

NORTH DAKOTA LEGISLATIVE MANAGEMENT

Minutes of the

TAXATION COMMITTEE

Tuesday, July 22, 1997
Roughrider Room, State Capitol
Bismarck, North Dakota

Representative Wesley R. Belter, Chairman, called the meeting to order at 9:00 a.m.

Members present: Representatives Wesley R. Belter, Grant C. Brown, Chris Christopherson, Mick Grosz, Ralph L. Kilzer, Kenneth Kroepflin, Ronald Nichols, Dennis J. Renner, Earl Rennerfeldt, Arlo E. Schmidt; Senators Randel Christmann, Ed Kringstad, Randy A. Schobinger, Vern Thompson, Herb Urlacher

Members absent: Representatives William E. Gorder, Edward H. Lloyd, Alice Olson, Ben Tollefson; Senators Layton Freborg, Meyer Kinnoin

Others present: See attached appendix

Chairman Belter called on committee counsel for review of Legislative Council rules of operation and procedure relating to interim committees.

Chairman Belter welcomed committee members and reviewed his expectations for activities of the committee.

Chairman Belter called on Tax Commissioner Rick Clayburgh. The Tax Commissioner said he or members of his staff will attend all meetings of the interim Taxation Committee and provide information to the committee as requested.

PROPERTY TAX RELIEF STUDY

Chairman Belter called on committee counsel to present a memorandum entitled [Property Tax Relief through Alternative Sources - Background Memorandum](#). Committee counsel said property tax liability is determined using the mill rates of taxing districts in which the property is located applied to the taxable value of the property. He described how mill rates are determined, and he described levy limitations that apply to political subdivisions. He also discussed how taxable valuation of property is determined.

Committee counsel described a study conducted during the 1993-94 interim by a consultant under contract with the Legislative Council. He said the study focused on comparison of tax burdens among the property, sales, and income taxes within the state and with five other states in the region. He said the study focused on the period from 1960 to 1992 and that 1992 data was the most recent available at that time. He said the consultant converted all dollar amounts in the study period to 1994 dollars using consumer price index computations. He reviewed the conclusions of the study and copies of the study report were distributed to committee members. He said if the committee wishes to update the information in the study that relates to this

study resolution, it would be necessary to obtain the services of the consultant who did the study because of the conversion of dollar amounts by the consultant and the need to make the same conversion on more recent data to make comparisons on the same basis.

Committee counsel said other avenues for gathering of information for the study would include review of allocations of funds from the state to school districts and other political subdivisions in recent years and testimony could be sought from representatives of taxpayer groups and political subdivisions to suggest potential alternative revenue sources that might be used to reduce property tax burdens.

Representative Schmidt said he introduced the study resolution because of concerns expressed to him about property tax valuation and liability increases. He said many farmers in his area are concerned about valuation and liability increases and have investigated to determine the cause. He said it was discovered that much of the valuation increase is attributable to the capitalization rate used in the agricultural property valuation formula. He said he hopes the study will reveal a solution to the problems of recent sharp increases in agricultural property valuation.

Senator Thompson said he is sympathetic with the goals of the sponsor of the study resolution and many farmers in his area have lost property, due in part to property tax burdens. He said it is also important to remember that the Legislative Assembly must be sensitive to the effects of property tax relief on political subdivisions. He said political subdivision revenue sources are limited and political subdivisions must be given the ability to provide needed services for citizens.

Representative Brown said information should be obtained concerning the willingness to update that study and anticipated cost from the consultants at the North Dakota State University Department of Agricultural Economics who completed the 1993-94 study. He said this would be important information to develop and the information should be obtained if the committee decides to request funding approval from the chairman of the Legislative Council.

Senator Urlacher said it would be useful for committee members to obtain information on who bears the burden of property taxes. He said information on the impact of various taxes at different income levels would give the committee good background information on who is most seriously impacted in the existing tax structure.

Representative Brown said it would also be important to examine available information on which taxes are most regressive.

Senator Urlacher said it would be useful to have a presentation to the committee by representatives from the Department of Agricultural Economics at North Dakota State University on how the agricultural property valuation formula calculations are made.

Representative Schmidt said another difficulty that has arisen in his area is that assessors and local officials are reluctant to abate taxes on flooded lands because a large portion of the tax base is being lost to rising water. He asked for a review on assessment procedures in the case of flooded property.

TAX-EXEMPT PROPERTY IMPACT ON SCHOOL DISTRICTS

Chairman Belter called on committee counsel for presentation of a memorandum entitled [Tax-Exempt Property Impact on School Districts - Background Memorandum](#). Committee counsel said the existence of tax-exempt property within a school district affects the school district in two ways--by limiting the amount of property tax revenue the school district levy will generate (in some cases) and by excluding the value of that property from the equalization factor in the foundation aid allocation formula.

Committee counsel said the Fargo School District has unlimited levying authority under North Dakota Century Code (NDCC) Chapter 15-51. He said Section 57-15-14 allows school districts with a population of more than 4,000 to be granted unlimited levying authority upon approval by a majority vote of electors and a school district with fewer than 4,000 population may be granted authority to levy any specific number of mills approved by a vote of 55 percent or more of electors. He said school districts that do not have unlimited levying authority or authority to levy an excess levy are subject to a general fund levy limitation of 185 mills on the dollar of taxable valuation of property in the district. He said a school district subject to this limitation may increase its levy by up to 18 percent in dollars from the prior school year, up to the 185-mill limitation.

Committee counsel said school districts at or near the general fund levy limitation have been eligible for optional percentage levy increases in dollars since 1981. He said taxing districts that have been using percentage increase authority may be levying at a rate well in excess of the 185-mill limitation. He said 1997 legislation allows a school district eligible for federal funds on a matching basis as a result of a disaster declared by the President of the United States to levy an amount required to match federal funds, up to an increase of two percent more than the amount levied by the district in the base year, but other school districts under optional levy authority may levy only up to the amount levied in the base year. He said the significance of the limitation based on mills or based on dollars levied is that a limitation based on dollars levied

is unaffected by increases or decreases in taxable valuation of property within the district, except for adjustments made to reflect property added or removed from the tax rolls. He said a district levying on a mill limitation is subject to fluctuations in tax dollars raised as taxable valuation of property in the district changes.

Committee counsel described provisions relating to approval of excess levies under NDCC Chapter 57-16 and school district levies for various special fund purposes.

Committee counsel said the foundation aid allocation formula contains an equalization factor that is applied after determination of payments due to the district for tuition apportionment, per student aid, special education aid, and transportation aid. He said the factor operates by multiplying 32 mills times the latest available net assessed and equalized valuation of property in the school district and the resulting amount is subtracted from the payment to the school district. He said for school years after 1996-97, the number of mills in the equalization factor is adjusted by a growth factor.

Committee counsel said that because the equalization factor is multiplied times valuation of property in the school district, the more taxable property that exists in the district the greater the amount deducted from foundation aid payments to the district. He said property that is not on the tax rolls generates no revenue for a school district, unless payments in lieu of taxes are received for the property, and the property will not decrease foundation aid to the district. He said tax-exempt property is not equalized in the foundation aid formula.

Committee counsel reviewed property tax exemptions for various kinds of property that are exempt under the Constitution of North Dakota or statutory law and provisions governing payments in lieu of taxes on certain types of property. He said property on which payments in lieu of taxes are made may generate revenue for school districts and this revenue is not equalized because it is not recognized in the equalization factor in the foundation aid allocation formula. He said 1997 House Bill No. 1068 restructured taxation of the telecommunications industry and provides that telecommunications service providers will pay gross receipts taxes in lieu of property taxes and that the revenues will be allocated among political subdivisions in approximately the same manner as under previous law. He said these revenues are not equalized in the foundation aid formula and may cause differences in funds available to school districts.

Committee counsel said state law has required establishing valuations for exempt property for many years. He said assessment officials have not complied with the law in many cases. He said 1995 Senate Bill No. 2081 required assessment officials to establish assessed valuations for all tax-exempt property by 1998. He said assessment officials expressed concern about this requirement because valuing all exempt property is viewed as a waste of time and resources in some cases. He said 1997 legislation changed the

requirement and will require assessed valuations to be established for property exempt as a new or expanding business, improvements to property, buildings belonging to institutions of public charity, new single-family residential or townhouse or condominium property, early childhood services property, or pollution abatement improvements. He said information should become available during this interim on these assessments. He said some assessment officials have completed assessment of exempt property and a report was presented to the 1995-96 interim Taxation Committee by Mr. Ben Hushka, Fargo City Assessor, on exempt valuations in the city of Fargo.

Chairman Belter called on Mr. Richard Ott, North Dakota School Boards Association, for comments on the tax-exempt property impact on school districts study. Mr. Ott said the School Boards Association had legislation introduced in 1997 that would have allowed school districts to opt out of property tax exemptions granted by cities or counties affecting property within the school district. He said the bill failed but the association still supports this change. He said information should be obtained to evaluate how successful property tax exemptions have been in establishing new businesses. He said another concern of the association is that loss of revenue under the foundation aid allocation formula combined with the levy limitation that applies to school districts gives the school district no alternative to make up loss of revenues through property tax levies. He said the association will be pleased to provide information to the committee during the interim as requested.

Representative Brown asked whether the School Boards Association could develop information to show the total effect of property tax exemptions on school districts when those exemptions have been granted by cities or counties. Mr. Ott said information is not readily available but probably can be developed by the association.

Representative Belter asked Mr. Barry Hasti, State Supervisor of Assessments, what information is available on tax exemptions that have been granted by political subdivisions and the effect on school districts. Mr. Hasti said information is available on optional property tax exemptions but the data will not show impact on school districts.

In response to a question from Representative Belter, Mr. Hasti said the Tax Department will begin to receive information on valuations of exempt property beginning in June 1998 under the 1997 amended requirements for assessment of certain exempt property.

Senator Urlacher asked whether cities have information available on valuation of exempt property. Ms. Bev Neilson, North Dakota School Boards Association representative, Fargo, said information prepared by the city of Fargo assessment department showed that in 1995 Fargo had over \$96 million in valuation of exempt property. She said over \$41 million of that amount was in new residential property. She said this represents approximately 20 percent of the

value of all property in Fargo, but she is not certain whether it includes the value of state property such as the land and buildings at North Dakota State University.

Representative Grosz asked why school districts are unable to get city or county officials to understand the importance to school districts of decisions on granting property tax exemptions. Ms. Neilson said the school board in Fargo has a good relationship with the city of Fargo but in other areas of the state it appears problems exist in getting city and county officials to consider impacts of these decisions on school districts. Representative Grosz asked whether school districts would like to have veto authority over at least the portion of property tax levied by schools on property being considered for optional exemptions. Ms. Neilson said school districts would like to retain their taxing authority on those exempted properties.

Senator Urlacher said the League of Cities and the Association of Counties should be requested to provide assistance on gathering information on valuations of exempt property. Chairman Belter requested committee counsel to seek that assistance.

Representative Kilzer said he has concerns with property tax exemptions as applied to hospitals and clinics. He said it seems there is unfairness in a situation of which he is aware a clinic within a hospital is exempt from property taxes while privately operated clinics are subject to property taxes. He said another area of concern is that much of the activity occurring in modern hospitals competes directly with services of private enterprise. He said he thinks there are several areas that require consideration regarding application of property tax exemptions for hospitals.

Senator Christmann said the concern of schools on having a vote or veto authority in property tax exemption decisions should be tempered by considerations on school bonding or building plans, which affect other political subdivisions, and perhaps other political subdivisions should have voting rights in deliberations of school districts.

FARM BUILDINGS EXEMPTION STUDY

Chairman Belter called on committee counsel for presentation of a background memorandum on a study assigned by the chairman of the Legislative Council regarding application of the property tax exemption for farm buildings.

Committee counsel presented the memorandum entitled [*Farm Buildings Exemption Study - Background Memorandum*](#). He said the property tax exemption has separate application for farm residences and farm buildings other than residences. He said the provision relating to farm residences is much more detailed and provides criteria to determine what is a farm and who is a farmer and imposes income limitations on persons who qualify for the residence exemption. He said the exemption for farm buildings other than residences is limited only in that it does not apply to a structure or improvement used in connection with a retail or wholesale business other than farming, a structure on

platted land within the corporate limits of a city, or a structure located on railroad operating property.

Committee counsel said a 1977 North Dakota Supreme Court decision in *Butts Feed Lots v. Board of County Commissioners* concluded that a feedlot was an industrial activity and the buildings did not qualify for the farm buildings exemption. He said the Supreme Court found that contract feeding of cattle not owned by the owner of the facility is an industrial activity and raising cattle owned by the owner of the facility is an industrial activity if the feed for the cattle is not grown onsite. He said the Supreme Court also said an operation may be industrial if replacement animals are not raised onsite. He said the Tax Commissioner has adopted guidelines pursuant to the *Butts* decision providing that animals' feed must be primarily grown by the person raising the animals and the enterprise must be operated in connection with or incidental to an ordinary farming operation.

Committee counsel said this study directive is a continuation of a study conducted during the 1995-96 interim. He said the 1995-96 study arose because of events that transpired in Richland County. He said a large turkey-raising operation was established in Richland County in 1995. He said the operator constructed 35 large turkey barns on the property and Richland County officials assumed that the property would not qualify for the farm buildings exemption under the *Butts* analysis. During consideration of the issue, Richland County officials recognized that several existing operations that raise turkeys, cattle, or hogs would also become taxable under the guidelines adopted to implement the *Butts* decision.

He said the 1995-96 interim committee toured Richland County turkey-raising operations and talked to turkey growers and Richland County officials. He said information presented to the committee indicates that there is dissatisfaction with the requirement that feed for animals must be grown onsite. He said many operators believe it is a better management decision to purchase feed for animals. Committee counsel said the 1995-96 interim committee discussed several factors that might be used to distinguish between industrial or commercial operators and agricultural operators. He said none of the factors provided a solution to the application problems without creating difficulties.

Chairman Belter said this study assignment arose because recent events in Cass County indicated a need for an improvement in application of the exemption. He said a long-time hog operation has been sold to a former employee who has no property on which to raise feed for the animals so the operation would become an industrial operation subject to property taxes under the *Butts* decision. He said another Cass County operation is being converted to a custom feed operation and it is being debated whether that property will be subject to taxes. He said it is apparent this problem will continue to occur and a legislative solution should be determined. He said he does not believe it is fair that special rules should apply

to livestock producers and that all agricultural operators should be equally treated.

Senator Christmann asked for information on activity in Richland County since the conclusion of the 1995-96 study. Chairman Belter asked committee counsel to get an update for the committee.

Chairman Belter called on Mr. Donald Siebert, Ward County Director of Tax Equalization, for comments on the farm buildings exemption. Mr. Siebert said application of the exemption for farm residences and buildings always presents problems for assessment officials. He said one situation that is of particular concern is that young farmers are unfairly treated. He said a farmer in the first year of operation is not eligible for the farm buildings and residence exemption because the statutory provision requires a farmer to be a person who earned more than half of the family income from farming in the previous year. He suggested that the committee recommend an amendment to the law so that a first-year farmer could qualify for the exemption. He said the goal of the provision should be to encourage young farmers to begin farming and not to penalize them because they are new to farming.

In response to a question from Representative Belter, Mr. Siebert said there are no livestock feeding operations in Ward County now and the last one folded five years ago but was subject to assessment and taxation on farm buildings.

Chairman Belter called on Mr. Wade Moser, Executive Director, North Dakota Stockmen's Association, for comments on the study of the farm buildings exemption. Mr. Moser said the association is concerned about several aspects of application of the exemption. He said consideration must be given to treatment of cooperatives. He said another area of concern is in contract feeding and the point at which an operator would lose the exemption in contract feeding operations. He said dairy operators are another area of concern because dairy cattle require high-quality feed that must be purchased and this may disqualify all dairy operations from the exemption. He said share cattle agreements may be considered an industrial activity at some point. Mr. Moser said perhaps a different approach is needed and it might be necessary to look at issues of adding value through processing versus adding value through feeding as differentiating factors for raising of livestock and poultry.

Representative Belter asked Mr. Terry Traynor, North Dakota Association of Counties, whether many county governing bodies are struggling with the issue of farm building exemptions. Mr. Traynor said all county commissioners are aware that feeding operations are in a gray area under the statutory provision and court decision. He said evolution of agricultural industry practices may be responsible for placing many operators in possible conflict with the law.

Senator Urlacher said he believes a change in the law is necessary because for many operators it is not practical to process their own feed and it is not fair to base exemption decisions on that factor.

Representative Belter asked Mr. Moser whether he would be willing to try to reach a consensus recommendation among agricultural groups on how the exemption should be modified. Mr. Moser said the Ag Coalition is meeting soon and he will raise this topic for discussion.

LIGNITE INDUSTRY TAXATION AND REGULATORY ENVIRONMENT

Chairman Belter called on committee counsel for presentation of a memorandum entitled [Taxation and Regulatory Environment for North Dakota's Lignite Industry](#). Committee counsel said supporters of the study resolution and the text of the resolution stated that taxation and regulatory compliance costs constitute up to 30 percent of production costs for North Dakota lignite and that reducing these costs could improve the competitive position of the lignite industry.

Committee counsel said the coal severance tax and privilege tax on coal conversion facilities were enacted in 1975. He said the coal severance tax rate was initially set at 50 cents per ton with an escalator clause. He said legislation and action of the escalator clause increased the coal severance tax rate to a high of \$1.04 per ton. He said 1987 legislation reduced the general coal severance tax rate to 75 cents per ton, eliminated the escalator provision, and imposed an additional separate tax of two cents per ton, with proceeds of the separate tax allocated to the lignite research fund. He said the rate of severance tax has been unchanged since 1987. He said the 1987 legislation was the result of an interim study in which the committee used the services of a consultant to analyze the competitive position of the lignite industry.

Committee counsel described allocation of revenue from coal severance taxes and said coal severance tax revenues for the 1997-99 biennium are estimated to be \$45.8 million. He said the state general fund would receive \$22.3 million of this amount, political subdivisions would receive \$15.6 million, and the coal development trust fund would receive \$6.7 million. He said the remaining \$1.2 million would go to the lignite research fund.

Committee counsel said the privilege tax on coal conversion facilities was set at an initial rate of one-fourth of one mill per kilowatt hour of electricity produced and an alternative tax was established for coal gasification facilities at the greater of 2.5 percent of gross receipts or 10 cents per 1,000 cubic feet of synthetic natural gas. He said in 1983 an additional one-fourth of one mill per kilowatt hour was imposed for electrical generating plants. He described changes to the coal conversion tax and allocation of tax revenues and said estimated revenues for the 1997-99 biennium are estimated to be about \$30.8 million. He said political subdivisions are expected to receive \$6.1 million and the state general fund is expected to receive about \$24.7 million.

Committee counsel said NDCC Section 54-17.5-02 requires the Industrial Commission to consult with the

Lignite Research Council regarding administration of the lignite research fund. He said applications are made for funding from the lignite research fund and priority is to be given to projects, processes, or activities that will preserve existing jobs and production, create the greatest number of new jobs and additional production, attract matching investment, and result in development and demonstration of a marketable product with a high level of probability of rapid commercialization. He said priorities are also established for applications for funding for marketing and reclamation research.

Committee counsel said for the 1997-99 biennium estimated receipts are approximately \$6.2 million and the beginning balance is approximately \$7.9 million. He said estimated expenditures from the lignite research fund for the biennium are about \$13.4 million, including about \$400,000 for a lignite marketing feasibility study and \$13 million for administration and development of the lignite research, development, and marketing program. He said the Industrial Commission has authorized investment of \$4.2 million from the fund in the lignite to anhydrous ammonia project of the Dakota Gasification Company. In addition, he said, the Industrial Commission has approved issuance of tax-exempt bonds to provide \$8.1 million to the Dakota Gasification Company.

Committee counsel described regulatory aspects of state law relating to the coal industry. He said the Industrial Commission has jurisdiction over exploration for coal and the Public Service Commission has jurisdiction over surface mining and reclamation operations. He said NDCC Chapter 38-18 provides surface owner protection from undesirable effects of development of minerals underlying the surface of their property. He said the Public Service Commission may not issue a surface mining permit unless the application is accompanied by statements of consent executed by each surface owner whose land is included within the permit area.

Committee counsel said it is also important to recognize that many provisions of the North Dakota Administrative Code relate to regulation of the lignite industry. He said more than 300 sections of the Administrative Code have been adopted by the Industrial Commission and Public Service Commission regarding coal exploration and surface mining and reclamation. He said administrative rules of the State Department of Health and the State Tax Commissioner also affect coal mining operators. He said 1997 House Bill No. 1410 prohibits State Department of Health rules on air quality affecting coal conversion facilities more strict than federal rules under the Clean Air Act and 1997 Senate Bill No. 2356 prohibits the State Department of Health from adopting administrative rules on sulfur dioxide air quality which are more strict than federal rules under the Clean Air Act.

Chairman Belter called on Mr. John Dwyer, President, North Dakota Lignite Council, for comments on the study. Mr. Dwyer said it is appropriate that the Legislative Council consider taxation and regulatory

impacts on the coal industry because the Legislative Assembly has not looked carefully at the taxation and regulatory environment for the North Dakota lignite industry since the 1985-86 study.

Mr. Dwyer said the lignite industry is extremely competitive and success in the industry may be a matter of very small cost considerations. He said the North Dakota lignite industry competes with Canadian hydropower, subbituminous coal production from Montana and Wyoming, and other electricity producers from other fuel sources within the midwest area power pool (MAPP). He said test burns have been conducted at the Stanton and Leland Olds stations this year to determine the feasibility of using subbituminous coal from out-of-state sources. He said the loss of the contract for supplying coal to the Big Stone Station has also impacted the North Dakota lignite industry.

Mr. Dwyer said power is sold in the midwest area power pool on a one-half of one mill margin so tax and regulatory costs are critical to whether sales are made by producers. He said the regulatory concerns of the industry involve the requirement of about 40 separate permits that are required for the lignite industry in various levels of exploration and production.

Mr. Dwyer said production expenses of the lignite industry have increased. He said rankings of North Dakota lignite plants against other plants in competitiveness have fallen from 1993-95. He said this is a matter of great concern to the North Dakota lignite industry and the industry hopes the committee will determine ways in which tax and regulatory costs of the industry can be reduced.

In response to a question from Representative Brown concerning the greatest factor in the reduction of rankings for North Dakota generating facilities, Mr. Dwyer said Montana and Wyoming have excess coal production capacity and have lowered prices. He said this affects the environment in which North Dakota lignite generators operate.

Senator Christmann asked how the industry will be impacted by new federal regulations on air quality. Mr. Dwyer said the industry does not anticipate significant impact and has consulted with the State Department of Health on this topic. He said he believes the industry is in compliance already because the industry has state of the art equipment for pollution control.

Representative Nichols asked for information on the externalities tax lawsuit. Mr. Dwyer said the situation arose because Minnesota had proposed imposition of a heavy tax on power from lignite because of emissions. He said the Minnesota Public Utilities Commission hearing involved over 40 parties and the North Dakota lignite industry position has prevailed to this point in the administrative proceeding. He said he expects the litigation may last two to three years. He said the result of this proceeding is significant to the industry because this additional cost for North Dakota lignite would seriously impair the ability to compete for sales in Minnesota.

Chairman Belter asked Mr. Dwyer to describe the results of the test burn of subbituminous coal. Mr. Dwyer said unfortunately the test burn indicated that subbituminous coal burns very efficiently and the price is very competitive for use in North Dakota power plants. He said the only advantage for lignite is the absence of railroad shipping costs. He said the Lignite Council would be happy to share the results of the test burns with the committee.

Senator Urlacher asked what has occurred at the Big Stone Station with the loss of production from the Gascoyne Mine and the change to use of Montana coal. Mr. Dwyer said the change has been good for the Big Stone Station and bad for the North Dakota lignite industry. He said rail costs were the determining factor in the change. He said shipping costs are now prohibitive for lignite and we will not see rail transportation of North Dakota lignite. Shipping subbituminous coal from Montana or Wyoming is economically feasible in the current competitive environment.

Representative Brown asked why Wyoming and Montana do not have more generating stations since they have substantial coal production. Mr. Dwyer said North Dakota is a better location for generating stations because there is an adequate supply of water from the Missouri River and electric lines to transport electricity from the facilities is a consideration that weighs in North Dakota's favor. He said there is a line loss of electricity in transporting power by wire and North Dakota is closer to markets to the east.

Chairman Belter called on former Governor Arthur Link for comments on the study of the lignite industry. Former Governor Link said the coal severance and conversion taxes were enacted during his term as Governor and were the subject of great debate and deliberation. He said an interesting point raised during consideration of coal taxation issues is that the Minnesota sales tax on the consumer end of the stream of electricity is greater than all combined coal taxes imposed in North Dakota on production. He said he believes the area that requires research is the conversion of lignite to a higher grade of coal before putting it into the coal conversion facility process. He said he thinks converting lignite to a higher grade fuel would be the most important development to secure the future of the lignite industry. He said committee members should be cognizant in deliberations of the impact on North Dakota taxpayers of reducing taxes on the coal industry because the lost revenue to the state and political subdivisions must be made up by other taxpayers.

Chairman Belter said updating the study conducted during the 1985-86 interim has been investigated. He reviewed a letter from Dr. David Ramsett, University of North Dakota, who conducted the 1985-86 study. In the letter, Dr. Ramsett said updating of the study should include, at a minimum, analyzing trends in capacity utilization of regional power producing facilities, trends in lignite and subbituminous coal production, trends in MAPP sales by regional power producers, assessment

of competition between subbituminous and lignite coal, trends in public utility regulation, and state severance tax updates for North Dakota, Wyoming, and Montana. Dr. Ramsett indicated the likely cost of the study would be \$8,000 to \$10,000, not including publication costs.

Representative Brown asked whether the Lignite Council can provide an update on the status of research on improving the grade of lignite. Mr. Dwyer said that is a high priority of research, and he described activities in the area and said further information could be provided.

Senator Urlacher said he would favor completing an update of the earlier coal industry taxation study.

Senator Christmann asked Mr. Dwyer whether the Lignite Council has the data to complete the study. Mr. Dwyer said the Lignite Council has the necessary information but he believes it is important for the committee to obtain independent analysis of the information.

Representative Nichols asked for an update on the anhydrous ammonia production project at the Dakota gasification facility. Mr. Dwyer said the ammonia production plant is now at 65 percent capacity and it will work. He said the goal of the project and other similar research is to generate revenue from byproducts instead of synthetic natural gas because the cost to produce synthetic natural gas makes the product noncompetitive with natural gas. He said the lignite industry is very encouraged by the anhydrous ammonia project results.

Chairman Belter requested committee counsel to obtain information for the next committee meeting on having Dr. Ramsett update the most recent study of taxation of the coal industry and to investigate the possibilities of sharing funding for the study with the lignite research fund.

CHARITABLE ORGANIZATIONS PROPERTY TAX EXEMPTION

Chairman Belter called on committee counsel for presentation of a memorandum entitled [Charitable Organizations' Property Tax Exemption - Background Memorandum](#). Committee counsel said the text of the study resolution states that the nature and activities of charities and the amount of property owned by charities have changed substantially over the years, acquisition of property by charities shifts additional tax burdens to other taxpayers, consideration should be given to what is a charity, consideration should be given to full or partial assessment of property taxes for the value of services provided to charities, and legislation considered in 1997 called these issues into consideration.

Committee counsel said the Constitution of North Dakota provides in Article X, Section 5, that ". . . property used exclusively for schools, religious, cemetery, charitable or other public purposes shall be exempt from taxation." He said the constitution does not define what is a charitable purpose. He said the constitutional provision has been implemented by

NDCC Section 57-02-08(8) which provides an exemption for buildings belonging to institutions of public charity, including public hospitals and nursing homes, used wholly or in part for public charity, together with the land actually occupied by such institutions not leased or otherwise used with a view to profit. He said concern was expressed by some during the 1997 legislative session that this study resolution would include property of religious organizations. He said the sponsor of the resolution testified that the study is not intended to affect any exemptions for religious organizations and is intended to review only the application of the exemption for institutions of public charity.

Committee counsel said most property tax exemptions provided by the Legislative Assembly do not apply to land because the constitution allows the Legislative Assembly authority to exempt only personal property, which is defined by the constitution to include buildings. He said the Legislative Assembly has consistently exempted both buildings and land owned by charitable organizations because the constitutional provision provides that all property owned by those organizations is exempt. He said the significance of this is that for many exemptions when property is acquired and a building constructed by an exempt entity, the land remains on the tax rolls, but when a charitable organization acquires property the land is removed from the tax rolls which diminishes the tax base.

Committee counsel reviewed opinions of the Attorney General and letters of Tax Department legal counsel and court decisions interpreting the charitable property exemption. He said these interpretations require unity of ownership and use to qualify for the exemption. He said this means property must be owned by a charitable organization, the property's use must be devoted to charitable purposes, and it must be actually used in carrying out the charitable purposes of the organization claiming the exemption. He said interpretations indicate that if property is used partly for charitable purposes and partly for other uses, the dominant use determines whether the property is exempt and an assessment may be prorated if it can be shown that parts of the property are used exclusively for charitable purposes.

Committee counsel said interpretations indicate that when a charitable organization charges a fee and operates at a small net profit which is reinvested in the organization's charitable operations, the operation is "not with a view to profit" as used in the statute. Interpretations indicate that the meaning commonly given to the phrase "not used with a view to profit" is that no individual stockholder or investor will receive any kind of profit, gain, or dividend from operation of the charitable activity.

Committee counsel said interpretations indicate that the exemption for charitable organizations applies only to land actually occupied by the organizations. He said interpretations have been made that vacant lots owned by charitable organizations are not exempt because they are not actually occupied by the organization or by

a public hospital. He said in the case of farmland left to a charitable organization by inheritance, this interpretation means that property would be subject to taxes although it is owned by a charitable organization.

Committee counsel said an interpretation has been made that a charitable organization does not have to be incorporated to qualify for the exemption. He said this is an important consideration because there is often confusion about "501(c)(3)" organizations, which is a designation under the federal Internal Revenue Code and has nothing to do with the charitable organization property tax exemption.

Committee counsel said 1997 legislation amended requirements for assessment officials to value exempt property but it will still be required by NDCC Section 57-15-01.1 that valuations be established for property belonging to institutions of public charity. These valuations must be established for taxable year 1999. He said information should become available during this interim which could be reviewed by the committee with regard to valuations for exempt charitable organization property.

Chairman Belter called on Ms. Shelly Warner, President, North Dakota Long Term Care Association, for comments on the study of the charitable organization property tax exemption. Ms. Warner said the association wants to be involved in this study. She said members of the association operate 88 facilities in the state, only 10 percent of which are for profit. She said facilities that have gone into residential services and congregate living have generally paid property taxes on that portion of their facilities. She said this is not the case in Bismarck and the difference in assessment and taxation of residential and congregate living facilities may be a good discussion topic.

Ms. Warner said the association recognizes that its members benefit from services provided by political subdivisions. She said if consideration is given to partial taxation for charitable organizations, it must be remembered that rules on nonprofit organizations do not allow paying property taxes in some cases, such as Medicaid reimbursement rules that apply to nursing homes. She said it should also be remembered that if partial assessment of property taxes applies to nursing homes, Medicaid appropriations from the state would have to be increased to reflect any taxes paid. She said during the interim the association hopes to have providers come before the committee to discuss the situation in which they operate.

Representative Kilzer said he is interested in the issue of diversification and asked whether the motive of nursing homes becoming involved in residential and congregate living is for benevolent purposes or for profit

motives. Ms. Warner said nursing homes have generally become involved in these activities because there is a demand in the community for these kinds of services with no other provider. She said residential and congregate living arrangements are generally a less costly alternative to full nursing home care.

Chairman Belter asked for committee suggestions on information committee members would like on this study topic. Representative Brown said he would like to obtain input from charitable organizations and information from representatives of local governments on the amount of charitable organization property exempt from taxes. He said he would like to know whether local governments believe they should grant exemptions to charitable organizations rather than having them granted automatically by state law.

Representative Belter said information should be obtained from hospitals and other exempt organizations on values of property, operating revenues and expenses, and other topics. He said information should be obtained from local governments on the costs of services provided to exempt properties of charitable organizations.

Representative Brown said information should be requested from the Fargo city assessor and others, if available, on valuations of hospitals and other exempt charitable organization property.

Representative Brown said information should be obtained from the National Conference of State Legislatures or other source on how other states treat property of charitable organizations, specifically on treatment of hospitals.

Chairman Belter said he anticipates the next meeting of the committee will be held in September. He asked for suggestions from committee members on scheduling. Senator Christmann said the Five-State Legislative Conference will be held in Bismarck and will be attended by many committee members. He said it would be useful to schedule the meeting to coincide with the conference. The chairman said the next meeting would be tentatively scheduled for September 30 and could run over to the following day if necessary.

The meeting was adjourned by the chairman at 3:00 p.m.

John Walstad
Committee Counsel

ATTACH:1