NORTH DAKOTA LEGISLATIVE MANAGEMENT

Minutes of the

TAXATION COMMITTEE

Tuesday, May 29, 2012
Roughrider Room, State Capitol
Bismarck, North Dakota

Representative Wesley R. Belter, Acting Chairman, called the meeting to order at 9:00 a.m. He said Senator David Hogue, Chairman, is unable to attend the meeting, and Representative Craig Headland, Vice Chairman, was detained but would arrive during the meeting.

Members present: Senators Randy Burckhard, Dwight Cook, Jim Dotzenrod, Lonnie J. Laffen, Dave Oehlke, Ronald Sorvaag; Representatives Larry Bellew, Wesley R. Belter, David Drovdal, Glen Froseth, Lyle Hanson, Patrick Hatlestad, Craig Headland, Richard Holman, Shirley Meyer, Mike Nathe, Marvin E. Nelson, Mark S. Owens, Roscoe Streyle

Members absent: Senator David Hogue; Representative Jim Kasper

Others present: Representative Jerry Kelsh, member of the Legislative Management, was also in attendance.

See Appendix A for additional persons present.

It was moved by Representative Drovdal, seconded by Representative Hatlestad, and carried on a voice vote that the minutes of the March 23, 2012, meeting be approved as distributed.

PROPERTY TAX STUDY

Chairman Belter called on Committee Counsel for a presentation of a bill draft [13.0088.01000] to provide property tax relief. Committee Counsel said the bill draft was prepared at the request of Senator Hogue and is intended to provide a residential property tax credit as additional property tax relief in combination with the mill levy reduction grant relief currently provided by allocations to school districts. Committee Counsel said the bill draft provides a reduction of $3,375 of taxable valuation of an individual's primary residence, which is equivalent to a reduction of $75,000 of true and full valuation. He said the reduction is increased for an individual 65 years or older to $5,625 of taxable valuation, which is equivalent to $125,000 of true and full valuation. He said the reduction is in addition to any homestead credit or property tax credit for disabled veterans to which the homeowner is entitled.

Committee Counsel said the bill draft makes the residential property credit available to certain kinds of residential property used in a farming or ranching operation and not exempt as a farm residence. He said the reduction would continue to apply for an individual who does not reside in the primary residence due to confinement in a nursing home, hospital, or other care facility as long as the residence is not rented to another individual.

Committee Counsel said the bill draft requires the property owner to file an annual application by March 1 to establish that the property owner was eligible for the reduction as of February 1 of that year. He said the bill draft requires the applicant to provide a Social Security or taxpayer identification number. He said any Social Security or taxpayer identification number is required by the bill draft to be used for purposes of administering the reduction and must be deleted or obscured from any document released to the public.

Committee Counsel said the bill draft provides that the reduction is effective only until the end of the taxable year. He said the reduction remains effective for the entire taxable year, even if the property is sold to another purchaser.

Committee Counsel said the bill draft provides a penalty for claiming the reduction for more than one property, in which case the reduction for that applicant must be canceled, and that applicant is not entitled to a reduction for the following two taxable years.

Committee Counsel said the bill draft provides an appropriation of $384 million, which is the estimated fiscal cost of the state payment for the residential property tax credit provided by the bill draft. He said the bill draft would be effective beginning with the 2013 taxable year.

Representative Drovdal asked if the bill draft would allow the buyer of a home to enjoy the property tax credit claimed by the seller earlier in the year. Committee Counsel said the credit would apply to the property for the entire year and would benefit the buyer of a home. He said from an administrative view, it would be difficult to allow the credit for a part of a year and subject the property to property taxes beginning at some point during the year.

Senator Sorvaag said if an individual over age 65 obtains the larger credit, a subsequent purchaser under age 65 would receive that benefit. Committee Counsel said that is correct.

Senator Cook said the bill draft uses the phrase "primary residence" and asked if that phrase appears elsewhere in the North Dakota Century Code or Constitution of North Dakota. Committee Counsel said he will search existing law to find any uses of the phrase.

Representative Nathe asked why the credit is available only for one year at a time. He said it seems it would be easier to allow the credit to be claimed once and remain available as long as the individual owns and occupies the home. Committee Counsel said it was suggested that the credit be available for just one year at a time, and that annual applications would have to be made to obtain the credit. He said he believes that approach would be intended to track ownership changes. He said he would provide further information on that question at the next committee meeting.

Representative Meyer asked if farm homes would be subject to property taxes under the bill draft. Committee Counsel said the status of farm homes would not change under the bill draft, and they would remain exempt from property taxes if the owner qualifies under the existing farm residence exemption.

Representative Kelsh said he is concerned about the possibility that a homeowner will fail to file the claim for the credit by the deadline. He said this would be a big issue because many individuals would not remember to complete the application and file it on a timely basis. He said he is also concerned that the bill draft provides no benefit in property tax relief for agricultural land.

Senator Laffen said if the state takes over property tax payments for a substantial part of property value, there may be an opportunity for political subdivisions to raise mill rates and increase the amount of property taxes the state would be required to pay. Committee Counsel said that possibility exists, and political subdivision levies are restricted by law to specific amounts in mills but if a political subdivision has additional levy authority within existing mill levy limitations, increases could be made.

Chairman Belter called on Mr. Jerry Coleman, Department of Public Instruction, for cost analysis of expanding the mill levy reduction grant property tax relief approach to cover up to 185 mills of school district property tax levies. Mr. Coleman said he was requested to expand the approach under the bill draft [13.0018.01000] under committee consideration based on the approach used to provide property tax relief for the years 2009 to 2013. He said some changes would have to be made in the bill draft, but his analysis is based on the assumption that up to 185 mills of relief would be provided for school districts. He provided a copy (Appendix B) of his analysis. He said the current cost estimate for 2013-15 biennium mill levy reduction grants of up to 75 mills is $395,622,720. He said additional grants of up to an additional 110 mills of mill levy reduction grants would cost an additional $604,796,492. He said the combined amount to provide up to 185 mills of mill levy reduction grants to school districts for the 2013-15 biennium would be $1,000,419,212.

Representative Nathe asked what that expenditure would provide as a property tax reduction. Mr. Coleman said the bill draft would have to be adjusted because the bill draft currently allows school districts to levy up to 110 mills. He said assuming that levy authority is eliminated, total property taxes statewide would be reduced by about 45 percent.

In response to a question from Representative Drovdal, Mr. Coleman said the elimination of school levy authority that would be funded under the bill draft is only for general fund, tuition, and transportation levies and would not include other levies of school districts for indebtedness or special levies.

Representative Kelsh said under the bill draft approach, property tax relief would be based on 2008 property tax levies of school districts. He said this would mean that a school district that levied 160 mills in 2008 would receive 160 mills of property tax relief. Mr. Coleman said that is correct.

Chairman Belter called on Mr. Ryan Rauschenberger, Deputy Commissioner, Tax Department, for information on the fiscal effect of the bill draft to provide a residential property tax credit for the first $75,000 of valuation of a primary residence, which is increased to $125,000 for property owners 65 years and older. He said the fiscal analysis is based on a sampling of seven counties to determine the number of primary residences affected and extrapolating that information to a statewide basis. He said the analysis assumes the mill levy reduction grant remains in place on the same basis as the 2011 legislation. He said with the mill levy reduction grant program in place, average statewide property tax levies are approximately 315.4 mills. He said using that basis and valuations of primary residences from the sampling, the estimated fiscal effect is approximately $384 million for the 2013-15 biennium, and about $20 million of that amount is attributable to the extra $50,000 of property value reduction for individuals 65 years and older.

Representative Nathe asked what $1 billion of mill levy reduction grant relief per biennium would provide as a percentage of property taxes. Mr. Rauschenberger said about 45 percent of property tax collections are for school districts so that would be close to the percentage of property tax relief. Representative Nathe asked how much property tax relief in dollars would be provided to a homeowner by state payment of taxes on the first $75,000 of value of a primary residence. Mr. Rauschenberger said reduction of about $75,000 in true and full value of a residence would provide about $1,000 per year of property tax relief, based on the statewide average mill rate.

Chairman Belter called on Ms. Marcy Dickerson, State Supervisor of Assessments and Director of the Property Tax Division, Tax Department, for testimony (Appendix C) relating to the feasibility of reconciling taxable years for mobile home taxes and residential, commercial, and agricultural property taxes.

Ms. Dickerson said mobile homes may be taxed as real property if they are permanently attached to a foundation, and the land is owned by the owner of the mobile home. She said the more common situation in North Dakota is that the mobile home is treated as personal property and subject to mobile home taxes under North Dakota Century Code Chapter 57-55.

Ms. Dickerson said real property taxes are based on value on February 1. She said the February 1, 2012, assessment is the basis for 2012 property taxes, which are due on January 1, 2013. She said mobile home taxes under Chapter 57-55 are assessed as personal property and are due on January 10. She said taxes paid in January 2013 are identified as 2013 taxes, paid in advance for the upcoming calendar year. She said 2013 mobile home taxes would be calculated using the same mill rates used for 2012 real property taxes, because 2013 mill rates would not be available until late 2013.

Ms. Dickerson said timing differences between mobile home taxes and real property taxes are confusing to property owners and tax administrators. She said providing property tax relief for mobile homes is problematic. She said when the mobile home tax law was enacted in 1963, mobile homes were required to pay property taxes for the upcoming year, probably to lessen the possibility of moving the mobile home to avoid paying taxes. She said moving mobile homes was more likely when mobile homes were small enough to be towed by an automobile. She said today most mobile homes are never moved from the original location.

Ms. Dickerson said political subdivisions receive mobile home taxes from January 10 to March 1. She said in January 2013 mobile home owners will pay mobile home taxes for 2013 at the same time owners of real property will pay taxes for the 2012 tax year. She said payment on mobile home taxes a year before real property taxes for the same year makes it impossible to change mobile home taxes to apply for the previous year without causing mobile home taxpayers to pay taxes twice for the same year. She said it would not be feasible to forgive a year of mobile home taxes because political subdivisions are counting on the revenue.

Ms. Dickerson said it appears there are two viable options to reconcile tax years for real property and mobile home taxes. She said Option 1 would be to provide that real property taxes and mobile home taxes are paid for the upcoming year. She said this would require making the real property tax payment a payment for two years, in name only. She said one drawback to the option is that special assessments and bond levies would be affected. She said one year of payments for these purposes would be missed, and the obligation would have to be extended an additional year. She said another drawback would be disruption of the equalization process for real property.

Ms. Dickerson said Option 2 would be to provide that mobile home taxes and real property taxes are paid for the prior year. She said this would put mobile homes on the same basis as real property is currently taxed. She said the most significant drawback to this approach is that mobile home taxes would be double for one year. She said it appears the fairest way to accomplish this change would be for the state to assume the cost of 2014 mobile home tax payments, which would be approximately $4 million. She said that would provide the anticipated revenues to political subdivisions and not require mobile home owners to pay tax twice for the same year. She said she believes Option 2 is preferable to Option 1.

Ms. Dickerson said it should be pointed out that the bill draft under committee consideration to reduce valuation of a primary residence does not include relief for mobile homes.

In response to a question from Representative Meyer, Ms. Dickerson said crew housing facilities are not taxable as real property nor as mobile homes under current law, but cities or counties may impose a fee for services provided.

Representative Nathe asked if Ms. Dickerson believes applying annually for the residential property tax credit creates problems. Ms. Dickerson said annual applications would require more paperwork for counties and would be very time consuming because of the large number of homes involved. She said the benefit to requiring annual applications would be to allow local officials to catch changes in ownership of property.

It was moved by Representative Froseth, seconded by Senator Cook, and carried on a voice vote that a bill draft be prepared to adjust mobile home taxes to the same annual cycle as real property taxes under Option 2 as suggested by Ms. Dickerson.

Chairman Belter asked if committee members have any comments or suggestions regarding the property tax relief study.

Representative Streyle said it appears it would be easier to provide property tax relief if state efforts focused on increasing per pupil payments to school districts. Senator Cook said the Education Funding and Taxation Committee is considering that option. He said there are several issues to be considered. Representative Streyle said it seems simpler and fairer to get equal benefit to students.

Senator Laffen said the Barnes County North School District is building a new school. He said the new school would replace schools nearly 100 years old for three school districts. He said those districts found it cheaper to build a new school to replace the old schools rather than trying to maintain the old schools. He said there is a lot of waste out there, but improvements are being made. He said North Dakota needs to achieve statewide property tax relief, but there also will be challenges to improve the efficiency of the existing functions of local government.

Representative Kelsh said he has concerns about efforts to provide property tax relief targeted to residential property. He said property tax relief needs to be general relief for all properties.

Representative Owens said the definition of primary residence in bill drafts considered by the committee should also include a stated number of acres of land. He said similar provisions in other states limit the acreage that would be subject to homestead credit, and an acreage restriction should be included in bill drafts being considered by the committee.

Representative Headland arrived and assumed the role of chairman. Chairman Headland called on Committee Counsel for presentation of the memorandum *Property Tax Exemptions Chronology*. Committee Counsel said in 1862 the first Dakota Territory Legislative Assembly enacted a property tax and provided property tax exemptions for property of the United States and Dakota Territory and political subdivisions and for cemeteries and land and buildings of literary and scientific institutions and benevolent, agricultural, and religious institutions. He said the 1889 Constitution of North Dakota provided property tax exemptions for federal and state property but not property of political subdivisions and provided that the Legislative Assembly shall by law exempt property used exclusively for school, religious, cemetery, or charitable purposes. He reviewed the memorandum and noted that a 1914 constitutional amendment not mentioned in the memorandum provided a property tax exemption for property of political subdivisions.

Committee Counsel reviewed a bill draft [13.0081.01000] requested to eliminate property tax exemptions granted at the discretion of cities or counties. He said the bill draft repeals Chapter 40-57.1 relating to exemptions for new and expanding businesses, Chapter 40-58 relating to urban renewal and tax increment financing, and Chapter 40-63 relating to renaissance zones. He said the bill draft eliminates Section 57-02-08(35) allowing an exemption for new single-family residential and townhouse and condominium property, Section 57-02-08(36) relating to early childhood services property, Section 57-02-08(37) relating to pollution abatement improvements, and Section 57-02-08(42) relating to homes still owned by the builder. He said the bill draft also repeals Chapter 57-02.2 relating to exemptions for property improvements. He said the effective date of the bill draft repeals the statutory provisions in 2013 but allows any exemptions granted before the repeal to remain effective for the duration of the exemption as granted by the city or county.

Committee Counsel distributed copies of the statutory provisions to be repealed by the bill draft.

Representative Streyle said looking at the chronology of property tax exemptions, it appears there has been continuing growth in the amount and kinds of property exempted. He said it appears it is time to consider reducing the amount of property exempt from property taxes.

Representative Drovdal said it appears property tax exemptions have been created by the legislature during times of no economic growth. He said the economic conditions have changed, and North Dakota is experiencing a period of rapid growth. He asked if there is information available on usage of discretionary property tax exemptions. Committee Counsel said he is not aware of current information on that question but the North Dakota League of Cities and North Dakota Association of Counties and other groups could be requested to gather information and provide it to the committee at the next committee meeting.

Senator Cook said the committee should investigate the feasibility of providing for property tax application for hospitals and similar facilities to the extent of police and fire protection and similar services provided by local government. He asked if that exemption is constitutionally provided. Committee Counsel said it appears it would be necessary to amend the constitutional provision to allow limited taxation of hospitals. Senator Cook said a proposal for a constitutional amendment should be prepared for committee consideration which would allow limited tax on some properties for basic services of local government that benefit those properties.

Senator Cook said job development authorities were authorized by legislation several years ago, and the committee should consider a bill draft to eliminate job development authorities.

Senator Cook said it would be useful to receive survey information on use of the $150,000 exemption that may be granted for new residential property. He said it would be useful to know if a lower exemption amount is being allowed in any city or county and if any city or county has ever allowed the exemption for new residential property and then ended the use of the exemption.

Representative Drovdal said with regard to the exemption to new residential property, input should be obtained from the North Dakota Association of Builders.

Committee Counsel distributed copies of a report disseminated by the Pew Center on the States, entitled *Evaluating State Tax Incentives for Jobs and Growth*. He said North Dakota is not discussed in detail in the report but is rated as "trailing behind" in evaluating the use of tax incentives. He said a report from the Department of Commerce will be presented at the next committee meeting regarding evaluation of tax incentives in North Dakota.

Committee Counsel distributed copies (Appendix D) of a communication from Ms. Clarice Liechty, Jamestown, relating to the bill draft [13.0052.01000].

Chairman Headland called on Committee Counsel to review a bill draft [13.0015.02000] providing for reporting of information on political subdivision, building authority, or other entity indebtedness. Committee Counsel said the committee at the previous meeting suggested that higher education institutions might also be included in reporting requirements. He said higher education institutions currently report information on indebtedness, which is compiled in supplementary information. He said a copy (Appendix E) of the June 30, 2011, schedule of bonds payable by higher education institutions is distributed to committee members.

Chairman Headland called on Mr. Scott Wegner, Arntson Stewart Wegner PC, for comments (Appendix F) relating to reporting of political subdivision bonded indebtedness and the effect of the passage of measure No. 2 on indebtedness of political subdivisions.

Mr. Wegner said information on bonded indebtedness is available from several sources. He said rather than imposing a reporting requirement, it would be preferable to have the Legislative Council or other gathering point prepare a listing from existing sources. He said information is available through the electronic municipal market access, municipal securities rulemaking board, United States Department of Agriculture, certain state agencies, and local banks. He said a better compilation would be achieved by having a single method of gathering and generating a list.

Mr. Wegner said if the committee prefers a reporting requirement, he would suggest adding the provisions to Chapter 21-06 relating to government finance. He said he would suggest that if reporting is required the reports should be filed with the Legislative Council or Advisory Commission on Intergovernmental Relations. He said joint powers agreements of political subdivisions are filed with the Advisory Commission on Intergovernmental Relations. He said he would suggest reporting requirements would apply only to future bond issues and that the Legislative Council would compile existing bond issue information. He said he also would suggest reporting within 60 days after bond issuance rather than as a precondition of issuance.

Mr. Wegner said he was requested to address the future prospects for political subdivision borrowing if measure No. 2 is enacted and property taxes are eliminated. He said if measure No. 2 is enacted, remaining options for political subdivision indebtedness would include water and sewer revenue bonds, sales tax revenue bonds, special assessment bonds, and MIDA bonds. He said there is a market for bonds backed by local sales tax revenue. He said special assessment bonds would no longer be backed by a possible deficiency levy from property tax sources. Committee Counsel asked if the lack of property tax backing would result in a higher interest rate on special assessment bonds. Mr. Wegner said that would be the likely result.

Mr. Wegner said if measure No. 2 is enacted, political subdivision indebtedness will not be available through general obligation bonds, limited tax levy bonds, tax increment financing, certificates of indebtedness, and lease revenue bonds, if property tax levies would be the source of lease payments.

Mr. Wegner said if measure No. 2 is enacted, he believes property tax-backed bonds issued before the effective date of measure No. 2 would not be impacted. He said he believes the state could not assume the debt on existing bonds but could provide funding for debt service or prepay or defease the bonds. He said one option for borrowing authority would be to authorize public school districts to levy a sales tax as backing for bond issues. He said the State Building Authority currently issues bonds to finance state buildings. He said the building authority could be authorized to issue bonds on behalf of school districts, and a method could be devised to provide that school districts would make payments to the building authority to pay the bonds. He said this bonding approach for school projects likely would not violate the state's constitutional $2 million debt limitation.

In response to a question from Representative Drovdal, Mr. Wegner said sales taxes of a political subdivision are workable as backing for indebtedness, but relative risk and interest rates are based on historical sales tax collections.

Senator Dotzenrod asked if compilation of information on political subdivision indebtedness could be done in a few hours or if it would require a greater commitment of time. Mr. Wegner said it would take a significant commitment of time initially and then maintaining the information would not be as intensive.

Representative Meyer asked if a person wants to find information about indebtedness of a political subdivision, whether the information is available. Mr. Wegner said the information is available, but some kinds of indebtedness may require looking in different locations.

Senator Sorvaag said it seems preferable to him to require political subdivisions to report indebtedness information to put the responsibility on them.

Senator Cook said the Legislative Council staff should do an indebtedness search for one sample county to see what information is there. Representative Meyer asked what the legislature and the public would do with the list of indebtedness. She said if legislators and the public do not believe political subdivisions are doing the correct thing on indebtedness, there are remedies. She questioned why legislation would add to the workload of political subdivisions by requiring reporting.

Senator Cook said he believes it should not be necessary for the public to seek information at various sources, and information should be available at a central source.

Representative Drovdal said it appears school district bonding would be significantly impacted by passage of measure No. 2. Mr. Wegner said school districts would be the hardest hit by passage of measure No. 2 in terms of ability to borrow money. He said school districts have no independent revenue source but could be given legislative authority to impose sales taxes. He said the State Building Authority could be a vehicle for school district borrowing, but statutory changes would be required.

Senator Cook said he likes the approach in the bill draft as it is. He said it will be useful for the Legislative Council staff to find out how long it takes to gather indebtedness information for political subdivisions.

Senator Sorvaag said he does not believe it would be a significant burden for political subdivisions to report information on indebtedness. He said he believes the bill draft should be changed to eliminate the requirement of indebtedness reporting before a bond issue. He said perhaps just requiring regular reporting of information, such as on a quarterly basis, would be workable.

Representative Meyer said quarterly reporting for all political subdivisions would require filing of approximately 2,100 quarterly reports. She said that seems an unnecessary burden on local governments. She said if the information is available from existing sources, it seems unnecessary to require reporting by political subdivisions.

Representative Kelsh said he agrees with Representative Meyer that reporting of indebtedness information by political subdivisions could impose an unnecessary additional burden.

Representative Belter said if he goes into the courthouse to seek information on indebtedness, the staff will have to assist him. He said in the end it may be easier for local government staff to report information than to provide individual assistance to people seeking information.

Senator Dotzenrod said as a property tax issue, taxpayers are ultimately liable for payment of the debt. He said there have been occasions in the past when legislators were not able to obtain information on indebtedness of political subdivisions, and state agencies did not know how to find information. He said he believes political subdivisions are getting into significant levels of indebtedness and he believes the state needs to be aware of what is happening on political subdivision debt issues and amounts.

SALES TAX STUDY

Chairman Headland called on Mr. Myles S. Vosberg, Director, Income, Sales and Special Taxes Division, Tax Department, for a presentation (Appendix G) of update information on streamlined sales tax issues. Mr. Vosberg said he anticipates a relatively small amount of legislation in 2013 to maintain North Dakota compliance with the Streamlined Sales and Use Tax Agreement.

COMMITTEE DISCUSSION

Representative Kelsh asked if it is required to have voter approval for all indebtedness of political subdivisions. Committee Counsel said information can be provided on the kinds of indebtedness that require voter approval.

Representative Nelson said the State Auditor should have information on political subdivision indebtedness collected through audit processes.

Representative Drovdal said lease-purchase arrangements should be treated as indebtedness. He said it does not appear lease-purchase arrangement debt issues would be on any described information sources because the debt is issued by a building authority or other entity. Committee Counsel said that is probably true and would be investigated.

Representative Streyle said he is concerned about park districts incurring debt. He said it appears park districts have authority to borrow, perhaps through the city. He said that issue should be investigated.

Representative Froseth requested information on how institutions within the North Dakota University System get approval to incur indebtedness.

No further business appearing, Chairman Headland adjourned the meeting at 12:15 p.m.

After adjournment, committee members were invited to tour AMCON Distributing Company under the guidance of Mr. John Job of AMCON Distributing Company. A copy of written information prepared by Mr. Job is attached as Appendix H. He said AMCON Distributing Company in Bismarck does cigarette excise tax stamping for customers in Minnesota, Montana, South Dakota, and Wisconsin. He said each of these states requires tax stamping for each package of cigarettes. He said AMCON Distributing Company was required to obtain a cigarette tax stamping machine to provide service for those customers. He said AMCON Distributing Company was able to obtain a reconditioned machine at an investment cost of about $80,000. He said if a distributor is unable to find a reconditioned machine, the cost of a new cigarette tax stamping machine would be approximately $140,000 to $150,000. He said the distributor would also need additional equipment, including an air compressor, three-phase power for the stamping location, and conveyors to move products to and from the stamping machine. He said AMCON Distributing Company also has a minimum of four people trained to operate the machine. He said the net result of these requirements is a substantial business cost for the distributor. He said each of the states for which AMCON Distributing Company does cigarette tax stamping operations has rules on minimum pricing of cigarettes, for the wholesaler to recover stamping costs.

John Walstad
Code Revisor

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