NORTH DAKOTA LEGISLATIVE MANAGEMENT

Minutes of the

ENERGY DEVELOPMENT AND TRANSMISSION COMMITTEE

Monday and Tuesday, October 10-11, 2016
Harvest Room, State Capitol
Bismarck, North Dakota

Senator Rich Wardner, Chairman, called the meeting to order at 10:00 a.m.

Members present: Senators Rich Wardner, Kelly M. Armstrong, Brad Bekkedahl, Bill L. Bowman, Philip M. Murphy, John M. Warner; Representatives Mike Brandenburg, Chuck Damschen, Ben Hanson, Corey Mock, Todd Porter

Member absent: Representative Dick Anderson

Others present: Senator Jessica Unruh, Beulah, member of the Legislative Management
See Appendix A for additional persons present.

It was moved by Senator Armstrong, seconded by Senator Bekkedahl, and carried on a voice vote that the minutes of the August 30, 2016, meeting be approved as distributed.

Chairman Wardner said the committee received information at the last meeting on a bill draft relating to an oil extraction tax exemption for enhanced oil recovery with carbon dioxide. He said the bill draft was presented to the committee for informational purposes and does not require committee action since the Taxation Committee was assigned the responsibility to study enhanced oil recovery.

BILL DRAFT RELATED TO WIND TURBINES

Bill Draft

The Legislative Council staff reviewed a bill draft [17.0273.01000] relating to a sales and use tax exemption for materials used in the construction of wind turbines. The bill draft removes the expiration date for the sales tax exemption and the use tax exemption. The bill draft includes a retroactive application to provide continuity between the existing expiration date and the effective date of the proposed changes.

In response to a question from Representative Porter, the Legislative Council staff said the retroactive application is anticipated to have no fiscal impact. He said both the sales tax exemption and the use tax exemption were administered based on the December 31, 2017, expiration date.

Wind Turbine Property Taxes

The Legislative Council staff presented a memorandum entitled *Property Taxes on Wind Turbines*. The memorandum provides information on the changes to the taxation of wind turbine electrical generation units as included in 2015 Senate Bill No. 2037. He said wind turbines which are completed before January 1, 2015, and which are less than 20 years from the date of first assessment are subject to a 3 percent valuation to determine the property tax levy, unless the wind turbines qualify for a lower valuation of 1.5 percent. He said all other wind turbines are subject to payments in lieu of property taxes, which are estimated to be the equivalent of valuing the wind turbines at 4.5 percent of the assessed value.

Estimated Fiscal Impact and Electrical Generation Tax Incentives

Mr. Ryan Rauschenberger, Tax Commissioner, Tax Department, presented information (Appendix B) regarding the estimated impact of the bill draft. He said an official estimate for the fiscal impact of the bill draft cannot be determined because the number of wind turbines that may be installed is unknown. He said the department prepared an example of the estimated fiscal impact based on a theoretical wind farm project of 500 megawatts. He said state sales tax collections would decrease by $20 million to $30 million if the sales and use tax exemption was made permanent and a 500 megawatt project was completed during the 2017-19 biennium.

Mr. Rauschenberger provided information (Appendix C) regarding a summary of federal and state tax incentives for electrical generation units, including coal-powered facilities and wind-powered facilities. He said the summary provides a comparison of property taxes, severance taxes, sales taxes, and income taxes at the state level as well as depreciation allowances and income tax credits at the federal level for electricity taxation. He said the department included calculations for costs per megawatt hour for each tax type and each power source based on actual scenarios as a comparison tool. He said the summary includes the two most significant tax incentives at the federal level even though other smaller, lesser known incentives may be available.

In response to a question from Representative Porter, Mr. Rauschenberger said complete tax parity between all resources used to generate electricity may not be possible particularly because of the impact of federal taxes and tax incentives.

Representative Brandenburg distributed information (Appendix D) regarding state and federal tax incentives for coal and oil extraction. He said the information was prepared for him by the Legislative Council staff as a supplement to the information provided by the Tax Department regarding electrical generation tax incentives.

Senator Bowman said developments and advancements in one energy resource may benefit another energy resource. He said oil and gas development activity increased the demand for electricity which may have resulted in benefits for the wind-powered electrical generation industry.

Cost and Benefit Analysis

Mr. Justin Dever, Co-Deputy Commissioner, Department of Commerce, presented information (Appendix E) regarding a cost-benefit analysis relating to a sales and use tax exemption for wind turbines. He said specific information regarding the incentives received by companies is not available due to confidentiality restrictions. He said the department calculated the estimated return to the state from the sales and use tax exemption by using publicly available data and an economic model for North Dakota developed by Regional Economics Models, Inc. He said based on the department's analysis for a sample case, the cost of the exemption is approximately $10.5 million with 50 percent of the cost returned to the state in 2 years and 7 percent per year returned to the state thereafter.

Purchased Power Agreements

Mr. John DiDonato, Vice President of Wind Development, NextEra Energy Resources, LLC., Juno Beach, Florida, presented information (Appendix F) regarding an overview of purchased power agreements. He said NextEra Energy Resources, LLC. has invested almost $2 billion in wind turbine development in North Dakota. He said purchased power agreements are long-term agreements between electricity suppliers and utility companies in which the suppliers agree to provide a certain amount of electricity to utility companies for a specified price. He said electricity suppliers carefully evaluate the tax environment before developing a project and entering into a purchased power agreement. He said the continuation of the sales and use tax exemption for wind turbines is an important factor when evaluating the cost and the return on investment for wind turbine projects. He said if the sales and use tax exemption expires, wholesale electricity costs may increase by $1.50 to $2.00 per megawatt hour.

In response to a question from Representative Porter, Mr. DiDonato said the sales and use tax exemption allows the electricity suppliers to maintain competitive pricing rates by reducing construction costs. He said the benefit of the sales and use tax exemption is passed on to end users because of the competitive pricing.

In response to a question from Chairman Wardner, Mr. DiDonato said generally, the average annual landowner payment for a wind turbine placed on the owner's land is $8,000 per megawatt of installed capacity. He said landowners can negotiate the terms for their payments, which could be based on a fixed dollar amount per turbine or the amount of electricity generated from each turbine.

In response to a question from Senator Bowman, Ms. Julie Voeck, Director, Regulatory Affairs, NexEra Energy Resources, LLC., Milwaukee, Wisconsin, said the in lieu of property tax payments for new wind turbines includes a fixed payment based on rated capacity of the turbine and a variable payment based on the electricity generated by the turbine during the taxable period.

Comments by Interested Persons

Mr. Alan Anderson, Commissioner, Department of Commerce, distributed information (Appendix G) regarding a policy update report for 2016 prepared by the EmPower ND Commission. He said the EmPower ND Commission supports the bill draft. He said the bill draft is based on one of the recommendations in the report.

Mr. Jason Bohrer, President and Chief Executive Officer, Lignite Energy Council, said the Lignite Energy Council supports the bill draft.

Mr. Brad Tollerson, Vice President of Planning and Strategy, Otter Tail Power Company, Fargo, provided comments (Appendix H) in support of the bill draft. He said the sales and use tax exemption may encourage the construction of additional wind turbines in North Dakota which will benefit landowners through easement payments, local political subdivisions through property tax revenues, and economic growth through job creation.

Mr. Greg Chamberlain, Regional Vice President of External Affairs, Xcel Energy, Minneapolis, Minnesota, provided comments (Appendix I) in support of the bill draft. He said Xcel Energy invested $260 million in a 150 megawatt wind turbine project in Rolette County and invested $300 million in a 200 megawatt wind turbine project in Courtenay. He said the sales and use tax exemption allowed the company to lower the costs of the projects which benefits rate payers with lower utility costs.

Mr. Jay Skabo, Vice President of Electric Supply, Montana-Dakota Utilities, provided comments (Appendix J) in support of the bill draft. He said the sales and use tax exemption will benefit customers with reduced rates, will keep North Dakota's tax environment competitive with Montana and South Dakota, and will provide tax fairness.

Mr. Todd Simmons, General Manager, Wind Operations, ALLETE, Inc., provided comments (Appendix K) in support of the bill draft. He said continuing the sales and use tax exemption will provide tax parity for all types of electrical generation facilities.

Ms. Elise Magnus, Commissioner, Cavalier County, said the Cavalier County Commission expressed support for the bill draft. She said wind turbine projects in the county have provided an economic benefit to the residents and have provided revenue to the county through property taxes.

It was moved by Representative Brandenburg, seconded by Representative Mock, and carried on a roll call vote that the bill draft relating to a sales and use tax exemption for wind turbines be approved and recommended to the Legislative Management. Senators Wardner, Bekkedahl, Bowman, and Murphy and Representatives Brandenburg, Damschen, Hanson, Mock, and Porter voted "aye." Senator Armstrong voted "nay."

RETAIL ELECTRICITY SALES REPORT

Ms. Julie Fedorchak, Commissioner, Public Service Commission, presented information (Appendix L) regarding a report on retail electricity sales meeting or exceeding the state renewable and recycled energy objective pursuant to Section 5 of 2015 Senate Bill No. 2037 and an overview of wind turbine bonding and reclamation policies. She said 15.45 percent of retail electricity sales in North Dakota were from renewable energy in 2015 compared to a goal of 10 percent. She said 6.5 million megawatt hours of electricity was produced from renewable energy in 2015 of which 2.6 million megawatt hours were utilized in North Dakota and 3.9 million megawatt hours were exported to other states. She said wind turbine operators are required to submit wind turbine decommissioning plans 10 years after completion of the turbine. She said the operators' plans must identify sufficient financial resources to decommission the wind turbines.

In response to a question from Chairman Wardner, Ms. Fedorchak said based on current estimates, the salvage value of wind turbine materials may be sufficient to cover the cost of decommissioning the wind turbines.

BILL DRAFT RELATED TO COAL CONVERSION TAX REVENUE ALLOCATIONS

The Legislative Council staff reviewed a bill draft [17.0271.01000] relating to the allocation of coal conversion tax revenue. The bill draft removes an expiration date which will allow the continuation of the 5 percent allocation of the general fund share of coal conversion tax revenue collections to the lignite research fund. The removal of the expiration date is estimated to decrease general fund revenues by $1 million in the second year of the 2017-19 biennium and by $2 million in each biennium thereafter.

Mr. Tyler Hamman, Director of Government Affairs, Lignite Energy Council, said the Lignite Energy Council supports the bill draft. He said continuing the funding for lignite research is an important part of helping the state to reduce carbon dioxide emissions from coal-powered electrical generation facilities.

It was moved by Representative Hanson, seconded by Senator Armstrong, and carried on a roll call vote that the bill draft relating to the allocation of coal conversion tax revenue be approved and recommended to the Legislative Management. Senators Wardner, Armstrong, Bekkedahl, Bowman, and Murphy and Representatives Brandenburg, Damschen, Hanson, Mock, and Porter voted "aye." No negative votes were cast.

STUDY OF ENVIRONMENTAL PROTECTION AGENCY REGULATIONS

Mr. David Glatt, Chief, Environmental Health Section, State Department of Health, presented information regarding an update on the federal Environmental Protection Agency (EPA) regulations of power plant carbon dioxide emissions related to the committee's assigned study. He said the regulations are intended to increase the efficiency of existing power plants, to increase the use of natural gas for generating electricity, and to increase the use of renewable resources for generating electricity. He said the regulations provide for a 30 percent reduction in carbon dioxide emissions by 2030 for the nation. He said North Dakota's reduction ranges from 37 percent under mass-based compliance to 45 percent under rate-based compliance. He said North Dakota's reduction in carbon dioxide emissions under the initially proposed regulations was 10.6 percent. He said 18 states support the regulations while 28 states oppose the regulations. He said North Dakota has joined other states in a lawsuit to oppose the EPA's regulations. He said the regulations are not currently in effect because a stay was granted during the litigation process. He said concerns about the regulations include the cost of purchasing credits, the early retirement of existing coal-powered facilities, and potential rate increases for customers. He said reductions in carbon dioxide are anticipated even if the EPA regulations are overturned because companies are facing pressure from public opinion to reduce emissions.

In response to a question from Representative Porter, Mr. Glatt said the carbon dioxide emissions are based on the location of the facility, but the credit for using renewable resources may be based on the location of the end users.

STUDY OF OIL AND GAS TAX ALLOCATION FORMULAS

Chairman Wardner presented information (Appendix M) regarding the oil and gas tax allocation formulas. He said he prepared a forecast for the 2017-19 biennium oil and gas tax allocations based on an average oil price of $45 per barrel and average daily production of 900,000 barrels per day. He said the Office of Management and Budget's forecast for the 2017-19 biennium, which was released in August 2016, was based on an average oil price of $52 per barrel in the first year of the biennium and $58 per barrel in the second year of the biennium. He said one of the concerns for the 2017-19 biennium is providing an adequate level of funding for political subdivisions while also providing an adequate level of funding for state programs. He said the estimated allocations to hub cities in his forecast are based on mining employment. He said based on data for calendar year 2015, the hub cities in the 2017-19 biennium are anticipated to be Williston, Dickinson, Minot, and Mandan. He said the estimated allocations to counties and state funds in his forecast are based on the allocation formulas under current law.

Chairman Wardner said even though the committee did not consider a bill draft related to changes for the oil and gas tax allocation formulas, individual legislators will likely introduce bills during the 2017 legislative session. He said a possible change to the formulas relates to the county allocations. He said the allocation formulas for counties under current law are based on the amount of oil and gas tax revenue that was allocated to the counties in fiscal year 2014 which may not accurately reflect the allocations that counties are currently receiving. He said the base year for the allocation formulas could be changed from fiscal year 2014 to 2016. He said changing the year could result in funding concerns for certain school districts which could be addressed through additional formula changes.

The Legislative Council staff presented a memorandum entitled *Oil and Gas Tax Allocation Formulas - Potential Change to Supplemental School District Allocation*. The memorandum provides information on oil and gas gross production tax allocations to counties for fiscal years 2014 and 2016, an example of the potential changes that could be made to the supplemental school district allocation, and the estimated fiscal impact of the potential changes. He said if the supplemental school district allocation is based on the counties' allocations in fiscal year 2016, the school districts in Bottineau County would no longer be eligible for the allocation while the school districts in Dunn County would become eligible. He said the example of potential changes addresses concerns related to the possible funding reduction for the school districts in Bottineau County and the possible funding increase for the school districts in Dunn County.

Senator Bekkedahl suggested the oil and gas tax allocation formulas relating to the state's share could be simplified to provide $300 million to the general fund, $300 million to the tax relief fund, up to $22 million to the state disaster relief fund, and all remaining revenue to the strategic investment and improvements fund.

OTHER

It was moved by Senator Murphy, seconded by Representative Mock, and carried on a voice vote that the Chairman and the Legislative Council staff be requested to prepare a report and the bill drafts recommended by the committee and to present the report and recommended bill drafts to the Legislative Management.

Chairman Wardner recessed the meeting at 2:50 p.m. and reconvened the meeting on Tuesday, October 11, 2016, at 7:40 a.m. He said the committee will attend an energy conference to receive information about updates in the energy industry.

Chairman Wardner recessed the meeting at 7:45 a.m. for attendance at the 2016 Great Plains and EmPower ND Energy Conference.

Chairman Wardner reconvened the meeting at 3:25 p.m. He said the committee will not be meeting again this interim. He acknowledged Senator Warner who will not be returning as a member of the 65th Legislative Assembly and thanked him for his past service to the citizens of North Dakota. He thanked the committee members for their work.

No further business appearing, Chairman Wardner adjourned the committee sine die at 3:30 p.m.

Adam Mathiak
Fiscal Analyst

ATTACH:13