MEASURING EFFECTIVENESS OF PROPERTY TAX EXEMPTIONS GRANTED BY CITIES AND COUNTIES

Section 2 of 2013 Senate Bill No. 2014 directs a study of methods to ensure an accurate and reliable means is developed to measure effectiveness and accountability of property tax exemptions and other economic development incentives granted by cities and counties and to determine whether other taxpayers in the city or county ultimately derive a measurable benefit from granting of the incentives.

North Dakota law provides discretionary authority for cities and counties to provide property tax exemptions for new or expanding businesses under North Dakota Century Code Chapter 40-57.1; improvements to property under Chapter 57-02.2; new single-family residential or townhouse or condominium property, early childhood services property, pollution abatement improvements, or certain builder-owned property under Section 57-02-08; renaissance zone property under Chapter 40-63; and tax increment financing (TIF) districts under Chapter 40-58.

New or Expanding Business Exemption

In 1969 the Legislative Assembly created Chapter 40-57.1 to provide cities, for property inside city limits, and counties, for property outside city limits, an economic development tool. The primary economic development tool in Chapter 40-57.1 is authority of cities or counties to grant partial or complete property tax exemptions or the option to make payments in lieu of taxes for a limited period of time after negotiation with a potential project operator. The chapter also allows a project to receive an exemption from state income taxes for up to five years if approved by the State Board of Equalization.

After negotiation with a potential project operator, a city or county may grant a partial or complete property tax exemption for buildings, structures, fixtures, and improvements for up to five years from the date of commencement of project operations. The maximum length of a property tax exemption may be extended to 10 years if the project produces or manufactures a product from agricultural commodities. The option to make payments in lieu of taxes may be extended through the 20th year from the date of commencement of the project.

The property tax exemption or option to make payments in lieu of taxes is available for any revenue-producing enterprise. The income tax exemption available under Chapter 40-57.1 is limited to a primary sector business or a tourism business.

Exemption of Improvements to Buildings

In 1973 the Legislative Assembly created Chapter 57-02.2 to provide cities and counties discretionary authority to allow property tax exemptions for improvements to commercial and residential buildings and structures. The exemption is allowed if the city, for property within city limits, or the county, for property outside city limits, has adopted a resolution allowing the exemption. The duration of exemptions for improvements is limited to five years and does not apply to residential property unless it is at least 25 years old.

Tax Increment Financing

North Dakota law on TIF was first enacted in 1973 and is contained in Chapter 40-58, which is the chapter on urban renewal. Section 40-58-20 requires approval of a development or renewal plan for a development or renewal area. Under Section 40-58-01.1, "development or renewal area" is defined as "industrial or commercial property, a slum or blighted area, or a combination of these properties or areas that the local governing body designates as appropriate for a development or renewal project." Section 40-58-01.1 also defines "blighted area" as an "area other than a slum area which by reason of the presence of a substantial number of slums, deteriorated or deteriorating structures, predominance of defective or inadequate street layout, . . . unsanitary or unsafe conditions, deterioration of site or other improvements, diversity of ownership, tax or special assessment delinquency exceeding the fair value of the land, defective or unusual conditions of title, improper subdivision or obsolete platting, or the existence of conditions which endanger life or property by fire and other causes, or any combination of these factors, substantially impairs or arrests the sound growth of a municipality, . . . and is a menace to the public health, safety, morals, or welfare in its present condition and use." Whether these conditions exist in the area in question appears to be a question of fact that must be answered by the city governing body.

Creation of a TIF district "freezes" property valuations in that district for purposes of taxation by any political subdivision except the city. Even city general property tax levies apply only against "frozen" valuations of TIF district properties, and only the TIF district special fund levy applies against the incremental valuation of TIF district properties. A pool of money from existing funds or issuance of bonds is created to finance improvements within the TIF district. As property valuation from development within the TIF district increases, the amount of valuation exceeding the "frozen" valuation is subject to taxation only by the city for TIF district purposes, and the tax revenues from this valuation are segregated in a special fund to repay the bonds or other financing for the TIF project. Other taxing districts, such as a school district, continue to collect property taxes on property in the TIF district, but only up to the amount of the "frozen" valuation of the property.

As an alternative to sale of bonds for a TIF district, the city may grant a total or partial property tax exemption for the project in order to provide assistance to a project developer. The property tax exemption is limited to the tax increment value of the property. The property tax exemption may not extend for more than 15 years.

New Residential Property Exemption

Section 57-02-08(35) allows the governing body of the city, for property within city limits, or the governing body of the county, for property outside city limits, to approve by resolution an exemption for up to $150,000 of the true and full value of new single-family and condominium and townhouse residential property for up to two taxable years after the taxable year in which construction is completed and the residence is owned and occupied for the first time.

Early Childhood Services Buildings

Section 57-02-08(36) allows the governing body of the city, for property within city limits, or of the county, for property outside city limits, to grant a property tax exemption for the portion of a building used primarily to provide early childhood services by a licensed provider or used primarily as an adult day care center. The exemption is not available for property used as a residence.

Pollution Abatement Improvement Exemption

Section 57-02-08(37) allows the governing body of the city, for property within city limits, or the governing board of the county, for property outside city limits, to grant a pollution abatement improvement property tax exemption to abate emissions of pollution for part of an agricultural or industrial facility required to comply with local, state, or federal environmental quality laws, rules, regulations, or standards.

Builder-Owned Single-Family Residential Property Exemption

Section 57-02-08(42) allows the governing body of the city, for property within city limits, or the governing body of the county, for property outside city limits, to provide an exemption by resolution for new single-family residential property for the taxable year in which construction began and the next two taxable years, if the property remains owned by the builder, remains unoccupied, and special assessments and taxes on the property are not delinquent. A builder is limited to exemption for no more than 10 properties under this subsection in a taxable year within each jurisdiction that has approved the exemption.

Renaissance Zone Exemptions

A city may apply under Section 40-63-02 for Department of Commerce Division of Community Services approval designating a portion of the city as a renaissance zone. Under Section 40-63-03, the zone approval application must show all of the following criteria:

1. The property must all be within the boundaries of the city.
2. The city must propose a development plan.
3. The renaissance zone may not be more than 23 square blocks but may be expanded up to 38 blocks at a rate of one additional block for each 5,000 population beginning at a population level of 10,000.
4. All blocks in the zone must be contiguous except a single noncontiguous area not exceeding three square blocks may be included.
5. Proposed land usage for zoned property must include both commercial and residential property.
6. The application must include the proposed duration of renaissance zone status, not exceeding 15 years. The Division of Community Services may extend the duration of renaissance zone status in increments of up to five years.

The primary incentives for property owners or purchasers of renaissance zone property are income and property tax exemptions.

Income Tax Exemptions

1. An individual who purchases or rehabilitates single-family residential property as a primary residence as a zone project is exempt from up to $10,000 of personal income tax liability for five taxable years after the date of occupancy or completion of rehabilitation.
2. A taxpayer that purchases, leases, rehabilitates, or makes leasehold improvements to residential, public utility infrastructure, or commercial property for any business or investment purposes as a zone project is exempt from any tax on income derived from the business or investment location for five taxable years beginning with the date of purchase, lease, or completion of rehabilitation.
3. If the cost of a new business purchase, leasehold improvement, or expansion of an existing business as a zone project exceeds $75,000 and the business is in a city with a population not more than 2,500, an individual taxpayer may elect to take an income tax exemption of up to $2,000 of personal income tax liability for up to five taxable years.
4. If a property owner not participating in a renaissance zone project is required to make changes in utility services or building structure because of changes to property that is part of a zone project, the owner of the nonparticipating property is entitled to a state income tax credit equal to the amount of investment required to complete the required changes.
5. A credit against financial institutions tax, individual income tax, and corporate income tax is allowed for investments in historic preservation or renovation of property in a renaissance zone. The credit is 25 percent of the amount of investment, up to a maximum of $250,000. The credit may be claimed in the year in which the preservation or renovation is completed, and any excess credit may be carried forward for up to five taxable years.
6. A credit against financial institutions tax, individual income tax, and corporate income tax is allowed for investments in a renaissance fund organization. The credit is 50 percent of the amount invested and the credit may be carried forward for up to five taxable years. Renaissance fund organization investments are limited to a total amount of credits not exceeding $7.5 million for investments in renaissance fund organizations.

Property Tax Exemptions

1. A city may grant a partial or complete property tax exemption for single-family residential property, exclusive of the land, if the property was purchased or rehabilitated by an individual as a primary place of residence as a zone project.
2. A city may grant a partial or complete property tax exemption on buildings, structures, fixtures, and improvements purchased or rehabilitated as a zone project for any business or investment purpose for up to five years following the date of purchase or completion of rehabilitation.

EVALUATING TAX INCENTIVES

The Pew Center on the States released a 2012 report entitled *Evaluating State Tax Incentives for Jobs and Growth*. The report has been distributed to Taxation Committee members for review. The report concluded North Dakota is "trailing behind" among states in evaluation of effectiveness of tax incentives for economic development. The report lacks detail on what was considered in North Dakota. North Dakota has a business incentive accountability law (Chapter 54-60.1) that requires the Department of Commerce to collect and report to the Legislative Council information from state grantor reports on business incentives. Section 54-60.1-08 requires political subdivisions to compile an annual grantor report on any business incentive granted by the political subdivision. There is no requirement for compilation of the political subdivision grantor reports.