

NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

TAXATION COMMITTEE

Thursday, September 3, 1998
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, William E. Gorder, Mick Grosz, Ralph L. Kilzer, Kenneth Kroeplin, Edward H. Lloyd, Ronald Nichols, Earl Rennerfeldt, Arlo E. Schmidt, Ben Tollefson; Senators Randel Christmann, Layton Freborg, Meyer Kinnoin, Ed Kringstad, Randy A. Schobinger, Vern Thompson, Herb Urlacher

Members absent: Representatives Alice Olson, Dennis J. Renner

Others present: See Appendix A

It was moved by Senator Kringstad, seconded by Senator Urlacher, and carried that the minutes of the July 7, 1998, meeting be approved as mailed.

COAL INDUSTRY STUDY

Chairman Belter called on Dr. David Ramsett, Director, Division of Economics and Public Affairs, University of North Dakota, for presentation of a report prepared by Dr. Ramsett, on a consultant basis, entitled *Competition in North Dakota's Coal-Electric Utility Industry: Lignite vs. Subbituminous Coal*.

Dr. Ramsett said before beginning coverage of the report he would review observations made in a 1986 report he prepared for the Legislative Council regarding the lignite industry. He said the 1986 study stated that shifts in the competitive positions of lignite coal and subbituminous coal were cause for concern for the future competitive status of lignite. He said the observation was made in the 1986 study that it would be possible market pressures that would make it feasible that decreases in freight rates and subbituminous coal costs would create an economic environment in which burning subbituminous coal in North Dakota power plants would be economically viable. He said this observation has proven to be a good description of what has occurred since 1986.

Dr. Ramsett said his current study and report reaches the following conclusions:

1. Coal is more important than ever to national energy production.
2. Open market competition is here at the wholesale level in electric energy production

and open market competition will soon become the norm at the retail level.

3. The driving force in the nation's coal industry is low sulfur western subbituminous coal produced in Wyoming and Montana.
4. Users of subbituminous coal have enjoyed continuous price reductions due to rising productivity in mining and transportation.
5. Electric power producers must choose the most cost-efficient energy source. Continuing price decreases in the delivered price of subbituminous coal to electric power plants in the region are threatening the economic viability of North Dakota's mine-mouth coal-electric power industry.
6. Coal taxation has become a bigger issue for the North Dakota coal-electric utility industry as the delivered price of subbituminous coal has dropped.
7. North Dakota must evaluate the economic effects of taxing lignite coal because of the economic impact and the state revenue impact of the coal-electric utility industry and the increasing potential that subbituminous coal could be burned in North Dakota power plants.

Dr. Ramsett said the role of coal in the national energy picture is significant because the nation routinely expects abundant and inexpensive electricity. He said coal provides twice as much electricity as any other single energy source. He said lignite production is currently responsible for about eight percent of total national coal production. He said the most significant change in national coal production is the dramatic growth in production of subbituminous coal.

Dr. Ramsett said significant changes are occurring in the national electric utility industry and industry competition. He said the industry is going from exclusive regional operation to open market sales. He said the industry was segregated and is going to a national sales market. He said the industry was regulated and is going to free market competition. He said the industry is in transition and the ultimate character of the industry cannot be determined but there will clearly be significant changes.

Dr. Ramsett said North Dakota's region of the country is a net exporter of electric power. He said

this means that states in this region are in competition with each other for markets. He said this makes it necessary to closely examine competitive factors in surrounding states to assess the continued economic viability of lignite coal. He said North Dakota is the only state in the region that uses lignite coal to produce electric power. He said coal-fired electric power production in North Dakota is at mine-mouth facilities. In contrast, all other states in the region use imported subbituminous coal to generate electric power production. He said the vast majority of this coal is shipped in by rail from Wyoming.

Dr. Ramsett said the best means of measuring competitiveness in the coal industry is comparing coal costs per megawatt hour (CCMH). He said this statistic is important to measure the portion of the variable cost of a megawatt hour of electricity that is attributable to the purchase of coal. He said this statistic accounts for several factors, including the price of coal delivered to the producing plant, the British thermal unit (Btu) rating of the coal, and the efficiency of the plant burning the coal.

Dr. Ramsett said comparing the CCMH for 1991 and 1996 shows a significant change in regional competitive considerations. He said the CCMH in North Dakota was \$8.29 in 1991 and \$8.32 in 1996. He said this does not indicate significant change in CCMH in North Dakota, but other regional states have experienced significant declines in CCMH because of importation of subbituminous coal, principally from Wyoming. He said the CCMH in Nebraska has decreased from \$8.72 in 1991 to \$7.88 in 1996. He said this significant decrease is a good indication of the significant impact of Wyoming coal in the regional market. He said examining CCMH data for November 1997 indicates continuation of the trend for other states. He said each state in the region has experienced a decrease in CCMH from 1991 to 1997 except North Dakota, which has experienced an increase of 5.7 percent. He said this compares with decreases of 34.9 percent for Nebraska, 33.1 percent for Missouri, 28.3 percent for South Dakota, and 19.5 percent in the national average CCMH.

Dr. Ramsett said comparison of North Dakota and Nebraska statistics indicates Nebraska experienced a 35.1 percent decline in coal costs from 1991 to 1997 while North Dakota experienced an increase of 7.6 percent in coal costs during the same time period. He said net electricity generated in Nebraska increased 26.9 percent in that time period versus an increase of 2.2 percent in North Dakota.

Dr. Ramsett said examining productivity statistics indicates lignite productivity has remained about even from 1992 to 1996. He said during that time period productivity for subbituminous coal has increased 49.1 percent, leading to a cost reduction of 21.3 percent. He said the increased productivity in subbituminous coal is attributable to thicker seams of coal, less overburden to remove and replace, larger

mines, and improved equipment for subbituminous mining operations.

Dr. Ramsett said another significant edge for subbituminous coal competitiveness has been deregulation of rail rates, which has substantially reduced shipping costs for coal. He said unit trains increase the number of tons that may be shipped. He said a greater density of track use has increased the shipping capacity for coal. He said improved rail technology has also played a significant role in increasing the ability to ship coal.

Dr. Ramsett said it appears the future will bring increased open market sales of electricity and strong regional competition in the marketplace. He said North Dakota cannot control prices in the open market for electricity, and it will be necessary for the electric power industry in North Dakota to control operating or input costs to remain competitive. He said approximately two-thirds of operating costs are coal costs. He said this raises the question of whether North Dakota power plants would be better off burning subbituminous coal rather than lignite coal. He said this decision involves several issues, including consideration of mine ownership and the relation of the mine to the generating plant it serves. He said adding new rail to stations serving power plants will also become a significant consideration. He said one issue that must be addressed is the uncertainty of future rail costs if the North Dakota electric utility industry becomes dependent on imported coal. He said another consideration is the issue of loyalty to the state and employees, and these considerations will be important to decisions about importing coal. He said the pure economics of CCMH provides a compelling case for North Dakota coal-fired power producers to substitute subbituminous coal for lignite coal in some, if not all, power plant production. He said the declining coal prices and transportation costs for subbituminous coal are making these issues that the electric utility industry and North Dakota political decisionmakers cannot ignore.

Dr. Ramsett said with regard to the issue of coal taxation, it is not his intention to tell the Legislative Assembly what it should do with regard to tax policy. He said his effort in the report is to provide information on which decisions can be based, including a valid means of comparison of coal taxes, which is only one component of coal costs. He said each state in the region imposes taxes on coal. He said the North Dakota coal severance tax is a specific tax of 77 cents per ton. He said Wyoming imposes two taxes based on the assessed valuation of coal, which generated a combined tax of 57 cents per ton in 1996. He said Montana taxation of coal is more complicated and consists of a coal severance tax of 15 percent of market value, a gross proceeds tax of five percent, and a resource indemnity tax of four-tenths of one percent of gross market value. He said comparison of Wyoming, Montana, and North Dakota coal tax rates indicates Wyoming has the lowest rate

of taxation and Montana the highest. He said North Dakota falls in the middle of the comparison by any method of comparison. He said the most valid comparison is the tax per million Btus which is calculated at 3.4 cents in Wyoming, 5.9 cents in North Dakota, and 7.6 cents in Montana.

Dr. Ramsett said coal taxation issues in North Dakota are somewhat different from those issues in Wyoming and Montana. He said in Wyoming and Montana the principal reason to produce coal is to export the coal to other states. He said in North Dakota the coal is not an exported product but is used to generate electric power for exportation. He said this characteristic of coal taxation in North Dakota was unimportant in the past due to the market for electricity, which allowed the tax to be passed forward to final consumers. He said this becomes less feasible as more electric power sales are made on the open market under pure competition. He said taxing severance of lignite is like taxing an input cost for other industries, somewhat similar to taxing fertilizer for farmers. He said consideration of three alternative scenarios for the future may give an impression of future changes. He said one scenario would be continuing use of lignite coal exclusively for electric generation. He said continuation of current trends would indicate a gradual loss of market share for the North Dakota electric utility industry, resulting in gradual reductions in activity for coal mines and decreases in income and sales tax revenues for the state. He said a second scenario involves beginning to substitute subbituminous coal for lignite coal. He said lignite production would decline, resulting in decreased income and employment. He said the state would lose coal tax revenue from reduced production of lignite and would lose income and sales tax revenue from reduced economic activity. He said the third scenario assumes North Dakota coal severance tax is eliminated and replaced with an equivalent tax on electric power production that is not sold on the open market. He said this approach would retain most revenues currently generated by coal taxes while allowing coal-electric utilities to compete more effectively for open market sales of electricity.

Dr. Ramsett said it is important to remember that North Dakota tax policy for the coal industry is not what has created the current economic problems faced by the industry. He said the price reductions in subbituminous coal and transportation costs have been so significant that they are responsible for the competitive prices faced by the industry. He said taxation policy becomes significant because close competitive pricing could depend on several variables, including a reduction in tax burdens to allow an improved competitive position.

Dr. Ramsett said there are areas in which more information is required. He said virtually no information is available regarding open market sales of electric power. He said very little information is available on rail shipping cost policies for coal. He said more

accurate information is required for comparison of coal costs for North Dakota versus other states. He said coal costs for North Dakota electric power plants are understated because of their mine-mouth nature and the absence of comparable transportation costs. He said additional information is needed regarding transmission line costs incurred by North Dakota electric power producers to allow accurate comparison of North Dakota costs to costs for other states.

Representative Belter asked whether shipping coal is cheaper than moving electricity by transmission lines. Dr. Ramsett said he does not believe shipping coal is cheaper but that there are high fixed costs in constructing and operating transmission lines.

Representative Belter asked why North Dakota lignite productivity had declined, according to the data in the report. Dr. Ramsett said this is probably a temporary situation and, although he is not certain what the reason would be, he suspects the temporary decline in productivity has to do with differences in the thickness of overburden or the underlying coal seam and technology.

Representative Belter said pressure from federal legislation on environmental standards is creating concern for the lignite industry, and he asked Dr. Ramsett whether this will also affect the future of lignite production. Dr. Ramsett said he did not examine that aspect of regulation, but this will be a continuing concern for all coal producers. He said environmental concerns are probably a greater stress for the lignite industry because other types of coal burn cleaner.

Senator Christmann said the data in figure No. 9 of the report indicates that the cost of Wyoming coal in South Dakota is extremely low, and he asked why that occurs. Dr. Ramsett said he had the same question when he reviewed the data, but he is not certain what the reason for the low cost would be. He said he thinks the answer relates to reduced transportation costs and perhaps a unique situation.

Representative Tollefson asked whether technology to extract moisture from lignite would help the competitive position of lignite in the market and whether the technology is available. Dr. Ramsett said he is not an expert in technology issues of this kind, but if the technology is available, it would also benefit subbituminous coal.

Chairman Belter called on Mr. John Dwyer, President, North Dakota Lignite Energy Council, for comments on the coal industry study. Mr. Dwyer said Dr. Ramsett's report underscores what the Lignite Energy Council has been saying for several years--that the lignite industry is in a fierce competitive war in the marketplace.

Mr. Dwyer said the Lignite Energy Council intends to work with the Governor, legislators, and the industry to develop a legislative approach for consideration in the 1999 Legislative Assembly. He said the Lignite Energy Council anticipates that the Legislative Assembly will continue the policy of help and

cooperation for the lignite industry that has always been provided.

Mr. Dwyer said there are several problem areas requiring attention to assist the lignite industry in its competitive efforts. He said Environmental Protection Act clean air requirements are a continuing concern. He said the North Dakota lignite industry has spent over \$1 billion to date and is subject to continuing pressure for changes and improved technology. He said the Kyoto Treaty and local regulations add further concern for clean air considerations imposing pressure on the industry. He said the lignite industry has gone to great lengths to comply with clean air requirements, and these expenses are a continuing concern.

Mr. Dwyer said the Great Plains Synfuels Project is under increasing financial pressure. He said fluctuating prices for natural gas create an uncertain marketplace. He said increased byproduct sales from the project have been important but will be insufficient to offset the loss of income from expiring contracts in the years 2002 and 2004. He said relief from the state and federal governments may be necessary to continue operation of the project.

Mr. Dwyer said another area of concern is the railroad transportation cost component. He said if railroad transportation costs for subbituminous coal continue to decrease, it will obviously affect decisions in the lignite industry. He said stability of railroad transportation pricing is another area of concern.

Mr. Dwyer said the externalities lawsuit in Minnesota was concluded successfully for the lignite industry. He said legal costs were extremely high for the effort, and prevailing does not guarantee that those responsible for the Minnesota law will give up. He said the possibility of large legal expenditures in the future is a concern.

In answer to a question by Representative Belter, Mr. Dwyer said the productivity decline was not due to a lack of effort. He said the temporary decline rate relates to the size of overburden being removed in current mining activity and to a loss of tonnage for various reasons, including importation of Powder River Basin coal for test burn purposes.

Mr. Dwyer displayed a slide showing taxation and regulatory costs per ton of lignite. He said the average price of lignite is approximately \$9, and 20 to 30 percent of that cost is attributable to regulatory and taxation costs. He said taxation costs are approximately \$1.49 per ton.

Mr. Dwyer displayed slides showing information on results of a Powder River Basin coal test burn at the Leland Olds Station. He said Powder River Basin coal burns with substantially lower levels of sulfur dioxide and nitrous oxide. He said the significance of this is that blending of Powder River Basin coal with North Dakota lignite for burning in the future may become environmentally significant as air standards become more stringent. He said blending Powder River Basin coal will reduce emissions from North

Dakota plants. He displayed slides showing information on economics of Powder River Basin coal burned in the Leland Olds Station. He said the price of Powder River Basin coal is \$3.12 per ton compared to \$10.56 per ton for lignite at the plant. He said the Powder River Basin coal would be subject to transportation costs of \$8.02 per ton plus the new North Dakota sales tax for imported coal of \$1.02 per ton. He said the comparison is a total cost per ton for Powder River Basin coal of \$12.16 versus a cost of \$10.56 per ton for lignite at the Leland Olds Station. He said the fact that a ton of lignite is less expensive is perhaps misleading. He said a more realistic measure of economics is converting the costs of coal to a price per million Btus. He said on this basis, North Dakota lignite cost is \$.78 per million Btus compared to \$.72 per million Btus for Powder River Basin coal delivered to the Leland Olds Station.

Senator Urlacher asked what ratio of Powder River Basin coal to lignite is used for blending. Mr. Dwyer said the blend tested was approximately 10 percent, but the blend could be adjusted for environmental or cost factors.

Representative Belter asked whether the Wyoming coal industry could increase its production capacity. Mr. Dwyer said Wyoming coal is now in extreme overproduction, which is why the price for Wyoming coal is so low. He said the Wyoming coal industry will continue to target out-of-state markets. He does not think more generating plants will be built in Wyoming, because Wyoming does not have adequate water supplies for generating plants.

Representative Tollefson asked whether it would be beneficial to eliminate the state severance tax and place greater reliance on a tax on electric generation. Mr. Dwyer said dropping the severance tax would make lignite more competitive but that would not be the recommendation of the Lignite Energy Council at this time. He said severance taxes are in lieu of sales taxes, and a sales tax in North Dakota would amount to approximately 50 cents per ton, while the severance tax is 77 cents per ton.

In response to a question from Representative Nichols, Mr. Dwyer said reclamation costs in North Dakota are higher than in Montana and Wyoming because the lignite industry is moving much more overburden to remove the underlying deposits of coal. He said the North Dakota lignite industry may need to look at ways to reduce costs of reclamation as part of its future competitiveness. He said the North Dakota lignite industry reclamation efforts exceed federal standards in several respects.

Representative Brown asked about the status of litigation by Montana coal interests challenging the North Dakota sales tax applications to imported coal. Mr. Dwyer said arguments in that case will be heard in the middle of September 1998.

Senator Christmann asked what variables can be considered as ways to reduce the cost per ton for lignite, other than tax levels. Mr. Dwyer said there are

some areas in regulatory considerations that could be looked at for potential cost reductions. He said reclamation is one area where North Dakota is more stringent than federal law, and it might be possible to relax some standards to reduce costs while maintaining North Dakota's good record on environmental concerns.

Chairman Belter called on Mr. Brian Gehring, Editor, Hazen Star newspaper, who said he would be concerned about effects of coal severance tax reductions on political subdivisions in the coal production area. He asked what proposed severance tax reduction is being considered. Mr. Dwyer described the allocation of coal severance tax revenues among political subdivisions and the state. Mr. Dwyer said there is no pending proposal for reduction of the coal severance tax, but if such a proposal is developed, there would be consultation with political subdivisions in the coal production area because the Lignite Energy Council considers those political subdivisions to be key players in development of legislative proposals.

Chairman Belter said the committee and the legislature have the report on the competitiveness on the lignite industry which will be good background information to consider. He said he expects the lignite industry to analyze its position and consult with the Governor, legislators, political subdivisions, and industry officials to develop proposals for consideration in the 1999 Legislative Assembly.

Representative Schmidt asked for information on areas of difference in North Dakota reclamation law and federal requirements. Mr. Jim Deutsch, Public Service Commission, said North Dakota law and rules regarding handling of topsoil and restoration to premined status are more stringent than federal requirements. He said federal requirements generally apply only to prime farmlands while North Dakota requirements apply to all mined lands. He said the depth of soil under North Dakota law and rules is also more stringent than federal requirements.

Senator Urlacher asked whether the preexisting terrain must be replaced even if it could be improved by the reclamation effort. Mr. Deutsch said there is room for improvements of terrain in areas such as a more gradual slope, but generally the effort is to replace terrain in its preexisting condition, if possible.

PROPERTY TAX EXEMPTIONS EFFECT ON SCHOOL DISTRICTS STUDY

Chairman Belter called on committee counsel to review two bill drafts relating to establishing a role for school districts in decisions on new industry property tax exemptions.

Committee counsel said the first bill draft relating to this topic would provide that a city or county granting an exemption or payments in lieu of taxes for a new industry would not create an exemption or payments in lieu of taxes with regard to property taxes levied by a school district unless the exemption or

payments in lieu of taxes are specifically approved by motion of the school board of the affected school district. He said the bill draft was revised after the July committee meeting to restate the authority as a positive statement rather than a motion to disapprove.

Committee counsel said the second bill draft relating to this study is patterned after 1995 legislation that expired in 1997. He said the bill draft would provide that a city or county considering a property tax exemption or option to make payments in lieu of taxes for a new industry must include, as nonvoting ex officio members of the city or county governing body, a representative appointed by the school board and the board of township supervisors from each affected school district or township. He said the bill draft contained an expiration date as considered at the July committee meeting, but the expiration date has been removed from the bill draft pursuant to a request of the committee in July.

Chairman Belter called on Ms. Bev Nielson, North Dakota School Boards Association, for comments on the committee study. Ms. Nielson said the association believes the bill permitting a school board to sit in on deliberations is inadequate representation. She said the association would prefer the authority for the school board to vote on exemption decisions with regard to its own levy authority. She said as an alternative, the association would prefer an option in which a school board member sitting in on deliberations with the city or county governing body would get a vote on the decision.

Chairman Belter called on Mr. Ken Yantes, North Dakota Township Officers Association, who said the association has supported the bill draft providing for ex officio participation of school district and township officials in exemption decisions in the past. He said he believes the association would support this bill draft during the next legislative session.

Chairman Belter called on Mr. Scott Stromme, Bismarck City Assessor, who said the city of Bismarck has not taken an official position on the bill drafts being considered by the committee. He said the school levy in Bismarck is a little more than 55 percent of total taxes imposed on property, and providing the school district authority to opt out of exemptions would greatly dilute the value of exemptions as economic development tools. He said even though the 1995 law expired in 1997, school officials continue to be invited to participate in exemption decisions in Bismarck. He said the message sent by the 1995 law has been received, and local officials are conscious of school district opinions with regard to property tax exemption decisions.

Chairman Belter asked for committee opinions on the two bill drafts. Senator Freborg said it seems appropriate to him that the school district, as the major property tax levying authority, should have the power to determine whether exemptions should be granted for properties within the school district. He said he would support the bill draft giving the school

district authority to approve exemptions for new business property.

It was moved by Representative Gorder and seconded by Representative Nichols that the bill draft providing school districts authority to approve or disapprove property tax exemptions for new industries be approved and recommended to the Legislative Council.

Representative Lloyd said he does not believe school board members would support property tax exemptions for new businesses.

Senator Freborg said he does not believe school board members would automatically reject property tax exemptions for new businesses.

Representative Kilzer said diluting authority over exemption decisions would make it difficult for a taxpayer to know to whom complaints should be made about exemption decisions. He said extending this authority to school districts would also serve as an argument that the authority should be extended to other political subdivisions.

Senator Kinnoin asked whether a school district would be able to grant an exemption on terms other than the exemption granted by the city or county under existing law. Committee counsel said he does not believe the school district could vary the terms of an exemption. He said North Dakota Century Code (NDCC) Chapter 40-57.1 allows a project operator to negotiate with a city or county governing body for an exemption and the length of time the exemption would apply. He said that chapter and the bill draft under consideration do not indicate that the school district could change the terms of an exemption but the bill draft states that school boards would have the authority to approve the exemption as to school district property tax levies. He said it appears this means approval of the exemption as granted by the city or county.

Representative Belter said he sympathizes with concerns of school districts, but he believes economic development officials will keep school district concerns in mind. He said he does not think decision authority on exemptions should be diluted.

The question was called and **the motion was defeated**. Voting in favor of the motion were Representatives Brown, Gorder, Kroeplin, Nichols, and Schmidt and Senators Freborg, Kinnoin, and Kringstad. Voting in opposition to the motion were Representatives Belter, Christopherson, Kilzer, Lloyd, Rennerfeldt, and Tollefson and Senators Christmann, Schobinger, and Urlacher.

It was moved by Senator Kinnoin and seconded by Senator Christmann that the bill draft providing for ex officio membership of school board and township representatives on city or county governing bodies considering property tax exemptions for new businesses be approved and recommended to the Legislative Council.

Senator Freborg asked why the bill draft provides that school district and township representatives would be nonvoting members of the city or county governing body. Committee counsel said the nonvoting status was provided in the 1995 law, and this bill draft was requested to be based on that law. Senator Freborg said the school district and township representatives should have voting authority. Representative Christopherson asked whether the committee could move to amend the bill draft to allow voting authority for school district and township representatives. Chairman Belter said that motion would be in order.

It was moved by Senator Freborg, seconded by Senator Urlacher, and defeated on a voice vote that the bill draft be amended by removing the nonvoting ex officio status of the school district and township representatives. In discussion of the motion, Representative Grosz said when a city makes an exemption decision, that decision applies to the county and the reverse would be true. He said he questions whether this change would open the door to suggestions that more political subdivision representatives be allowed to sit in and vote on these decisions. Representative Brown said he agrees with the concerns expressed by Representative Grosz, and he questions how far we can go to provide voting authority. Senator Christmann said that would also be a concern to him because law provides for an odd number of officials on governing bodies and adding additional members may make the possibility of tie votes more likely. Senator Urlacher said he supports participation of school and township officials in discussions but allowing the option to vote could become complicated.

The question was called on approval of the bill draft without amendment and **the motion carried**. Voting in favor of the motion were Representatives Belter, Brown, Christopherson, Gorder, Grosz, Kilzer, Kroeplin, Lloyd, Nichols, Rennerfeldt, Schmidt, and Tollefson and Senators Christmann, Freborg, Kinnoin, Kringstad, Schobinger, and Urlacher. There were no negative votes.

CHARITABLE ORGANIZATION PROPERTY TAX EXEMPTION STUDY

Chairman Belter called on committee counsel to review a bill draft based on a recent Pennsylvania law regarding property tax exemptions for charitable institutions. Committee counsel said a copy of a recent article from the *Journal of Multistate Taxation* regarding the Pennsylvania law was distributed to committee members. He said the bill draft is patterned after 1997 Pennsylvania House Bill No. 55, approved November 26, 1997. He said the article described the legislation as extraordinarily complex, and it is probably fair to say that every word was written in light of its effect on the hospital community. He said the author of the article observed that it remains to be seen whether the Pennsylvania law will

set a standard for review of charitable status in Pennsylvania and perhaps in other states with similar problems or whether it will prove too complex and difficult to administer.

Committee counsel said the Pennsylvania law was based on the 1985 Pennsylvania Supreme Court decision in *Hospital Utilization Project v. Commonwealth*, 487 A. 2d 1306, in which the Pennsylvania Supreme Court established five criteria to determine whether an organization is a purely public charity. He said the five criteria require that an organization must advance a charitable purpose, operate entirely free from private profit motive, donate or render gratuitously a substantial portion of its services, benefit a substantial and indefinite class of persons who are legitimate subjects of charity, and relieve the government of some of its burden. He said this five-part test forms the basis of the Pennsylvania law and of the bill draft before the committee. He reviewed the provisions of the bill draft regarding the five criteria. He said the bill draft expands substantially on how the five criteria are to be applied, and there are several provisions in the bill draft that are not clear in terms of to whom they would apply. He said these provisions were probably added as a result of concerns during consideration of the Pennsylvania legislation to address individual situations of charitable institutions in Pennsylvania. He said the bill draft repeals the current North Dakota exemption for charitable organizations and replaces it with the provisions based on the Pennsylvania law. He said the Pennsylvania law was apparently based largely on concerns about hospitals but applies to all charitable organizations and consideration should be given as to whether it is appropriate for all charitable organizations in North Dakota to be subject to these provisions.

Representative Tollefson said the key factor in the bill draft is to define what constitutes a purely public charity. He said this is a very difficult concept, and this is illustrated by the length and complexity of the bill draft based on the Pennsylvania law.

Representative Brown said the basic concept of the bill draft is a good approach, but he believes the Pennsylvania legislation became too complex in attempting to define the five criteria, and this bill draft will require more discussion and study than the committee has time for during this interim.

Representative Kilzer said the five concepts that are the basis of the bill draft seem simple but adding the great level of detail contained in the bill draft goes beyond a simple approach and appears to be too complex. He said he still believes it would be much easier to limit exemptions to areas of a facility used for inpatient services.

Chairman Belter called on committee counsel to review a bill draft allowing imposition of special assessments by cities against exempt property of charitable organizations. Committee counsel said the bill draft was patterned after NDCC Chapter 40-22.1, which allows imposition of special assessments

against business property for business promotion activities. He said the bill draft would allow a city to establish a special assessment district composed only of property of charitable organizations exempt under subsection 8 or subsection 31 of NDCC Section 57-02-08. He said the subsection 8 exemption is for property of charitable organizations and the subsection 31 exemption applies to group homes for developmentally disabled persons owned by an organization exempt under Section 501(c)(3) of the Internal Revenue Code. He said a special assessment district could include multiple, noncontiguous property areas and parcels and must include all properties which in the judgment of the governing body of the city are benefited by police and fire protection and infrastructure expenditures paid from the budget of the municipality. He said the bill draft limits the amount that may be levied against subject properties to the ratio that the value of those properties bears to the total valuation of those properties plus the taxable property in the city, and the amount levied may not exceed that percentage of the municipal expenditures for police and fire protection and infrastructure costs. He said the bill draft sets a ceiling that may be imposed but does not require that amount must be levied and allows any lesser amount to be imposed against subject properties. He said an amendment is required in the bill draft to clarify the collection, penalties, and administration of these special assessments in the same manner as provided for other special assessments by law. He said the amendment is required in the last sentence of NDCC Section 40-22.2-08 to provide that special assessments levied under this chapter are subject to extension, collection, payment, interest, and penalties in the manner provided in Chapters 40-24 and 40-25. He said this would allow administration in the same manner as for other special assessments.

Senator Urlacher asked whether this bill draft allows local flexibility in imposing special assessments against charitable property. Committee counsel said the bill draft is intended to provide flexibility and that it is not mandatory to levy these special assessments and the amount of special assessments is open to decision by the city governing body.

Representative Tollefson said the concept of the bill draft is his, and he arrived at this approach because special assessments are not considered to be property taxes and should not violate the constitutional property tax exemption for charities. He said the intention is that charitable organizations would pay for the value of services provided by the municipality in the same manner as charitable organizations pay for special assessments under existing law, because the services contribute to the value of the property. He said he has discussed this approach with officials in Minot who think it is a good approach to allow contributions for costs of services provided directly to benefit charitable organizations, which are currently subsidized by other taxpayers. He said this

approach may make for interesting local politics but gives the city an option to use if the city wishes to seek fair contributions for city services from charitable organizations.

Representative Belter asked whether the bill draft would apply to church property or private schools. Committee counsel said the bill draft would not apply to church property unless the church owns property that is used to operate a charitable organization. He said the property used for religious services and a home for a priest or minister is exempt under Section 57-02-08(7)(9) and the exemption for private schools is provided under Section 57-02-08(6), and these properties are not addressed by this bill draft.

In response to a question from Senator Christmann, Mr. Barry Hasti, State Supervisor of Assessments, said the organizations that are exempt under Section 57-02-08(8) would include hospitals, nursing homes, historical societies, the Red Cross, the YMCA, homeless shelters, and the Salvation Army to the extent property is not used for religious services.

Chairman Belter called on committee counsel to review a bill draft providing that the property tax exemption for hospital property applies only to the portion of a building used to provide inpatient services. Committee counsel said the bill draft has not been changed since it was reviewed by the committee in July and provides that the exemption for hospital property is limited to portions of a building used primarily to provide inpatient services or operations essential to the ability to provide inpatient services in the building.

Representative Brown asked who will make the determination of how this exemption is applied. Committee counsel said local assessment officials will be required to determine which portions of a hospital building would be exempt under this approach. He said there would be difficulties in administering the law and making these determinations, but assessment officials are currently faced with similar situations in assessment of hospital property because of the existence of pharmacies, gift shops, and shared facilities between an exempt hospital and a taxable clinic.

Representative Belter asked Representative Kilzer what is meant by inpatient services. Representative Kilzer said his intention is that inpatient means a person hospitalized or admitted to the hospital, and the objective is to not allow exemption for expansion of hospital property into areas beyond treatment of hospitalized persons because many hospitals are now expanding into other kinds of facilities not originally intended to be exempt under the existing law.

Chairman Belter called on Mr. Brian J. Nermoe, Manager, Public Policy, MeritCare Health System, for comments on the committee study. A copy of Mr. Nermoe's prepared testimony is attached as Appendix B.

Senator Kringstad asked how many properties are owned by MeritCare Health System. Mr. Nermoe said

the system owns property in several areas of North Dakota and Minnesota, and its inpatient service center is the hospital in Fargo.

Senator Kinnoin asked what is the advertising budget for MeritCare Health System per year. Mr. Nermoe said he is not certain what the advertising budget would be, and it would be difficult to distinguish advertising expenditures from public service-type announcements. He said he would provide information on this to Senator Kinnoin.

Committee counsel asked whether there is a difference in property tax exemptions or property tax rates for MeritCare Health System properties in North Dakota and Minnesota. Mr. Nermoe said he is not certain but could research that issue.

Chairman Belter called on committee counsel to review a bill draft to limit the acreage that may be acquired by a nonprofit organization in North Dakota. Committee counsel said the bill draft has not been changed since it was considered by the committee in July. He said the bill draft is the same as 1997 Senate Bill No. 2385 which was vetoed by the Governor. He said the bill provides that a nonprofit organization may not acquire more than 16,000 acres of land in North Dakota. He said the bill was vetoed by the Governor, who stated in his veto message that the bill addresses a valid public policy concern but that the Governor intended to initiate a process to inventory nonprofit land ownership and develop an agreement on how much is enough property for these organizations to own. Committee counsel said the Governor's office declined an invitation to address the committee on this issue.

Representative Grosz said it seems this approach does not address legislative concerns about protecting the tax base. He said he fears this approach would serve more as a means to depress land prices. He said if that is the purpose of the bill, it is a wrong approach. He said if the legislature is concerned with the tax base, legislation should be enacted providing that landowners must continue to pay taxes. He said the approach in the bill draft is against the traditional willing buyer, willing seller concept.

Senator Christmann said there are problems with charitable organizations acquiring farm property. He said when a charitable organization buys property, it knows it will not be paying property tax in the future, and for that reason, it can afford to bid more for the property than a farmer would be able to pay.

Senator Urlacher said a big concern of the Legislative Assembly is the declining tax base due to acquisition of taxable property by charitable organizations and the removal of that property from the tax base. He said remaining landowners are faced with a growing tax burden due to these acquisitions, and he thinks farmers require some form of protection.

Chairman Belter invited testimony from interested persons regarding the charitable organization bill drafts being considered by the committee.

Mr. Wade Peterson, Medcenter One Care Center, Mandan, said his organization is concerned about the approach in the bill patterned after Pennsylvania law. He said most nursing home facilities would have problems under the community service requirement of the bill draft. He said placing a property tax burden on nursing homes would simply add to the amount that must be charged to residents for nursing home services.

Mr. Wade Moser, North Dakota Stockmen's Association, said North Dakota's corporate farming law is a statement of state policy with regard to ownership of agricultural land. He said the federal government has several new programs, and private foundations have huge amounts of money to acquire farmland for preservation. He said the Stockmen's Association is concerned about preservation of private ownership of farmland for the continued health of the farm economy. He said the Governor's Wetlands Committee is working on issues of land usage, and he serves on that committee. He said approximately 8.3 million acres in North Dakota, or 21 percent of acreage, is controlled by government ownership, including CRP land. He said this amount does not include sodbuster or swampbuster restricted lands. He said an enormous amount of potential farmland is already outside private ownership, and he thinks the Legislative Assembly should enact the bill limiting acreage for organizations. He said this would be in harmony with the restriction against corporations buying farmland.

Mr. Joe Satrom, Nature Conservancy, said the Nature Conservancy owns 18,262 acres in North Dakota. He said the Nature Conservancy willingly pays property taxes on all of that property. He said the Nature Conservancy deals only with willing sellers in acquisitions in North Dakota. He said the Nature Conservancy has recently turned down acquisition of substantial amounts of farmland. He said the Nature Conservancy opposes the bill draft limiting acreage that may be acquired by nonprofit organizations.

Representative Brown asked whether there is an advantage to a seller in selling property to a nonprofit organization. Mr. Satrom said there is no advantage to sellers unless they sell the property for less than full value, in which case they could take credit for a charitable contribution for the amount less than full value.

Senator Urlacher said holdings of the Nature Conservancy continue to grow, and he asked whether that acquisition policy will continue. Mr. Satrom said the Nature Conservancy currently owns 18,262 acres of land in North Dakota and is currently involved in another acquisition of a limited nature. He said the organization pays full assessment and property taxes like other taxpayers, although it is not required by law. He said the Nature Conservancy would support enactment of legislation requiring the Nature Conservancy to pay property taxes on its land holdings.

Chairman Belter asked whether the committee wishes to take action on the bill draft based on Pennsylvania law regarding charitable organizations property tax exemptions. No motion was made.

It was moved by Senator Kringstad, seconded by Representative Lloyd, and carried that the bill draft allowing imposition of special assessments against charitable property be amended by amending the final sentence of Section 40-22.2-08 to read "special assessments levied under this chapter are subject to extension, collection, payment, interest, and penalties in the manner provided in chapters 40-24 and 40-25."

It was moved by Representative Tollefson, seconded by Representative Brown, and carried on a roll call vote that the bill draft, as amended, relating to imposition of special assessments against property of charitable organizations be approved and recommended to the Legislative Council. Voting in favor of the motion were Representatives Belter, Brown, Christopherson, Gorder, Grosz, Kilzer, Kroeplin, Lloyd, Nichols, Rennerfeldt, Schmidt, and Tollefson and Senators Christmann, Freborg, Kinnoin, Kringstad, Schobinger, and Urlacher. There were no negative votes.

It was moved by Representative Kilzer, seconded by Representative Tollefson, and failed on a roll call vote that the bill draft relating to imposition of property taxes for hospital property not used primarily to provide inpatient services be approved and recommended to the Legislative Council. Voting in favor of the motion were Representatives Grosz, Kilzer, and Tollefson and Senators Freborg, Kinnoin, and Kringstad. Voting in opposition to the motion were Representatives Belter, Brown, Christopherson, Gorder, Kroeplin, Lloyd, Nichols, Rennerfeldt, and Schmidt and Senators Christmann, Schobinger, and Urlacher. In discussion of the motion, Representative Schmidt said he opposes the concept of the bill draft because of its effect on small town medical facilities.

It was moved by Representative Brown, seconded by Senator Christmann, and failed on a roll call vote that the bill draft relating to limitation of the acreage of property that may be owned by a nonprofit organization be approved and recommended to the Legislative Council. Voting in favor of the motion were Representatives Belter, Brown, Kroeplin, Lloyd, Rennerfeldt, Tollefson, Christmann, Schobinger, and Urlacher. Voting in opposition to the motion were Representatives Christopherson, Gorder, Grosz, Kilzer, Nichols, and Schmidt and Senators Freborg, Kinnoin, and Kringstad. Chairman Belter declared the motion defeated for lack of a majority. In discussion of the motion, Representative Schmidt said he thinks it is wrong to limit the opportunity of a seller to sell property to whom he chooses.

AGRICULTURAL PROPERTY ASSESSMENT STUDY

Chairman Belter called on Mr. Dwight Aakre, North Dakota State University Extension Service, Fargo, for presentation of an analysis of the effects of a bill draft to restrict changes in the capitalization rate used in the agricultural property valuation formula. Mr. Aakre said the proposal would restrict the capitalization rate to no less than 10 percent and no more than 11 percent. He said the capitalization rate is presently calculated as an average of annual interest rates charged by AgriBank for farm loan mortgages over the latest 12 years with the high and low years excluded.

Mr. Aakre said the chart showing mortgage rates are the actual rates used from 1980 through 1997. He said it was necessary to estimate mortgage rates for the years 1998 through 2007 by regression analysis of the relationship between AgriBank mortgage rates and federal home mortgage rates and Moody's AAA corporate bond rate.

Mr. Aakre said a computation was done of values for all agricultural lands in all counties using alternative capitalization rates. He said the computations indicate a range of approximately four percent in the difference of land values depending on whether the capitalization rate is 10.14 percent or 9.77 percent.

Mr. Aakre said values for agricultural land for 1998 through 2007 are shown in the data he prepared. He said values are capitalized at 10 percent, the proposed minimum in the bill draft and, as an alternative, are capitalized at the projected capitalization rate for each year. He said limiting the capitalization rate to no less than 10 percent will result in land valuation reductions of approximately 2.5 percent per year with total reduction of approximately 14 percent by the year 2007.

Representative Schmidt said he believes North Dakota farmers need this legislation, especially in the Devils Lake Basin where valuations continue to climb despite economic hardships of farmers. He said he appreciates concerns about tinkering with the valuation formula, but the Legislative Assembly has done so in the past, and he believes it is appropriate to do so in the current agricultural economy.

In response to a question from Representative Belter, Mr. Hasti said taxes paid will not relate directly to valuation changes. He said valuation plays a part in determining property tax liability but several other variables are involved, including local levy amounts, the mix of property types in the taxing district, and other factors.

Chairman Belter called on committee counsel to review a bill draft to freeze the capitalization rate in the agricultural property valuation formula. Committee counsel said the bill draft provides that the capitalization rate may not be less than 10 percent and may not be more than 11 percent.

Senator Christmann said the bill draft is intended to assist struggling agricultural property owners, and

he asked why a cap should be placed on the high end of the interest rate. He said capping the low end assists farmers, but capping the high end would be a problem in the future if interest rates rise over an extended period of time.

Representative Schmidt said he is not too concerned about the cap at the 11 percent rate on the high end because he is primarily concerned about decreases in the capitalization rate and resulting increases in property valuations.

Senator Thompson said he sat in with the State Board of Equalization meeting earlier today and the board is dealing with valuation problems for agricultural properties in Devils Lake Basin counties. He said the State Board of Equalization has tabled action because it would be difficult and would impose a hardship on those counties to follow the letter of the law in applying agricultural property valuations as determined under the statutory formula. He said he believes this bill draft is important to show the concern of the Legislative Assembly with these difficulties.

Representative Grosz said valuation changes for agricultural property will shift tax burdens from agricultural to residential property owners. He said if that is all that would be accomplished, it may create a problem. He said shifting tax burdens onto residents of small towns who are subject to fixed incomes is not a desirable alternative. He said the balance among tax burdens for property tax types will be a topic of future consideration.

Representative Belter said he opposes the concept in the bill draft. He said as a farmer he is concerned about valuation changes, but he said the Legislative Assembly must be very careful that there is a legitimate reason to alter the agricultural property valuation formula and that changes are not made simply to achieve reductions for agricultural property owners. He said it looks to him as though this bill draft would have variable effects based on the county mix of residential and agricultural property.

Representative Gorder said we are in an agricultural crisis like he has not seen before. He said there is a great need in the affected area for property tax relief, and he supports the approach in the bill draft.

Representative Brown asked how long it would be until the bill draft begins to affect property valuations. Mr. Aakre said the 1999 tax year would be the first year affected.

Chairman Belter called on committee counsel to review a bill draft providing for separate valuation of inundated agricultural land. Committee counsel said the bill draft was reviewed at the July meeting and should be amended to substitute the word "inundated" for the word "unproductive" throughout the bill draft and that a blank is included in the bill draft which must be completed to supply a percentage of noncropland valuation that would be the value for inundated agricultural land for each county. He said the bill draft was suggested to deal with assessment problems that have arisen in Devils Lake Basin counties. He said

current law requires county average agricultural value to equal the amounts determined under the formula. He said the problem with this is that property that has been inundated and is unproductive can receive a valuation reduction by the county board of equalization, but the remaining properties in the county must be increased in valuation to achieve the average valuation required by the formula. He said the bill draft creates a category of inundated agricultural land that is unsuitable for growing crops or grazing farm animals for a full growing season or more. He said this classification would allow inundated properties to be separately considered and not affect county average agricultural valuations for property that is not inundated.

Representative Belter asked how much would be an appropriate value per acre for inundated lands under the bill draft. Senator Thompson said in his area, valuations of approximately \$15 per acre are being placed on inundated lands. Mr. Barry Hasti, State Tax Department, said Ramsey County noncropland valuations are approximately \$97, and noncropland valuations for the region range from about \$64 to about \$112. He said approximately 10 percent of noncropland valuation would result in per acre average valuations from 6 to 11 dollars.

It was moved by Representative Nichols, seconded by Representative Lloyd, and carried that the bill draft be amended by using 10 percent of average noncropland valuation as the value for inundated agricultural lands and that the word "inundated" be substituted for the word "unproductive" throughout the bill draft.

Chairman Belter called on committee counsel to review a bill draft to include a producer cost index in the agricultural property valuation formula. Committee counsel said the bill draft has been considered by the committee at previous meetings and would require the formula to include a base year index of prices paid by farmers compared with an average of those costs over the most recent 10 years and would require that the changes in prices paid by farmers be used to factor into the valuation formula. He said Mr. Aakre analyzed this change for the committee at its July meeting and indicated that a valuation decline of about two percent per year would occur compared to calculations under the current formula. He said Mr. Aakre estimated the cumulative effect of this change would be a reduction of approximately 25 percent in agricultural property valuations by the year 2010.

Representative Grosz said he is concerned that including a farmer's cost index in the valuation formula will lower agricultural property valuations too much. He said someone has to pay property taxes and substantial agricultural property valuation decreases will cause a substantial shifting of property tax burdens.

Ms. Patti Lewis, North Dakota Farm Bureau, said the area that requires control is setting of budgets by

political subdivisions. She said political subdivision spending is what drives property tax amounts. She said the Farm Bureau does not support altering the valuation formula simply to control property tax levels.

Mr. Lauren Hunze, Director, McLean County Tax Equalization Board, said local boards of tax equalization can make adjustments in property valuations. He said he is concerned about the bill draft allowing reduced valuation for inundated lands. He said McLean County has had lots of wetlands plowed up, and he asked whether valuations will go back up when the property is put into production. He said he is concerned about changes to the valuation formula because it has worked well for agriculture in North Dakota.

It was moved by Senator Thompson, seconded by Representative Gorder, and carried on a roll call vote that the bill draft limiting the capitalization rate to no more than 11 percent and no less than 10 percent in the agricultural property valuation formula be approved and recommended to the Legislative Council. Voting in favor of the motion were Representatives Gorder, Grosz, Kroeplin, Nichols, and Schmidt and Senators Christmann, Freborg, Kinnoin, Kringstad, and Thompson. Voting in opposition to the motion were Representatives Belter, Brown, Christopherson, Kilzer, Lloyd, Rennerfeldt, and Tollefson and Senators Schobinger and Urlacher.

It was moved by Representative Nichols, seconded by Senator Thompson, and carried on a roll call vote that the bill draft, as amended, relating to valuation of inundated agricultural land be approved and recommended to the Legislative Council. Voting in favor of the motion were Representatives Belter, Brown, Gorder, Grosz, Kroeplin, Nichols, and Schmidt and Senators Christmann, Freborg, Kinnoin, Kringstad, Schobinger, Thompson, and Urlacher. Voting in opposition to the motion were Representatives Christopherson, Kilzer, Lloyd, Rennerfeldt, and Tollefson.

It was moved by Senator Urlacher and seconded by Representative Lloyd that the bill draft relating to including a farmers price index in the agricultural property valuation formula be approved and recommended to the Legislative Council. In discussion of the motion, Senator Urlacher said he believes production costs have become so significant to farmers that the oversight of not including this factor in the valuation formula needs to be corrected.

Representative Grosz said he would support this change for the time being but the cyclical nature of agriculture must be remembered, and if agricultural production costs decline, it will result in property tax valuation increases.

In response to a question from Representative Brown, Mr. Aakre said farm production costs have increased approximately 67 percent in 10 years while

yields have increased by 7.5 to 8 percent over that time period, and prices have declined.

Representative Belter asked Mr. Aakre whether there are inequities in using production costs in the valuation formula. Mr. Aakre said if the cost index is correct, it would work similarly to the landowners' share currently used in the formula but would be computed on an annual basis, so it should be more accurate. He said a criticism could be that the formula does not account for technological improvements that will increase production.

Commissioner Rick Clayburgh, Tax Department, said budget control is the significant factor in limiting property taxes. He said simply holding property valuations in check may not provide any property tax relief.

Representative Rennerfeldt said the city of Williston has some of the highest property taxes of North Dakota cities, and many citizens are on fixed incomes. He said he thinks it would be unfair to provide by legislation for reduction in farmland valuations and a resulting shift in property tax burdens to city property.

The question was called and **the motion carried**. Voting in favor of the motion were Representatives Brown, Gorder, Grosz, Kroeplin, Lloyd, Nichols, and Schmidt and Senators Christmann, Kinnoin, Thompson, and Urlacher. Voting in opposition to the motion were Representatives Belter, Christopherson, Kilzer, Rennerfeldt, and Tollefson and Senators Kringstad and Schobinger.

Chairman Belter called on committee counsel to review a bill draft to make clear that a beginning farmer is entitled to the farm residence exemption. Committee counsel said the bill draft was considered at the July committee meeting and relates to a problem encountered in Ward County when tax officials observed that the law requires a farmer to have received 50 percent or more of annual net income from farming. Strictly applied, the law would prevent beginning farmers from qualifying for the exemption since they would not have a history of farm income to consider. Committee counsel said the bill draft changes the provision of existing law by providing that a beginning farmer is entitled to an exemption if the beginning farmer has acquired ownership and occupancy of a farm within the three preceding calendar years, normally devotes the major portion of time to producing products of the soil, poultry, livestock, or dairy farming, and does not have a farm income history for each of the three preceding calendar years. He said this would have the effect of allowing a beginning farmer to qualify for the farm residence exemption for three years regardless of income source. He said the bill draft should be amended pursuant to a suggestion at the July committee meeting by substituting the word "begun" for the words "acquired ownership and" and inserting the words "and operation" after the word "occupancy" on page 2, line 16,

and by substituting the word "operation" for the word "ownership" on page 2, line 21.

It was moved by Senator Kinnoin, seconded by Senator Christmann, and carried on a voice vote that the bill be amended as suggested.

It was moved by Senator Kinnoin, seconded by Senator Christmann, and carried on a roll call vote that the bill draft, as amended, relating to beginning farmers qualifying for the farm residence exemption be approved and recommended to the Legislative Council. Voting in favor of the motion were Representatives Belter, Brown, Gorder, Grosz, Kilzer, Kroeplin, Lloyd, Nichols, Rennerfeldt, Schmidt, and Tollefson and Senators Christmann, Kinnoin, Kringstad, Thompson, and Urlacher. Voting in opposition to the motion was Representative Christopherson.

Chairman Belter called on committee counsel to review a bill draft relating to valuation of exempt property by assessors. Committee counsel said the committee considered a previous version of this bill draft at the July meeting to repeal NDCC Section 57-02-14, which requires the assessor to value any property that is exempt from taxation that is not owned by state, federal, and local government. He said the problem with the previous version of the bill draft is that 1995 and 1997 legislation requires assessment of only certain exempt property, but the provisions of Section 57-02-14, enacted in 1897, require assessment of additional property, in conflict with the more recent legislation. He said the bill draft now would add farm buildings and residences to the properties excluded from assessment. He said he would suggest for clarification that the word "farm" be added immediately before the word "residences" on page 1, line 13.

It was moved by Representative Grosz, seconded by Representative Schmidt, and carried on a roll call vote that the bill draft relating to valuation of exempt property be amended by inserting the word "farm" immediately before the word "residences" on page 1, line 13, and, as amended, that the bill draft relating to valuation of exempt property be approved and recommended to the Legislative Council. Voting in favor of the motion were Representatives Belter, Brown, Christopherson, Gorder, Grosz, Kilzer, Kroeplin, Lloyd, Nichols, Rennerfeldt, Schmidt, and Tollefson and Senators Christmann, Kinnoin, Kringstad, Thompson, and Urlacher. There were no negative votes.

Chairman Belter called on committee counsel to review a bill draft relating to the farm buildings exemption. Committee counsel said the bill draft was considered by the committee in July and the bill draft amends existing law to provide that factors announced by the North Dakota Supreme Court in the *Butts* decision would not be considered in applying the exemption for farm buildings. He said the bill draft specifically excludes consideration of whether the farmer grows or purchases feed for animals raised on

the farm, whether the farmer owns the animals being raised on the farm, whether replacement animals are produced on the farm, and whether the farmer is engaged in contract feeding of animals. He said the bill draft also incorporates language intended to implement the suggestion of members of the Ag Coalition that processing of agricultural products should not qualify as farming under the exemption. He said the bill draft attempts to do this by providing that business other than farming would include processing to produce a value-added physical or chemical change in an agricultural commodity beyond the ordinary handling of that commodity by a farmer prior to sale. He said the language is intended to allow flexibility of interpretation by assessment officials to recognize ordinary farm practices but to exclude processing that goes beyond ordinary handling. He said the other significant change in the bill draft is inserting the word "primarily" in regard to the usage of a farm building. He said existing law requires exclusive usage for agricultural purposes, which means the exemption is lost with even an incidental usage of a building for other purposes.

Chairman Belter called on Mr. Moser who said the Ag Coalition has reviewed the bill draft and supports enactment of the bill draft.

Chairman Belter called on Ms. Lewis who said the North Dakota Farm Bureau has reviewed the bill draft and supports enactment of the bill draft.

It was moved by Senator Christmann, seconded by Representative Grosz, and carried on a roll call vote that the bill draft relating to factors to be considered in applying the farm buildings exemption be approved and recommended to the Legislative Council. Voting in favor of the motion were Representatives Belter, Brown, Christopherson, Gorder, Grosz, Kilzer, Kroepflin, Lloyd, Nichols, Rennerfeldt, Schmidt, and Tollefson and Senators Christmann, Kinnoin, Kringstad, Thompson, and Urlacher. There were no negative votes.

PROPERTY TAX RELIEF STUDY

Chairman Belter called on Mr. Hasti for presentation of information requested by the committee comparing property taxes among various property classifications in recent years. Mr. Hasti said he prepared information to address the issue on the basis of county population because property tax burdens differ within counties based principally on the amount and mix of residential and commercial property in the county. He said the charts he prepared illustrating the changes show the percentage of total property taxes paid by the four classifications of property for the years 1984 to 1998. A copy of the data presented by Mr. Hasti is attached as Appendix C.

Mr. Hasti said the proportionate share of property tax paid on a statewide basis by owners of agricultural property has declined from 38.2 percent of the total in 1984 to 31.7 percent of the total in 1998. He said the

percentage of total property taxes from agricultural property declines as population increases and that as population grows there is a narrower range of the proportionate share of property tax among the four property classifications. He said in counties of fewer than 2,500 people, property taxes from agricultural property have remained between 72 and 77 percent of total property taxes for the county. He said the percentages decline as population grows, and that in counties with 20,000 or more population agricultural property accounts for 11.8 percent of property taxes paid in 1998, which represents a reduction from 16 percent in 1984.

Mr. Hasti said that in counties of fewer than 20,000 population, agricultural property pays the largest share of property taxes. He said that in the eight counties with more than 20,000 population, residential property is subject to the greatest property tax share and currently exceeds 50 percent of total property taxes paid in those counties. He said the effect of the eight large population counties is so pervasive that the statewide totals show that residential property pays the largest share of property taxes and has done so since 1990.

Senator Christmann said it would be interesting to compare data on what an average farmer and an average urban resident have paid in property taxes over a period of several years. Mr. Hasti said there is not sufficient data to complete that kind of comparison.

Chairman Belter called on Mr. Tony Clark, Tax Department, for presentation of information requested by the committee regarding comparison of income among regions of the state. A copy of the data prepared by Mr. Clark is attached as Appendix D. Mr. Clark said interesting comparisons exist among regional per capita income considerations. He said in 1986 per capita income among the regions was in a relatively narrow range from \$11,157 to \$13,461. He said by 1996 the regional incomes had stratified and ranged from \$15,905 to \$23,117. He said the average increase in per capita income per year has been variable among the regions in the comparison.

Mr. Clark said comparison of average annual wages by industry within the planning regions for 1996 is presented in a table in the materials distributed. He said comparison of North Dakota average annual wages by industry for 1986, 1991, and 1996 appears on the final page of the materials.

Mr. Clark said to the extent there is a property tax problem for agricultural property owners, it appears the problem is magnified more by low commodity prices rather than by property tax increases. He said the information available indicates that agricultural property is not really getting a larger burden of property taxes relative to other taxpayers, and if agricultural prices were better, much of the property tax concern would be alleviated.

Chairman Belter called on committee counsel to review a bill draft relating to the homestead property

tax credit for persons 65 years of age or older with limited income. Committee counsel said Chairman Belter requested preparation of the bill draft for consideration by the committee under the property tax relief authority of the committee. He said the bill draft provides for an increase of \$500 across the board in the income limits for eligibility for the homestead credit. He said the current high-income amount to qualify for the exemption is \$13,500, which would be raised to \$14,000 under the bill draft.

Representative Belter inquired about the fiscal effect of the bill draft. Committee counsel said the Tax Department has not had time to fully analyze the effect of the suggested change but believes the fiscal effect would be an increased cost to the state for reimbursing the homestead credit of less than \$200,000 per biennium. Committee counsel said the bill draft should be amended to correct an oversight appearing on page 1, line 12, and that the amount of "\$13,500" should be amended to read "\$14,000" to be consistent with other changes in the bill draft.

It was moved by Representative Grosz, seconded by Representative Rennerfeldt, and carried on a roll call vote that the bill draft be amended by substituting "\$14,000" for "\$13,500" on page 1, line 12, and that the bill draft, as amended, relating to qualification for the homestead credit be approved and recommended to the

Legislative Council. Voting in favor of the motion were Representatives Belter, Brown, Christopherson, Gorder, Grosz, Kilzer, Kroeplin, Lloyd, Nichols, Rennerfeldt, Schmidt, and Tollefson and Senators Christmann, Kringstad, Thompson, and Urlacher. There were no negative votes.

Chairman Belter said it appears the committee has concluded its interim business. He thanked the committee members for their work during the interim.

It was moved by Representative Brown, seconded by Representative Christopherson, and carried that the chairman and the staff of the Legislative Council 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 Council.

It was moved by Representative Rennerfeldt, seconded by Representative Christopherson, and carried that the meeting be adjourned sine die.

The meeting was adjourned at 5:30 p.m.

John Walstad
Committee Counsel

ATTACH:4