10).

After filing and approval of the city engineer's report, the city governing body may adopt a resolution declaring the necessity of the improvements (Section 40-22-08). A resolution of necessity is not required if the improvement is a water or sewer improvement, the improvement will be paid for by service charges, or a petition signed by owners of a majority of the area of property included within the district has been received. The resolution must be published once each week for two consecutive weeks in the official newspaper of the city (Section 40-22-15).

PROTEST OF IMPROVEMENTS BY SPECIAL ASSESSMENT

Within 30 days after the first publication of the resolution of necessity, owners of property in the

proposed improvement district are entitled to file written protests against adoption of the resolution (Section 40-22-17). If protests are filed, the city governing body must consider the protests at its next meeting after the expiration of the time for filing protests. If the protests received contain the names of owners of a majority of the area of property within the improvement district, the protest is a bar against proceeding further with the improvement project (Section 40-22-18). If the protests contain the names of owners of a majority of any separate property area included within the district, the protest is a bar against proceeding with the portion of the improvement to be assessed in whole or in part upon property within that area.

Concerns about the statutory requirement of protests by owners of a majority of the property within an improvement district prompted introduction of 2001 Senate Bill No. 2346. The bill would have excluded political subdivision property from consideration in protests and allowed a successful protest to be made by owners of a majority of the remaining property in the district. The bill failed to pass but pointed out the problem with existing law that a political subdivision could structure a special improvement district to contain a majority of property owned by the political subdivision, which would make it impossible for remaining property owners to successfully protest the project.

Concerns about the statutory requirement of protests by owners of a majority of the property within an improvement district prompted introduction of 2011 House Bill No. 1220. The bill would have changed the basis for a successful protest to bar proceeding with a special assessment project from the current requirement of protest by owners of a majority of the property in the district to a requirement of protest by owners of property that will be subject to a majority of the proposed costs of the project. The bill failed to pass the House of Representatives.

PROJECT BIDS

After adoption of a resolution of necessity and if sufficient protests are not filed, the city governing body must advertise for bids on a project. Public improvement contract bidding is governed by Chapter 48-01.2 (Section 40-22-19). The city governing body must award a contract for construction of a public improvement to the lowest responsible bidder (Section 48-01.2-07). The governing body may reject any bid and readvertise for proposals if no bid is satisfactory. If a contract for construction of a public improvement is estimated to exceed $100,000, plans, drawings, and specifications must be procured from a licensed architect or registered professional engineer (Section 48-01.2-02). Before acceptance of any bid, the city governing body must require the city engineer to reestimate the cost of the work under the bids. The governing body may not award the contract if the city engineer's estimate of the cost of the work subject to bids exceeds the engineer's original estimate of the cost of the work subject to bids by 40 percent or more (Section 40-22-29). Under Section 40-23-24, if ultimate costs of an improvement exceed the costs of the work as contained in the engineer's original estimate by 70 percent or more, the governing body of the city shall secure an audit of all costs included in the assessment for the project. The audit report must include a separate statement of the engineer's original estimate of the cost of the work, the actual cost of the work, the cost of extra work, engineering fees, fiscal agents' fees, attorneys' fees, publication costs, warrant printing costs, interest costs, and each separate item of expense incurred in making the improvement and levying the assessment for the improvement. The city is required to make a copy of the audit report available without charge to any person who requests a copy.

ASSESSMENT OF BENEFITS TO PROPERTY OWNERS

The executive officer of a city must appoint three "reputable residents and freeholders" of the city to the special assessment commission for the city. The special assessment commission must determine the lots and parcels of property which will be "especially benefited" by the improvement and "determine the amount in which each of the lots and parcels of property will be especially benefited" and assess against each of such lots and parcels "such sum, not exceeding the benefits, as shall be necessary to pay its just proportion of the total cost of such work . . ." (Section 40-23-07). As an alternative, the special assessment commission may assess benefits against property on a per-square-foot basis with consideration of the distance of the property from the marginal line of the public way or area improved (Chapter 40-23.1). Property of political subdivisions is not exempt from special assessments (Sections 40-23-07 and 40-23.1-06).

Under Section 40-23-25, the special assessment commission shall prepare and file with the city auditor a list of estimated future assessments on property located outside the corporate limits of the city at the time of contracting for an improvement but which the special assessment commission determines is potentially benefited by the improvement and likely to be annexed to the city.

Either the special assessment commission or the city auditor must prepare a complete list of benefits and assessments showing each lot, tract, or parcel benefited by the improvement and the amount assessed against it (Sections 40-23-09 and 40-23.1-07). Either the commission or the city auditor must publish the assessment list in the official city newspaper once each week for two consecutive weeks and include a notice of the time and place when the commission or the city auditor will meet to hear objections to any assessment by any interested party (Sections 40-23-10 and 40-23.1-08). At the hearing, the special assessment commission or the

city auditor may make alterations in assessments as may be just or necessary (Sections 40-23-11 and 40-23.1-09). Any person still aggrieved after consideration by the commission or city auditor may appeal by filing a written notice of appeal stating the grounds for the appeal (Sections 40-23-14 and 40-23.1-12).

At the regular meeting of the city governing body at which the assessment list is to be acted upon, any person who has appealed may appear and present reasons why the action of the commission should not be approved. The governing body of the city may increase or diminish any assessment as it deems just (Sections 40-23-15 and 40-23.1-13).

RESTRICTION OF AMOUNT OF BUDGET COSTS PAYABLE BY SPECIAL ASSESSMENTS

Under the terms of 2011 House Bill No. 1331, which failed to pass, special assessments against property would have been restricted to payment of no more than 50 percent of the cost of an improvement project. The apparent intention of the legislation was to force political subdivisions to find other ways to finance public improvement projects.

COLLECTION OF SPECIAL ASSESSMENTS

A special assessment is a lien against the property on which it is levied (Section 40-24-01). Special assessments may be paid by a property owner without interest within 10 days after they have been approved by the city governing body (Section 40-24-02). After 10 days, interest accrues on special assessments at an annual rate not exceeding one and one-half percentage points above the average net annual interest rate on any warrants or bonds for which they are pledged. Special assessments are generally payable in annual installments, which for most projects may be extended for up to 30 years (Sections 40-24-04 through 40-24-08). Annual installments of assessments must be certified by the city auditor to the county auditor annually for collection with property tax collections (Section 40-24-11).

Under Section 40-26-01, it is provided that courts shall review levy and apportionment of special assessments. However, North Dakota Supreme Court decisions (*Soo Line R.R. v. City of Wilton*, 172 N.W.2d 74 (N.D. 1969); *United Public School District v. Burlington*, 196 N.W.2d 65 (N.D. 1972); *Cloverdale Foods Co. v. City of Mandan*, 364 N.W.2d 56 (N.D. 1985)) have concluded that it is not the province of the court to substitute its judgment for that of the commission making the assessment, but merely to determine whether the commission was within its jurisdiction, was not mistaken as to the applicable law, and did not act arbitrarily, oppressively, or unreasonably, and to determine whether there is substantial evidence to support or justify the determination. Enactment of 2011 House Bill No. 1322 provided by amendment to Section 40-26-01 that if an action challenges the determination of benefits and special assessments imposed for agricultural property, the decision of the special assessment commission regarding agricultural property is not entitled to deference by the court and the court shall consider the determination of benefits and special assessments imposed for agricultural property de novo.

WARRANTS OR BONDS

After a construction contract for an improvement has been entered and the time has passed for filing protests, the city governing body may issue warrants or improvement bonds on the fund created for the improvement district (Section 40-24-19). Warrants or bonds are payable from the fund and if the fund has insufficient amounts for payment, the city may issue refunding special assessment warrants or bonds. Refunding special assessment warrants or bonds may be issued to extend maturities, reduce the rate of interest, equalize taxes to be levied by the city, or consolidate two or more outstanding issues of warrants or bonds.

Enactment of 2011 Senate Bill No. 2356 provided that under Chapter 40-22.1, allowing special assessments for business promotion, a municipality may not issue warrants, bonds, or any other form of indebtedness in anticipation of levy and collection of special assessments for business promotion.

SPECIAL ASSESSMENTS FOR PROMOTION OF BUSINESS ACTIVITY

Cities have authority under Chapter 40-22.1 to establish a special assessment district for business promotion to include all properties that will be benefited by the business improvement project. Under Chapter 40-22.1, an auditor's report and plans, specifications, and estimates must be prepared, and a resolution of necessity must be adopted and published. Protests filed by owners of one-third or more of the area of property in the district bar further proceeding with the project. The provisions of law governing special assessment collection and indebtedness apply to special assessments for business promotion.

RECREATION SERVICE DISTRICT SPECIAL ASSESSMENTS

A recreation service district is allowed to levy special assessments to provide services, including police protection, sewer and water, garbage removal, and public road construction and maintenance. Any recreation service district is deemed to be a "municipality" for purposes of special assessment provisions under Chapters 40-22 through 40-27 (Section 11-28.2-04.1).

WATER RESOURCE DISTRICTS

A water resource board may provide for the cost of construction, alteration, repair, operation, and maintenance of a water resource district project through issuance of improvement warrants or with funds raised by special assessments, general tax levy, issuance of revenue bonds, or a combination of these methods (Section 61-16.1-15). The water resource district board may assess the proportion of the cost of the project against parcels of land in proportion to the benefits to each parcel. Provisions for administration of special assessments by water resource districts are provided by Chapter 61-16.1.

COUNTY SPECIAL ASSESSMENTS

For a defined area outside the limits of any incorporated city, the board of county commissioners may initiate a special assessment district and levy special assessments for improvements. Under Section 11-11-55.1, a county is given all the authority and duties with regard to special assessments which belongs to cities in Chapters 40-22, 40-23, 40-23.1, 40-24, 40-25, 40-26, 40-27, and 40-28, and whenever action is required of city officials in those chapters, the comparable county officials shall take the action.

TOWNSHIP SPECIAL ASSESSMENTS

Under Chapter 58-18, created by 2001 Senate Bill No. 2328, townships are given authority to defray expenses of improvements through special assessment districts. A board of township supervisors may create an improvement district upon petition of 60 percent of the freeholders in a proposed improvement district area. Each improvement district must be of a size and form to include all properties the township board of supervisors believes will be benefited by the improvement project. The bill created a definition of the term "freeholder" for purposes of Title 58, meaning the legal title owner of the surface estate in real property.

After a township special improvement district has been created, the board of township supervisors is required to direct a competent engineer to prepare a report on the nature, purpose, and feasibility of the improvement and the probable costs of the work. The board of township supervisors must provide 30 days' written notice by first-class mail to each freeholder within the improvement district and publish a notice in a legal newspaper published in the township or, if there is no such newspaper, in the county's official newspaper at least 10 days prior to a special meeting for public disclosure of the findings of the engineer.

At the special township meeting for public disclosure of the findings of the engineer, the freeholders of the township in attendance are entitled to vote on the question of whether to proceed with the improvement project. Approval by 60 percent or more of the votes cast at the meeting or filed with the township clerk within 15 days after the meeting is required before the project may proceed. A freeholder affected by the project is entitled to one vote for each dollar of the proposed special assessment against the freeholder's property within the proposed improvement district. If there is more than one owner of a parcel of property, the votes available for the parcel must be prorated among the owners in accordance with their percentage ownership interests. If fewer than 60 percent of the votes cast on the question approve the project, the election result is a bar against proceeding further with the improvement project.

Aggrieved freeholders may appeal an assessment against their properties by notice of appeal to the township clerk. The township must schedule a special meeting to hear appeals. An aggrieved freeholder may present reasons to change the freeholder's assessment at the special meeting and the board of township supervisors may increase or diminish any assessment as it may deem just.

AGRICULTURAL PROPERTY TAX ISSUES

The study directive from 2011 House Bill No. 1322 includes examination of agricultural property tax classification and assessment issues, with emphasis on these issues within and near city boundaries. Under current law, there is no effect on agricultural property assessment from being located within and near city boundaries.

Under Section 57-02-01, agricultural property is defined as platted or unplatted lands used for raising agricultural crops or grazing farm animals. The Tax Department interprets statutory provisions to mean that agricultural property remains assessed as agricultural property until its primary use is changed. If property is used primarily for farming but is also used for other nonprimary uses such as fee hunting, the property retains agricultural property classification status. Under Section 57-02-01, platted land loses its status as agricultural property when any four of the following conditions exist:

1. The land is platted by the owner.
2. Public improvements, including sewer, water, or streets, are in place.
3. Topsoil is removed or topography is disturbed to the extent that the property cannot be used to raise crops or graze farm animals.
4. Property is zoned other than agricultural.
5. Property has assumed an urban atmosphere because of adjacent residential or commercial development on three or more sides.
6. The parcel is less than 10 acres [4.05 hectares] and not contiguous to agricultural property.
7. The property sells for more than four times the county average true and full agricultural value.

Agricultural lands are assessed on the basis of productivity under a formula contained in Section 57-02-27.2. Formula valuation is intended to determine capitalized average annual gross return

from various kinds of production data and information from detailed soil surveys. In determining relative value of assessment parcels, the assessor shall apply the following considerations:

1. Soil type and soil classification data from detailed or general soil surveys.
2. The schedule of modifiers that must be used to adjust agricultural property assessments within the county as approved by the state supervisor of assessments.
3. Actual use of the property for cropland or noncropland purposes by the owner of the parcel.

The potential modifiers that have been approved by the State Supervisor of Assessments for agricultural property assessment purposes include inaccessibility, irregular fields, nonconformity, poor drainage, rocks, salinity, stream overflow, and wind erosion. There are no modifiers based on proximity to a city. It appears proximity to a city may influence some of the factors that could cause property to lose its agricultural status. However, if property retains its agricultural status, it appears proximity to a city will not affect the assessment of the property.