MICROFILM DIVIDER

OMB/RECORDS MANAGEMENT DIVISION
SFN 2053 (2/85) 5M

ROLL NUMBER

DESCRIPTION

2348

2001 SENATE FINANCE AND TAXATION

SB 2348

2001 SENATE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. 2348

Senate Finance and Taxation Committee

☐ Conference Committee

Hearing Date 1/31/01

Tape Number	Side A	Side B	Meter #
1		x	17.2-end
2	x		0-11.8
2/6/01 - 2		x	6.3-23
2/7/01 - 2	x		24.9-32
Committee Clerk Signature Lynelle N. Kraft			

Minutes:

Senator Urlacher: Opened the hearing on SB 2348, relating to the definition of true and full value for property tax assessment of subsidized housing.

Senator Larry Robinson: Co-sponsored the bill, testified in support.

Steve Stoner: Private Developer in Fargo, testified in support. This bill would provide some relief.

Senator Judy Lee: Co-sponsored the bill, testified in support. Written testimony attached. Proposed amendment.

Jim Knudson: Developer in Valley City, testified in support. We do service the lower income tenants, we are restricted in the amount of rent that we can charge. It's only fair that what were getting in income is what they are actually using for a basis of value.

Senator Kroeplin: There is no subsidizing of the rent for these low income individuals? The rent that you collect is what you get?

Jim Knudson: Right.

Lynn Fundingson: Director of Fargo Housing Service, testified in support. Most states make accommodations in this area.

James Toomee: Private Developer in Fargo, testified in support. In the last two years we've had meetings with the state Tax Department to discuss this issue. The Tax Dept. was sympathetic but felt it was a public policy matter that had to be decided by the legislature. Many states are battling with this issue, and many have passed measures for relief for property taxes.

Senator Urlacher: You have an annual audit on those requirements and expenditures for your budget?

James Toomee: That's correct.

Senator Stenehjem: Who actually owns the buildings?

James Toomee: Explains.

Senator Nichols: Is there a lot of variation in the way the assessors do their job?

James Toomee: I would say there's a great variation.

Senator Urlacher: There is a limited amount of rent that can be charged based on income? As costs increase, and wages go up, less people are eligible and you can't build that cost increase into the amount that you are able to charge?

James Toomee: The income amounts are set every year. Explains.

Senator Kroeplin: What is the percent of the tax credits?

James Toomee: 9% of the improvements of a project over a period of 10 years. So the tax credit is actually 90%.

Don Haugland: Accountant, has been involved with the tax credit projects. What the idea behind the tax credit is that the more equity you can put into a project, the less debt you have to have.

Neal Eriksmoen: Real Estate Appraiser in Fargo, testified in support. Provides handout and explains it.

Senator Wardner: How much would this bill decrease the true and full value?

Neal Eriksmoen: It depends on what they base it on, maybe 25%.

Ben Hushka: Fargo City Assessor, testified neutrally. Written testimony.

Pat Richard: Housing Finance Agency, testified neutrally. We do receive annually financial operation statements from these projects. As the bill provides, the owner of the project, if he desires this method of real estate taxation approach, would authorize our release of that information of that information to the local assessor.

Senator Urlacher: Do all the projects have tax credits?

Pat Richard: Not all subsidized housing have tax credits. The first projects that were developed utilizing the tax credits were in 1987. The total is 120 that have utilized the tax credits since 1987.

Senator Urlacher: Closed the hearing. Action delayed.

Discussion held 2/6/01. Meter number 6.3-23.

Amendment introduced from Senator Lee.

Discussion held 2/7/01. Meter number 24.9-32.

AMENDMENT ACTION:

Motion made by Senator Stenehjem, Seconded by Senator Christmann, to move admendment numbered 10629.0102. Voice Vote taken. All in favor, amendment adopted.

COMMITTEE ACTION: 2/7/01

Motion made by Senator Nichols for a DO PASS AS AMENDED, Seconded by Senator Kroeplin. Vote was 1 yea, 5 nays, 0 absent and not voting. Motion failed.

Motion made by Senator Wardner for a DO NOT PASS AS AMENDED, Seconded by Senator Christmann. Vote was 5 yeas, 1 nay, 0 absent and not voting. Bill carrier was Senator Wardner.

FISCAL NOTE

Requested by Legislative Council
01/24/2001

Bill/Resolution No.: SB 2348

Amendment to:

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.*

	1999-2001 Biennium		2001-2003 Biennium		2003-2005 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues						
Expenditures						
Appropriations						

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

1999-2001 Biennium			2001-2003 Biennium			2003-2005 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts

2. Narrative: *Identify the aspects of the measure which cause fiscal impact and include any comments relevant to your analysis.*

SB 2348 defines true and full value of subsidized housing for property tax purposes. There is no change in overall revenues for the state or political subdivisions.

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, of the effect on the biennial appropriation for each agency and fund affected and any amounts included in the executive budget. Indicate the relationship between the amounts shown for expenditures and appropriations.*

Name:	Kathryn L. Strombeck	**Agency:**	Tax Department
Phone Number:	328-3402	**Date Prepared:**	01/30/2001

10629.0102
Title.

Prepared by the Legislative Council staff for
Senator Lee
February 5, 2001

PROPOSED AMENDMENTS TO SENATE BILL NO. 2348

Page 1, line 13, remove "arriving at the true and full value of" and replace "this" with "true and full value means"

Page 1, line 14, remove "includes" and replace "and" with ". In determining the value by this approach, the assessor shall consider the restrictions imposed on the property by the subsidy program."

Page 1, remove lines 15 through 21

Page 1, line 22, remove "(2)"

Page 2, line 6, after "instrumentality" insert ", or their successors"

Renumber accordingly

Date: 2/7/01
Roll Call Vote #: 1

2001 SENATE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. 2318

Senate Finance and Taxation Committee

☐ Subcommittee on
or
☐ Conference Committee

Legislative Council Amendment Number 10629.0102

Action Taken Move Amendment (voice vote)

Motion Made By Stenehjem Seconded By Christmann

Senators	Yes	No	Senators	Yes	No
Senator Urlacher-Chairman					
Senator Wardner-Vice Chairman					
Senator Christmann					
Senator Stenehjem					
Senator Kroeplin					
Senator Nichols					

Total (Yes) 6 No 0

Absent 0

Floor Assignment

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

Date: 2/7/01
Roll Call Vote #: 2

2001 SENATE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. 2348

Senate Finance and Taxation Committee

☐ Subcommittee on
or
☐ Conference Committee

Legislative Council Amendment Number

Action Taken Do Pass As Amended

Motion Made By Nichols Seconded By Kroeplin

Senators	Yes	No	Senators	Yes	No
Senator Urlacher-Chairman		✓			
Senator Wardner-Vice Chairman		✓			
Senator Christmann		✓			
Senator Stenehjem		✓			
Senator Kroeplin		✓			
Senator Nichols	✓				

Total (Yes) 1 No 5

Absent 0

Floor Assignment

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

Date: 2/7/01
Roll Call Vote #: 3

2001 SENATE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. 2348

Senate Finance and Taxation Committee

☐ Subcommittee on
or
☐ Conference Committee

Legislative Council Amendment Number

Action Taken Do Not Pass As Amended

Motion Made By Wardner Seconded By Christmann

Senators	Yes	No	Senators	Yes	No
Senator Urlacher-Chairman	✓				
Senator Wardner-Vice Chairman	✓				
Senator Christmann	✓				
Senator Stenehjem	✓				
Senator Kroeplin	✓				
Senator Nichols		✓			

Total (Yes) 5 No 1

Absent 0

Floor Assignment Wardner

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

REPORT OF STANDING COMMITTEE

SB 2348: Finance and Taxation Committee (Sen. Urlacher, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO NOT PASS** (5 YEAS, 1 NAY, 0 ABSENT AND NOT VOTING). SB 2348 was placed on the Sixth order on the calendar.

Page 1, line 13, remove "arriving at the true and full value of" and replace "this" with "true and full value means"

Page 1, line 14, remove "includes" and replace "and" with ". In determining the value by this approach, the assessor shall consider the restrictions imposed on the property by the subsidy program."

Page 1, remove lines 15 through 21

Page 1, line 22, remove "(2)"

Page 2, line 6, after "instrumentality" insert ", or their successors"

Renumber accordingly

2001 TESTIMONY

SB 2348

Mr. Chairman and members of the committee:

I am Senator Judy Lee from District 13 and I appear before you today to support SB 2348.

There are several investors in North Dakota who have been constructing apartment buildings for low and moderate income tenants. The rents in these buildings are required to be below a certain level in order to qualify for tax credits.

There has been a lack of clarity of the parameters for determining the true and full value of these apartment buildings, which has resulted in some assessors establishing values on the replacement costs, rather than considering what the rental income is. Because of this, the property taxes have been so high that the projects cannot cash flow. In at least one case, a project was not constructed, because the taxes were going to be so high that the numbers just wouldn't come out in the black.

This bill calls for using actual rental income and expenses in order to establish the true and full value for subsidized housing. The people who will follow me in appearing before you will give you additional information and will be able to provide more details on this problem which SB 2348 will help to solve.

I ask the committee to favorably consider SB 2348 and, by doing so, assist with the construction of low-income housing throughout both rural and urban areas of North Dakota.

January 31, 2001

THIS IS WHAT IT WOULD LOOK LIKE:

b. For purposes of subsidized housing, true and full value means the value determined by use of the income approach. In determining the value by this approach, the assessor must consider the restrictions imposed on the property by the subsidy program.

(2) The owner seeking valuation of property under this subdivision shall file a request for such valuation with the county director of tax equalization or city assessor by February 1st of each year. The request must be accompanied by a schedule of rents collected and rental expenses incurred in the prior year, information necessary to identify the property as subsidized housing, and consent for assessment officials to review information regarding the property in the possession of the housing finance agency, department of housing and urban development, farmers home administration, or other governmental agency or instrumentality, or their successors.

WRITTEN SUBMISSION OF STEVE STONER IN SUPPORT OF SENATE BILL 2348

Today the federal government provides affordable rental housing in our country by the Low Income Tax Credit Program (LIHTC). The LIHTC was established by the Tax Reform Act of 1986 as a tax incentive to private owners/investors to create rental property for low and moderately low-income families, seniors, and individuals. To claim tax credits and avoid credit recapture, LIHTC buildings must satisfy tenant income/rent restrictions for up to 30 years.

In North Dakota the LIHTC is available to buildings which are approved by North Dakota Housing Finance Agency (NDHFA). NDHFA selects the buildings and monitors them annually to ensure the income/rent restrictions are being observed. The restrictions require tenant incomes and rents be limited to levels based on medium income statistics set by HUD for each county in our country. For example, in Dunn County the restrictions are as follows:

Household Size	Income Limit	Maximum Rent
1-Person	$16,320	$437 - 1 BR
2-Person	$18,660	$525 - 2 BR
4-Person	$23,340	$607 - 3 BR

LIHTC Maximum Rents include all utilities.

Because of the tenant population served, limited rents, detailed tenant records which must be kept, and the annual reporting requirements to NDHFA, LIHTC buildings in North Dakota operate on an increasingly narrow margin of net income each year. This threatens the viability of existing buildings and will restrict future affordable housing development. In relation to expenses, a specific area of concern is the high percentage of income being paid by LIHTC buildings in property taxes.

By comparison to market rate rental property, LIHTC buildings have less income, higher expenses, and are more difficult to operate. It is estimated that a LIHTC building may have up to 30% less gross income and up to 15% more operating expenses. Yet LIHTC buildings pay a higher percentage of income to property taxes than market rate properties.

This disparity exists because assessors use the Cost Approach to determine taxable value. LIHTC buildings cost more to develop than market rate buildings due to complex LIHTC program requirements. However, rent limits imposed by the LIHTC, and the accompanying higher expenses, result in significantly lower income being produced. The fairer and more equitable method of determining taxable value for LIHTC buildings is to use the Income Approach. The State Tax Commissioner and local assessors are reluctant to use this method for LIHTC buildings believing it to be a "public policy" decision for the Legislature. Senate Bill 2348 provides a uniform and equitable method for the assessment of LIHTC buildings.

The proposed amendments to Senate Bill 2348 are made with the agreement of the assessor who spoke at the committee hearing and who now supports Senate Bill 2348 in its final form.

WRITTEN SUBMISSION OF NEAL ERIKSMOEN IN SUPPORT OF SENATE BILL 2348

My name is Neal Eriksmoen. I live at 1913 5th Street South in Fargo, ND. I am a licensed real estate appraiser in ND. In the course of my work I have noticed a Tendency towards the excessive taxation of Low Income Housing Tax Credit Properties. These are apartment properties that target low to moderate-income individuals and families.

It is my opinion that the excessive taxation occurs because of the reliance on the cost to construct these projects, rather than the income that they produce. Cost does not always equal value. Multi-family housing is bought and sold based on their ability to produce income, indicating that the Income Approach to Value is most important.

The development of a Low Income Housing Tax Credit Project in North Dakota results in a 30 year land use restrictive covenant between the owner and the North Dakota Housing Finance Agency, an agency of the State of North Dakota. This agreement limits the rental payments and requires the property to be leased to qualifying low or moderate-income individuals and families for a period of 30 years. This is a government control that must be considered in estimating the market value of this type of property, just like zoning would be considered in the appraisal of real estate.

I've indicated the cost of a Low Income Housing Tax Credit Project under the Investment Value heading (adjoining page). It is made up of a number of different expenses that are not typical of market rate apartment properties.

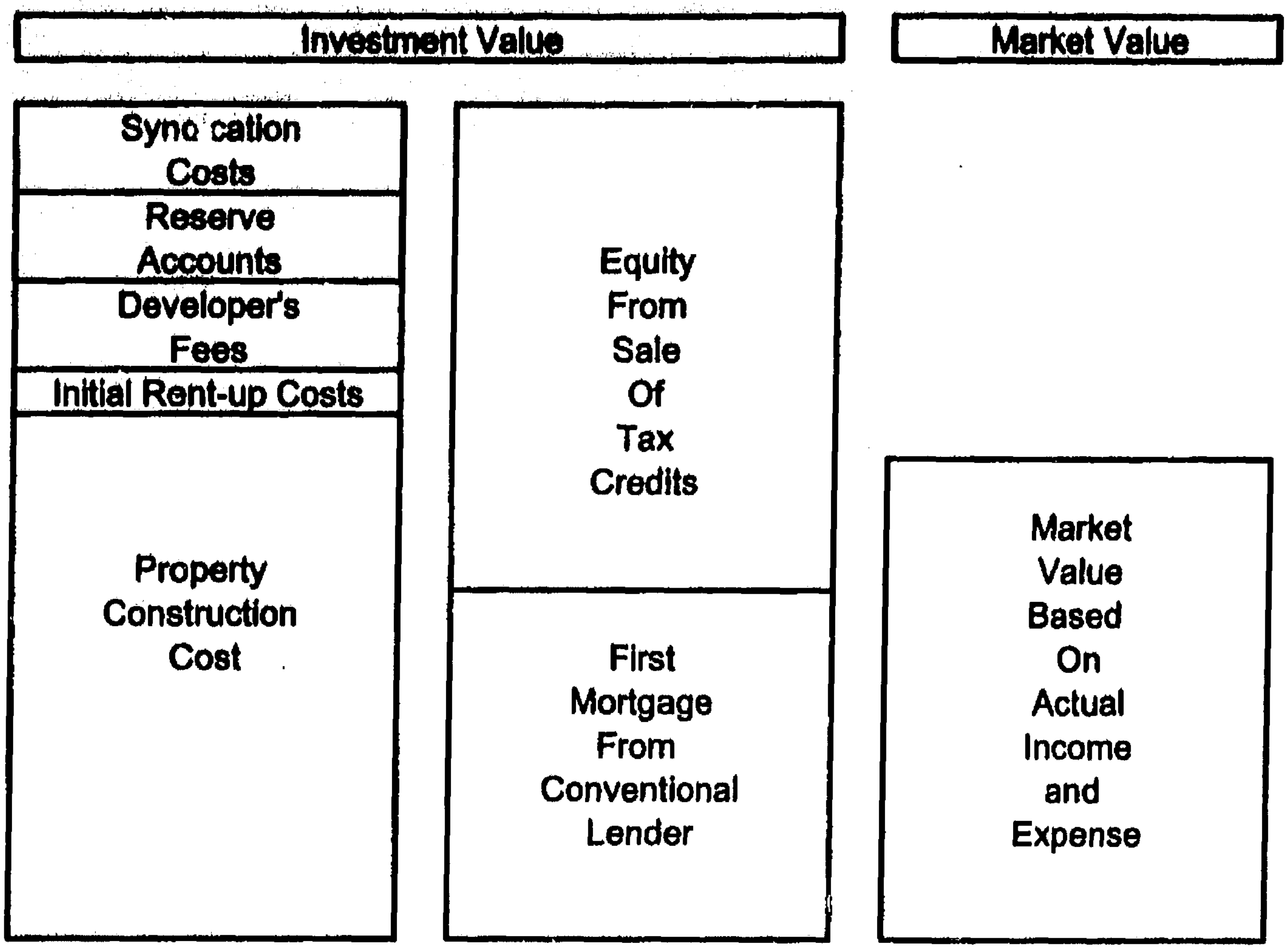
The middle column represents where the money comes from to develop LIHTC properties. Note the size of the mortgage. Lenders realize that the Market value of these properties is not equal to their costs, otherwise the mortgage portion would be 75% of the value.

When I estimate the market value of an LIHTC property for a lender, based on the income it produces, I arrive at a value that is represented by the third column, in relation to the overall cost of an LIHTC Property. Cost does not always equal value.

The Taxing procedure in ND is related in the middle of the page. The real estate tax in Fargo should be about 2.5% of value.

At the bottom of the page is an example of the Income Approach. You can see that it is not a complicated procedure. It indicates that the real estate tax should be equal to about 9-10% of the income. This is a fair amount. I've brought three statements from LIHTC properties that indicate taxes of 13 to 15.6% of the income.

Senate Bill 2348 would provide for the equitable taxation of this type of property. The excessive taxation of low-income housing will insure that this type of development does not occur in North Dakota. For this reason, I urge your support of Senate Bill 2348.



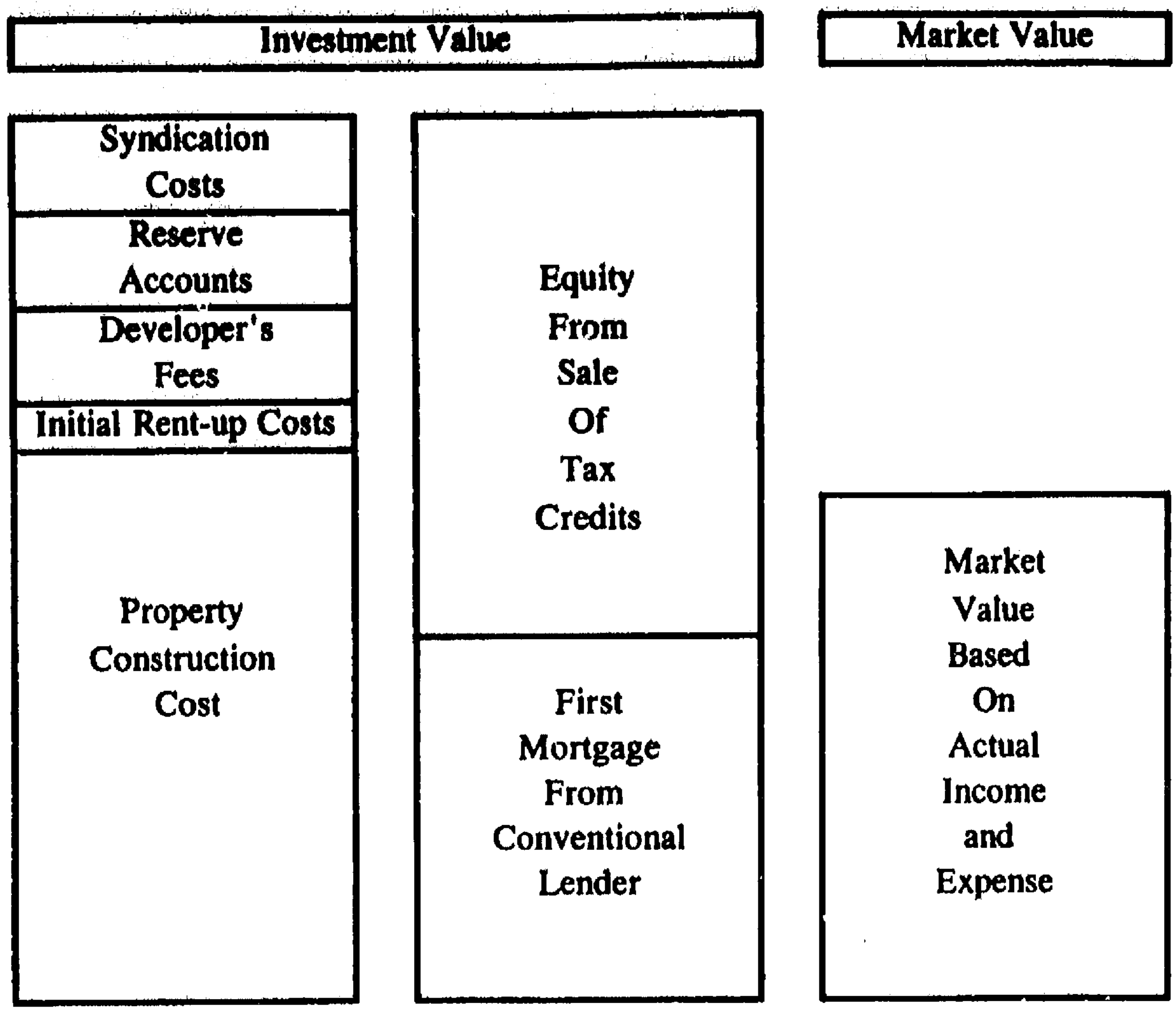
Taxing Procedure in North Dakota

True & Full Value (Market Value)		100%	
	X	50%	
Assessed Value		50%	
	X	10%	
Taxable Value		5%	
Fargo Mill Rate	X	0.49375	
Real Estate Tax as % of Value			2.4688%

Income Approach (LIHTC Property)

Gross Income (GI)	1.00	
Less Vacancy/Credit Losses (8% of GI)	(0.08)	
Effective Gross Income (EGI)	0.92	
Less Expenses (54%of EGI)	(0.4968)	
Net Operating Income	0.4232	
Overall Rate	12.0%	
Value (Net Operating Income /Overall Rate)		3.5267
Taxes as a percentage of Income (12% Overall Rate)		8.7065%
Taxes as a percentage of Income (10.5% Overall Rate)		9.9502%
Taxes as a percentage of Income (11% Overall Rate)		9.4980%

2348



Taxing Procedure in North Dakota

True & Full Value (Market Value)		100%	
	X	50%	
Assessed Value		50%	
	X	10%	
Taxable Value		5%	
Fargo Mill Rate	X	0.49375	
Real Estate Tax as % of Value			2.5%

Income Approach (LIHTC Property)

Gross Income	1.00	
Less Vacancy/Credit Losses	-8%	
Effective Gross Income (EGI)	0.92	
Less Expenses (55%of EGI)	54%	
Net Operating Income	0.42	
Overall Rate	12.0%	
Value (Net Operating Income /Overall Rate)		3.53
Taxes as a percentage of Income (12% Overall Rate)		8.7%
Taxes as a percentage of Income (10.5% Overall Rate)		10.0%
Taxes as a percentage of Income (11% Overall Rate)		9.5%

0348

EXPENSE COMPARABLE

LIHTC

Comparable:	
Address:	
Number Of Units:	22
GBA/Unit:	1,277
Heat Provided:	Yes
Basement Parking:	No
Elevator:	No
Age:	1997

Income/Expense Year:	1999 Historic		
		% EGI	Per Unit
Rental Income	$144,365	99.3%	$6,562
Garage Income	$0	0.0%	$0
Laundry Income	$20	0.0%	$1
Other Income	$962	0.7%	$44
EFFECTIVE GROSS INCOME	$145,347	100.0%	$6,607
LESS EXPENSES			
Real Estate Taxes	$18,946	13.0%	$861
Special Assessments	$0	0.0%	$0
Insurance	$1,973	1.4%	$90
Electricity/Gas	$8,390	5.8%	$381
Water, Sewer & Trash	$5,161	3.6%	$235
Maintenance/Repairs	$6,336	4.4%	$288
Paint/Decorate	$1,256	0.9%	$57
Cleaning	$488	0.3%	$22
Supplies	$579	0.4%	$26
Parking/Snow/Lawn	$2,755	1.9%	$125
Management	$5,400	3.7% +3	$245
Res Mgr/On-Site Mgr	$4,477	3.1%	$203
Other Salary-Security/Maint.	$3,341	2.3%	$152
Payroll Taxes	$0	0.0%	$0
Advertising	$266	0.2%	$12
Telephone	$306	0.2%	$14
Legal & Accounting	$1,599	1.1%	$73
Office/Administration	$2,872	2.0%	$131
Miscellaneous	$3,821	2.6%	$174
Replacements Reserves	$0	0.0% 49.8	$0
Total Expenses	($67,966)	-46.8%	($3,089)
NET OPERATING INC	$77,381	53.2%	$3,517

NORTH DAKOTA SENATE
FINANCE AND TAXATION COMMITTEE

Testimony of Ben Hushka
Fargo City Assessor
January 31, 2001

Mr. Chairman and members of the Senate Finance and Taxation Committee, my name is Ben Hushka. I am the City Assessor for Fargo.

I would like to address a few issues and concerns I have as an assessor in administering this bill should it pass in its present form.

In assessment, the more clearly defined a process or method is, the more uniformly it can be administered. Obviously the more ambiguous the law is in directing the tax process, the more inequity creeps into the system. I think most would agree that taxation among similar properties is best if uniform. That concept is based on the premise that like properties benefit similarly from the services that are provided through the property tax.

I would like to briefly point out some possibilities under this law if passed in its present form that could create some inequities and make administration difficult for assessment officials and boards of equalization.

- **Determination of the capitalization rate is not defined.** Since it is not clearly defined as to which capitalization rate to use or the method of determining it, there could be various interpretations of the appropriate rate. It could be argued that the rate should be derived from properties not involved in subsidy programs. It could also be argued that the rate for subsidized projects should be different due to the fact that there is less risk.

- **"Actual" income and expenses to be capitalized could be subject to different interpretations.** Questions could arise as to whether assessors should take the information as provided or establish some means to normalize it across similar projects. For instance, if two similar properties submit information and the expenses vary significantly, non-uniformity would exist if the actual income and expenses were capitalized as submitted. There would also be a question of whether reserves for replacement should be included as an expense or if "actual" repair and replacement costs in a given year should be used.
- **Exactly which actual expenses to be used is not clearly defined.** It is not clear whether expenses such as mortgage payments would be used. These would vary from investor to investor or by project. Also, expenses such as depreciation or items atypical of the market could be in question.
- **The time frame of the income to be capitalized is not defined.** Although this bill states that an owner seeking valuation by this method must certify income and expenses from the previous year, it is not defined if only that year's information is used. It is common practice in appraisal to utilize information over a period longer than one year to value by the income method.
- **Actual income and expenses could result in a partial assessment in the initial year.** In a case where a project finished construction in mid-year, there would only be partial income and expenses for that year. Existing law states that properties are valued as of February 1st each year. When the assessor values the property as of February 1st in this case, there is only partial (previous) year income and expenses to capitalize.
- **Not all subsidized housing projects would be assessed under the same method.** Only property owners who submit the information would be valued under this method. There could be cases, especially in smaller communities, where the subsidized income is actually higher than market rents.

- **Assessment officials would be required to reappraise these projects and reanalyze the income and expense information every year.** The requirement to analyze these projects individually and annually would shift work loads in assessment offices taking away from other areas of concern.

The issue of whether to create this new classification of property for a method of assessment other than present classifications in our property tax system is one I will not address. The basic question there is whether you feel it is in the best public interest to redistribute part of the burden of taxes to other classes of property to provide incentives to developers of subsidized, low income housing projects. That's a tough call.

I attempted only to point out some inconsistencies that could arise and possible problems assessors could face in administering this system.

This concludes my testimony. Thank you for your attention and, if you have any questions, I will try to answer them.