

NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

FINANCE AND TAXATION COMMITTEE

Thursday, June 1, 2006
Roughrider Room, State Capitol
Bismarck, North Dakota

Senator Herb Urlacher, Chairman, called the meeting to order at 10:00 a.m.

Members present: Senators Herb Urlacher, John M. Andrist, Dwight Cook, Harvey Tallackson, Ben Tollefson, Rich Wardner; Representatives Larry Bellew, Wesley R. Belter, Kari Conrad, David Drovdal, Pam Gulleason, C. B. Haas, Lyle Hanson, Craig Headland, Gil Herbel, Phillip Mueller, Kenton Onstad, Mark S. Owens, Arlo E. Schmidt, Dave Weiler, Clark Williams, Dwight Wrangham

Members absent: Senator Michael A. Every; Representative Ronald A. Iverson

Others present: See Appendix A

It was moved by Senator Tallackson, seconded by Senator Wardner, and carried on a voice vote that the minutes of the April 12, 2006, committee meeting be approved as distributed.

TAX DEPARTMENT

Chairman Urlacher called on Ms. Marcy Dickerson, State Supervisor of Assessments and Director of the Property Tax Division, Tax Department, for testimony in response to questions asked by the committee. A copy of Ms. Dickerson's prepared testimony is attached as Appendix B.

Ms. Dickerson reviewed information she gathered from other states concerning treatment of conservation reserve program (CRP) land that is also used for hunting or other recreational uses. She said primary use of land for agricultural purposes appears to be the most common criterion used by other states for classification of agricultural land. She said primary use of land is measured by revenue produced and if recreational use generates more revenue than CRP payments, the land loses its agricultural assessment status.

Ms. Dickerson reviewed data gathered on agricultural property within the city limits of the 13 largest cities in North Dakota from the 2005 abstract of tax lists. She said there are almost 6,000 acres of agricultural property within these cities with a cumulative true and full value of more than \$4.6 million. She said the average true and full value per acre assessed for these properties varies substantially among cities.

Senator Cook asked whether assessed valuation of agricultural land within cities is determined in the same manner as for other agricultural land. Ms. Dickerson said if the property is agricultural

property, it should be valued according to the productivity valuation method for agricultural property. She said she does not know why agricultural property within some cities is assessed at a much higher value per acre than one would expect under the formula. Senator Cook asked whether market value assessment is used for these properties. Ms. Dickerson said market value would not be the valuation method if the property is classified as agricultural. She said if property has been platted, there are seven statutory factors listed in the definition of agricultural property and if four or more of the factors apply, the property is not agricultural property and is subject to market value assessment.

Representative Mueller asked if Ms. Dickerson observed any approach in other states in her survey of treatment of CRP land used for recreational purposes that would be useful for North Dakota to follow. Ms. Dickerson said other states use basically the same approach used in North Dakota, in which the dominant source of income would determine whether the property is agricultural or not.

Committee counsel said it appears this state does not provide assessors any practical way to determine income from different uses for agricultural property. Ms. Dickerson said some states require property owners to file a claim for agricultural assessment status and on the claim, landowners are required to provide information on income from agricultural use and other uses of the property.

Senator Andrist said it has been stated that there could be constitutional problems in assessing property taxes differently for residents and nonresidents. He asked whether Ms. Dickerson got any sense from looking at other state laws of how tax preferences are provided for residents. Ms. Dickerson said most states provide a homestead credit, which allows a lower actual rate of taxation for state residents. Senator Andrist said he saw a news story about Florida residents receiving a lower tax rate than nonresidents. Ms. Dickerson said she is not familiar with how Florida treats residents for property tax purposes. Committee counsel said an income tax credit is another method used by states to provide a lower effective tax rate for residents. He said because the income taxes are primarily paid by state residents, the credit is unavailable to many nonresidents.

Representative Herbel said the chart of agricultural property valuation shows a substantial difference between Fargo and Grand Forks assessments of

agricultural land within the city. He asked why these valuations are so different. Ms. Dickerson said she is not sure but some of the valuations per acre look out of line with agricultural valuations that should be applied.

In response to a question from Senator Cook, Ms. Dickerson said she could look into the reasons for the high per acre assessment of agricultural property in Fargo.

Ms. Dickerson said the next issue she was asked to address relates to the number of nonresident owners of North Dakota property. She said information was requested from the Farm Services Agency but no response was received. She said representatives of the North Dakota Association of Counties conducted a survey of county officials to obtain information on nonresident property ownership, and a memorandum from Mr. Terry Traynor, Assistant Director, North Dakota Association of Counties, is attached to Ms. Dickerson's prepared testimony. Mr. Traynor's memorandum states that the county survey data is not yet complete but results have been received from 26 counties. Preliminary results indicate that nonresident ownership is varied across the state and commercial property has the highest nonresident ownership percentage and residential property appears to have the lowest nonresident ownership percentage. Mr. Traynor's memorandum states it is hoped that complete results of the county survey can be presented at the next committee meeting.

Chairman Urlacher called on Ms. Kathryn Strombeck, Research Analyst, Tax Department, for presentation of information on services that are subject to sales taxes in South Dakota and the potential revenue effect if the same services were taxable in North Dakota. A copy of the estimates prepared by Ms. Strombeck is attached as Appendix C.

Representative Conrad asked whether legal services taxable in South Dakota are subject to taxation when billed or when paid. Ms. Strombeck said the tax applies when services are billed and if bills are unpaid, the retailer is eligible for a credit for bad debt similar to the credit available to retailers in North Dakota.

Senator Andrist asked what is included in the category of advertising services. Ms. Strombeck said advertising agencies would be included and any other services within the standard industrial classification code for advertising services.

Senator Urlacher asked if there are substantial administrative problems in taxing services. Ms. Strombeck said Florida tried broadening the sales tax base to include services but backed off after encountering administrative and political problems. She said South Dakota and Hawaii tax a broad range of services.

In response to a question from Representative Mueller, Ms. Strombeck said the South Dakota sales tax rate is 4 percent but the estimates provided are

based on taxable sales and the estimates for North Dakota are based on the 5 percent state sales tax rate.

Committee counsel said the category shown as miscellaneous services not elsewhere classified shows a substantial amount of revenue. Ms. Strombeck said if multiple services are part of a sale, reporting is combined and may end up reported in the miscellaneous category.

EDUCATION PROPERTY TAX RELIEF STUDY

Chairman Urlacher called on committee counsel for presentation of a memorandum entitled [School District General Fund Levies and Limitations](#). Committee counsel said school districts have statutory authority to levy property taxes for special fund or general fund purposes. He said special fund levies may be unlimited or subject to a limit of a specific number of mills. He said the schedule of limitations prepared by the Tax Commissioner's office provides a brief summary of each statutory levy limitation that applies to school districts. He said school district general fund levies may be subject to limitation expressed in mills applied to taxable valuation of property or an optional limitation based on the number of dollars levied in property taxes in a base year or expanded or unlimited mill levy authority may be approved by the voters.

Committee counsel said North Dakota Century Code (NDCC) Section 57-15-14 allows a school district to impose a general fund levy of up to 185 mills against the taxable valuation of property in the school district. He said a school district may increase its property tax levy in dollars by up to 18 percent annually until the 185-mill limit is reached. He said this statute also gives school districts the option to seek increased or unlimited mill levy authority upon approval by voters of the school districts.

Committee counsel said NDCC Section 57-15-01.1 allows a school district to levy up to the highest amount levied in dollars in the three preceding taxable years, subject to adjustments. He said the base year amount is adjusted to reflect changes in taxable status of property, new property, and new or expired mill levy authority authorized by the voters or the Legislative Assembly. He said this optional levy authority was originated in 1981 when the property tax assessment system of the state was restructured. He said after restructuring, several school districts were above the general fund levy limitation cap so the optional method was necessary to avoid substantial cuts in levy authority. He said the optional levy method also provided for annual percentage increases in levies for several years, which further increased levies above the normal 185-mill cap rate.

Committee counsel said a report prepared by the Department of Public Instruction shows ranking of school districts by the number of mills levied in 2005 and the report is attached as an appendix to the

memorandum. He said the average general fund mill rate in this report is 199.24 mills but only 20 of the 204 school districts in the state levied more than that average amount. He said approximately 83 percent of school districts levied within the range from 130 to 200 mills.

Committee counsel said the report from the Department of Public Instruction has a column of information showing taxable valuation per pupil for each school district. He said this statistic is what is generally used to distinguish "rich" from "poor" school districts and could be used as a basis to address equity of funding issues. He said a review of taxable valuation per pupil shows that it is often true that districts with a higher than average taxable valuation per pupil are able to maintain a lower mill rate but that is not always the case. He said several school districts with a higher than average taxable valuation per pupil also have a higher than average general fund levy in mills.

Chairman Urlacher called on committee counsel to review a bill draft [70102.0100] to allocate school district property tax relief funds. Committee counsel said the bill draft was prepared based on suggestions of several committee members.

Committee counsel said the first section of the bill draft provides an appropriation of \$74,054,859 to the Tax Commissioner for allocation of school district property tax relief for the 2007-09 biennium. He said the bill draft specifies that \$35,897,132 is to be allocated in the first year and \$38,157,727 is to be allocated in the second year of the biennium.

Committee counsel said Section 2 of the bill draft provides the means of allocation of the funds to school districts. He said the bill draft requires determination of an adjusted combined education mill rate for each school district. He said the combined education mill rate is defined as the combined number of mills levied by a school district for the general fund and for an elementary, rural, or nonoperating school district, the number of mills levied for high school tuition and high school transportation. He said high school tuition and high school transportation levies are unlimited by statute. He said any excess levy authority approved by voters after 2006 would be excluded from the combined education mill rate. He said the bill draft requires subtracting from the combined education mill rate an unspecified percentage of the maximum number of mills that may be levied by a school district under NDCC Section 57-15-14. He said the bill draft amends that section to provide a declining maximum number of mills to be levied and a percentage of that number of mills would allow for a declining number of mills to be subtracted in determining the adjusted combined education mill rate. He said the effect of the adjusted combined education mill rate is that whatever base level number of mills is chosen for subtraction is the number of mills that must be levied by a school district before any property tax relief will be allocated. He said if the adjusted combined education mill rate is

zero for a school district, the bill draft provides no allocation of property tax relief.

Committee counsel said the next step in the allocation formula under the bill draft requires applying the adjusted combined education mill rate for the school district to the final equalized taxable valuation of property in the school district. He said this will determine the number of dollars in property taxes for each school district which is eligible for application of the property tax relief. He said the adjusted combined education levy in dollars for all school districts is totaled and divided into the amount for each school district to determine the percentage of total property tax relief funds to be allocated to the school district.

Committee counsel said subsection 5 of Section 2 of the bill draft is an optional provision that would allocate greater property tax relief to school districts with below average taxable valuation per pupil. He said this subsection requires that the statewide average taxable valuation per student be divided by the average taxable valuation per student within the school district to derive an adjustment factor. He said school districts with below average taxable valuation per student will have a factor greater than one which would be multiplied times the school district property tax relief allocation for the school district. He said if a school district's taxable valuation per student is higher than the average, that school district would have a factor of less than one, which would reduce the allocation. He said there is a wide range of taxable valuation per student among school districts, with some many times the statewide average and some being only a small fraction of the statewide average. He said the bill draft contains blanks that would need to be filled in if limitations are to be provided on the high and low ends of the allowable adjustment factors for school districts.

Committee counsel said the bill draft requires the Tax Commissioner to certify to each school district by August 1 the amount of school district property tax relief to be allocated to that school district for the next budget year. He said the school district budget and levy must be complete by August 15 and may be amended until October 10.

Committee counsel said Section 3 of the bill draft amends NDCC Section 57-15-01.1 to remove school districts from the existing statute that allows taxing districts to maintain a levy in dollars equal to the levy in the highest of the most recent three years, subject to adjustments. He said school districts have been removed from this section because special adjustments would be required for school districts with allocation of property tax relief funds. He said Section 4 of the bill draft creates a new Section 57-15-01.2, which applies only to school districts and would allow a levy in dollars based on the highest levy in the most recent three taxable years. He said the most significant difference between this new section for school districts and the existing section for all taxing districts is that this new section requires the base year levy in dollars to be adjusted

by subtracting the amount of school district property tax relief to be allocated to each school district for the budget year. He said a further adjustment is needed and that the amount of property tax relief to be subtracted for levy purposes must be adjusted by the amount of any school district property tax relief allocation that was included in the base year.

Committee counsel said the bill draft amends NDCC Section 57-15-14. He said the section currently allows a school district levying fewer than 185 mills to increase its levy in dollars by up to 18 percent until the cap of 185 mills is reached. He said the bill draft would overstrike the 18 percent increase and substitute an undetermined percentage increase to be allowed after property tax relief funds are allocated. He said the bill draft also reduces the 185-mill limit to 175 mills for taxable year 2007 and 165 mills for taxable year 2008 and beyond. He said this section of law also provides authority for school districts to obtain voter approval for a specific number of mills exceeding the statutory limit or for voter approval of an unlimited school district mill levy. He said the amendments in the bill draft would eliminate authority for voter approval of unlimited levies. He said this may not be interpreted to eliminate existing unlimited levies and additional language would be needed if that is desired. He said the authority for voter approval of a specific number of excess mills would be amended to allow voter approval of an unspecified percentage number of mills more than the maximum number of mills the school district may levy. He said the existing section contains different provisions for school districts having a population of more than 4,000 or less than 4,000. He said the only significant difference after the amendment would be that school districts of more than 4,000 would require a majority vote for approval of an excess levy and school districts of less than 4,000 would require a 55 percent majority vote for approval of an excess levy.

Committee counsel said Section 6 of the bill draft would require that when an amount to be levied is determined, the budgeted amount must be reduced by the amount of a property tax relief allocation before the property tax levy is determined.

Committee counsel said Section 7 of the bill draft provides a statement of legislative intent and requires a Legislative Council study. He said the bill draft specifies that the shift in education and taxation policy initiated by this bill draft would increase the state's share of elementary and secondary education funding from 47 percent in 2006 to 70 percent in 2014. He said the intent statement states that accomplishing this goal will require additional funding of approximately \$82 million for the 2009-11 biennium, \$86 million for the 2011-13 biennium, and \$75 million for the 2013-15 biennium. He said the funding percentages and dollar amounts are the amounts that were included in the estimates considered by the committee at the previous meeting for a four-biennium funding shift to a greater share of state funding for

education. He said the intent statement also requires the Legislative Council to assign a study in each interim through 2012 for the interim committee on taxation issues to consider compliance with and future funding for the shift in education and tax policy initiated by the bill draft.

Representative Williams said the bill draft calls for a 70 percent state share of elementary and secondary education funding as was the basis for the four-biennium funding shift reviewed by the committee at the previous meeting. He said the bill draft calls for allocation of funding to school districts on the basis of general fund, tuition, and transportation levies. He asked whether the four-biennium calculation of 70 percent funding was based on the combination of these three levies. Mr. Jerry Coleman, Department of Public Instruction, said the four-biennium funding shift to a 70 percent share of state funding was based only on general fund levies.

Representative Schmidt asked whether the bill draft would address the issue of the mill deduct used in the education funding formula. Committee counsel said the bill draft would not address the mill deduct or any other part of the education funding formula. Representative Schmidt said the mill deduct needs to be addressed by the other groups studying other education funding issues.

Representative Headland said a question to consider for committee members is whether a maximum taxable valuation per pupil should be used to limit property tax relief.

In response to a question from Senator Cook, committee counsel said reviewing the statistics provided by the Department of Public Instruction shows that a high taxable valuation per pupil does not always result in a lower than average mill rate for a school district.

Senator Urlacher said the bill draft is intended to be a starting point for committee discussion. He said it will be necessary for the committee to make decisions on the numbers and percentages to fill in the blanks in the bill draft. He said it will be necessary to insert amounts in these blanks to allow the Tax Department and Department of Public Instruction to analyze the effect of the bill draft for individual school districts.

Senator Andrist said he likes the fact that the bill draft provides an appropriation for property tax relief without tax increases. He said he is uncomfortable with the statement of intent including dollar amounts of future revenue enhancements. Senator Urlacher said he shares that concern but the amounts shown in the intent statement are the amounts determined to be necessary for future bienniums to complete the education funding shift under the four-biennium funding shift proposal considered by the committee at the previous meeting.

Representative Haas said over the years, the criticism has been that the Legislative Assembly has no long-range plan for elementary and secondary education funding. He said that was the reason for

the four-biennium funding shift proposal. He said whether the Legislative Assembly can comply with future additional state funding needs to accomplish the goal will be a decision for future Legislative Assemblies. He said the intent statement only sets the goal to achieve the four-biennium funding shift proposal.

Chairman Urlacher asked whether committee members have any suggestions for filling in the blanks contained in the bill draft.

Senator Cook said the public has not had an opportunity to see this bill draft before today. He said committee members and the public will need time to react to this proposal.

Senator Wardner said he would like to see an analysis of a range of percentages and numbers to be inserted in the bill draft. He said this would allow committee members a better opportunity to understand the effect of the amounts inserted in the blanks in the bill draft.

Representative Gulleon said the bill draft is rather complex and she would like to have a summary of each section of the bill draft e-mailed to each committee member so it could be provided to local school officials for consideration.

Representative Bellew said the Governor has entered an agreement to provide \$60 million of new funding for elementary and secondary education. He asked whether this bill draft would increase new funding for education to \$134 million. Committee counsel said the agreement entered by the Governor calls for \$60 million of enhanced funding for education. He said the bill draft is a different approach because it would not provide \$74 million of enhanced funding. He said the bill draft would allocate \$74 million of state funds to school districts but would also require school districts to reduce property tax levies, so most of the amount allocated by the bill draft would not result in a net gain of revenue for school districts.

Representative Mueller said the bill draft does not go beyond 2008 in its effect on school district funding. He said perhaps the bill draft should go farther than simply providing a statement of intent regarding future funding.

Representative Haas said it is important to remember that this bill draft represents a first step to providing permanent property tax relief for taxpayers. He said anything done in the 2007 Legislative Assembly can be undone in future Legislative Assemblies and decisions will have to be made in each legislative session based on conditions existing at that time.

Representative Herbel said it should be remembered that the bill draft is essentially a tax rebate to taxpayers from surplus state tax collections. He said future funding decisions will be addressed as time goes on and conditions allow. He said it is important for the Legislative Assembly to take this first step in reducing reliance on property taxes to fund elementary and secondary education.

Representative Belter said the intent statement in the bill draft states that the goal of the shift in funding is to achieve a 70 percent share of funding from state sources. He said he is not sure that is the appropriate level of the state's share of education funding.

Senator Andrist said a group of community newspapers conducts polls on various topics. He distributed copies of the May 31, 2006, *The Journal* from Crosby. He said the topic of the poll reported in this issue is whether readers of these community newspapers would prefer to lower property taxes by raising other taxes. He said in the 10 communities in which the poll was conducted, 67 percent of respondents said they like the state property tax system the way it is and in the Crosby community, 84 percent of respondents said they like the state property tax system the way it is.

Representative Weiler said there are some unanswered questions regarding the approach in the bill draft. He said one question is where the money will come from to accomplish the shift in funding over four bienniums. He said the bill draft does nothing to limit valuation increases so he is concerned about whether property tax relief will last. He said another issue that should be remembered is that the bill draft will not provide property tax relief for all property owners.

Senator Wardner said it is true that property valuation increases are not addressed in the bill draft. He said he agrees that this issue should be addressed but it needs to be separately addressed in other legislation.

Representative Herbel agreed with Senator Wardner that valuation increases should be addressed. He said it is also important to remember that the bill draft will reduce the maximum mill rate for most school districts from 185 to 165 mills and even if valuation increases are not limited, it is better to be taxed at 165 mills than to be taxed at 185 mills.

Representative Schmidt said he believes this bill draft is a start in reducing property tax burdens that should be made.

Representative Wrangham said education funding is an extremely complicated topic but the basic problem is budget control at the local level. He said this bill draft will not provide permanent property tax relief because it only provides for allocation of funds for one biennium.

After the luncheon recess, Chairman Urlacher asked if committee members have any suggestions on percentages and numbers to include in the blanks in the bill draft.

Representative Williams said he would like to see an approach that would enhance education funding equity. He said the Legislative Assembly has tried for years to achieve funding equity for students. He said it does not appear appropriate to use state average mill levies as a funding basis because only 20 of 204 school districts levy more than the average. He said if the Legislative Assembly is to provide tax relief,

it must be based on relief for levies for over 185 mills to address equity.

Senator Tallackson said this is a complicated issue and if a single percentage or number is chosen for each blank in the bill draft, it will not provide enough information for the committee to make adjustments. He said it would be more useful to choose a range of percentages and numbers for the blanks in the bill draft so the committee can observe the effect of using different factors. **It was moved by Senator Tallackson, seconded by Senator Wardner, and carried on a voice vote that the chairman work with the Legislative Council staff to develop a range of percentages and numbers to be inserted in the blanks in the bill draft to provide the committee examples of how these amounts would impact allocations.** Representative Conrad said the mill levy amounts chosen should include 185 mills and the statewide average of 199 mills.

Committee counsel said one blank in the bill draft for which a range of choices would not affect a run on the allocations for school districts is the limitation of annual percentage increases in school district levies for districts under 185 mills. He said it would be useful to insert a limit on increases if the committee desires an increase rate of less than 18 percent annually. Representative Haas suggested that an appropriate limitation would be two percentage points above the annual Kansas City Consumer Price Index.

Representative Belter said he does not like use of consumer price indexes in tax policies. He said he would prefer a fixed percentage rate.

Representative Haas said that for purposes of discussion, an amount should be inserted in the bill draft. **It was moved by Representative Haas, seconded by Representative Weiler, and carried on a recorded roll call vote that a limitation of two percentage points more than the consumer price index be applied as a percentage increase limitation for school districts levying below 185 mills.** Voting in favor of the motion were Senators Urlacher, Tallackson, and Wardner and Representatives Conrad, Drovdal, Gulleeson, Haas, Hanson, Herbel, Onstad, Owens, Schmidt, and Williams. Voting in opposition to the motion were Senators Andrist, Cook, and Tollefson and Representatives Bellew, Belter, Headland, Mueller, and Weiler.

Senator Cook requested preparation of an amendment for Section 7 of the bill draft relating to legislative intent. He said the amendment should state the intent that the objective of property relief is to reach a maximum level of three-fourths of one percent of true and full value as a maximum property tax. He requested that an estimate be obtained on how much replacement revenue that would require.

Representative Belter suggested that the limitation suggested by Senator Cook should be applied to all property. Senator Cook said an estimate should be obtained of how much revenue would be required to extend the limitation to all property.

Chairman Urlacher called on Representative Owens for presentation of suggestions for consideration by the committee for constitutional amendments and legislative changes relating to property tax relief. A copy of Representative Owens' prepared presentation is attached as Appendix D.

Representative Owens said he believes issues that must be addressed go beyond property tax reduction and increasing state funding for education. He said economic development considerations should also be included in committee recommendations. He said one aspect of low unemployment is that employers will observe that there is a shallow workforce pool and high residential property taxes discourage young people from staying in the state to find employment because property taxes may equal one-fourth or more of a monthly house payment. He said he has listened to the debate on property tax relief issues during the 2005 legislative session and the deliberations of this committee and his proposals are the product of deliberation on the concerns and discussions he has heard on these issues.

Representative Owens said his proposal is based on four cornerstones. He said the four cornerstones include property tax relief, controls on the growth of property taxes, tax law reconstruction, and elementary and secondary education funding.

Representative Owens said he would apply six rules to any recommended constitutional or legislative changes. He said the six rules are:

1. Property tax reduction must be meaningful.
2. No changes to current methods of computing property tax or determining mill levies.
3. No increase in income tax.
4. Constitutional amendments for both the property tax reduction and property controls.
5. Enhanced funding for elementary and secondary education.
6. Suggested changes should be offered to, but leave education policy for, the Education Committee.

Representative Owens said with regard to the cornerstone on property tax relief, he would recommend a constitutional amendment to provide a homestead property tax exemption of 40 percent of the entire tax bill but not exceeding the total amount of property taxes levied by the school district. He said the homestead credit should apply only for owner-occupied residences and farms or ranches. He said the exemption should also be allowed for family-owned and family-operated farm businesses conducted as a corporation, limited liability company, or similar legal entity, if all shareholders are North Dakota residents having common kinship. He said he estimates this reduction would reduce property taxes by approximately \$97 million. He said he estimates that property taxes currently represent 28 to 31 percent of monthly house payments. He said a 40 percent reduction in education property taxes would reduce property taxes to 15 to 19 percent of house payments.

Representative Owens said the second cornerstone of his proposal would be a constitutional amendment to limit growth of property taxes. He said the constitutional amendment would provide that beginning in 2009, total property taxes assessed against a residence could not increase by more than 5 percent in one year or the rate of inflation for the urban Midwest plus three-fourths of one percentage point, whichever is less. He said this limitation would not apply to the value of new construction and when property is sold, a new assessment of the property would be allowed. He said he would recommend that voters of a taxing district could allow an excess increase in taxes by a 60 percent majority vote.

Representative Owens said another aspect of his cornerstone relates to tax controls on the growth in city and county sales taxes, which make it more difficult for the Legislative Assembly to consider changes to state sales tax policies. He said he would recommend that political subdivisions of the state be limited to a maximum cumulative local sales tax of 2 percent and a limitation should be imposed so revenues from local sales taxes could not be used to replace property taxes or provide education funding.

Representative Owens said the third cornerstone of his proposal is reconstruction of tax laws. He said he would recommend repeal of the farm home property tax exemption. He said this would be contingent upon approval of the 40 percent homestead property tax credit. He said with the homestead credit applied to the value of agricultural property, most farmers would see a significant property tax reduction even if the farm home is subject to property taxes. He said it would also be necessary to generate a substantial amount of new revenue at the state level. He said he does not have specific recommendations for revenue increases but options for consideration would be a real property transfer fee, cigarette tax increases, and elimination of selected sales and use tax exemptions.

Representative Owens said that the net effect of the suggested changes for elementary and secondary education funding is a significant property tax reduction with replacement revenue plus \$34 million in enhanced funding for education. He said if the 40 percent homestead property tax credit is phased in with 10 percent additional credit each year for four years, additional funding of \$55 million per year would be required.

Representative Owens said he requested preparation of two resolutions for constitutional amendments and two bill drafts. He said the first House concurrent resolution [73013.0100] would create a constitutional provision to allow the owner of a homestead to claim a property tax credit against the total amount of property taxes due, with the discount for early payment of taxes, or the entire amount levied on the homestead by school districts, whichever amount is less. He said the amount of the credit would be 10 percent for taxable year 2009, 20 percent for taxable year 2010, 30 percent for taxable year

2011, and 40 percent for taxable years after 2011. He said the measure provides that a homestead is a dwelling occupied by the owner as a primary dwelling place plus up to one acre of land surrounding the dwelling. He said a homestead could consist of part of a structure containing multiple dwellings or part of a structure containing a dwelling and used in part for other purposes. He said for a farm or ranch residence occupied as a homestead, the credit would apply to the residence and all agricultural land in a single tract or contiguous tracts on which the residence is located.

Representative Owens said the second House concurrent resolution [73014.0100] would amend the constitution to limit property tax increases by a taxing district against a parcel of residential or commercial property to not more than 5 percent or the amount of the increase in the consumer price index plus three-fourths of one percentage point, whichever is less. He said the measure would allow a vote of 60 percent or more of the electors of a taxing district to allow a greater tax increase.

Representative Owens said the first bill draft [70110.0100] would limit the combined sales, use, and gross receipts taxes imposed by counties or cities under home rule authority to not more than a 2 percent combined rate on any taxable sale.

Representative Owens said the second bill draft [70112.0100] would eliminate the farm residence property tax exemption. He said one oversight in the bill draft is that it was supposed to be contingent upon approval by the voters of the constitutional measure to provide a homestead credit against agricultural property.

UTILITY SHAREHOLDERS OF NORTH DAKOTA

Chairman Urlacher called on Mr. Bob Graveline, Utility Shareholders of North Dakota, Bismarck, for comments on a study commissioned by the group. Mr. Graveline said he requested time from the chairman to present the study findings to the committee for informational purposes. He said Utility Shareholders of North Dakota hired Covenant Consulting Group as a consultant to review utility property taxes in North Dakota. He introduced Mr. Rod Backman, Covenant Consulting Group, Bismarck, for presentation of the report.

Mr. Backman said Covenant Consulting Group was retained by Utility Shareholders of North Dakota to review effects of property taxes as paid by utilities to local taxing districts. He said the emphasis of the study was to determine differences in property taxation between a rural electric cooperative and an investor-owned utility. He said in the study, attention was focused on Bismarck and Dickinson.

Mr. Backman said property tax application is substantially different for rural electric cooperatives and investor-owned utilities. He said rural electric cooperatives are subject to a 2 percent gross receipts tax instead of a property tax, except for taxes on land.

He said the rural electric cooperative gross receipts taxes are allocated to each county based on miles of transmission line located within each county as compared to the entire system. Within a county, taxes are allocated among taxing districts also using miles of line as the basis. He said investor-owned utilities pay property taxes subject to central assessment by the state of North Dakota and taxable value of a utility's property is subject to mill levies of taxing districts in which the property is located.

Mr. Backman said the analysis was based on computation of the amount of taxes that would be paid on rural electric cooperative property if the property were owned and operated by an investor-owned utility. He said under this analysis the investor-owned utility tax would be over nine times greater than the tax paid by the rural electric cooperative for a property in Bismarck. He said the study found that the Bismarck School District could have collected an additional \$143,780 from an investor-owned utility for property that is owned by a rural electric cooperative. He said analysis of data and estimates for Dickinson show a smaller ratio of investor-owned utility to rural electric cooperative taxes but analysis and conclusions are the same. He said the conclusion of the study is that in Bismarck and Dickinson, the cities and school districts would receive significantly more property tax dollars if the area within those taxing districts currently served by a rural electric cooperative were served by an investor-owned utility or if the rural electric cooperatives were taxed in the same manner of an investor-owned utility. A copy of the report is on file in the Legislative Council office.

Representative Wrangham said the Electric Industry Competition Committee has been examining tax equity in the state for investor-owned utilities and rural electric cooperatives over several years. He said that committee has not reached a consensus on how to address these tax issues. Mr. Backman said this study was presented for consideration by the Electric Industry Competition Committee.

Senator Cook asked committee counsel if he is correct in understanding that true and full valuation per pupil data for school districts does not reflect rural electric cooperative property and gross receipts taxes. Committee counsel said that is correct and because rural electric cooperative property is subject to payments in lieu of property taxes under the gross receipts tax, rural electric cooperative property is not assessed except for land. In response to another question from Senator Cook, committee counsel said investor-owned utility property is subject to assessment and is included in true and full valuation per pupil data. Senator Cook said this situation complicates equity issues among school districts because some school districts receive revenue from rural electric cooperative gross receipts taxes but that revenue is not reflected in the information the committee has been studying.

Senator Tallackson questioned why the presentation by the Utility Shareholders of North

Dakota was presented to the committee without an opportunity for rural electric cooperative representatives to attend and present their side of the issues. Chairman Urlacher said he would welcome a response from representatives of rural electric cooperatives if they wish to address the committee.

Senator Cook said he would also welcome a response from rural electric cooperative representatives as to why their property or gross receipts taxes should not be reflected in taxable valuation per student for funding purposes or reflected in the mill deduct factor under the foundation aid allocation formula.

LEVIES IN MILLS STUDY

Chairman Urlacher called on committee counsel to review a bill draft [\[70035.0100\]](#) considered by the committee at the previous meeting relating to information that must be included with annual property tax statements. Committee counsel said the bill draft has not been changed since it was reviewed by the committee at the previous meeting. He said the bill draft relates to the annual property tax statement provided to taxpayers by the county treasurer. He said current law requires only that the tax statement must include the true and full value of the property and the total mill levy applicable. He said the bill draft expands the information that must be included in, or provided with, the annual property tax statement. He said the true and full value of the property would be required to be provided for the immediately preceding taxable year and for the taxable year to which the tax statement applies. He said the bill draft would also require information to show, for each taxing district levying taxes against the property and the consolidated levy by all taxing districts levying against the property, the taxes levied in dollars for the preceding year, the taxes levied in dollars for the taxable year to which the tax statement applies, taxes expressed in dollars of taxes per \$1,000 true and full value of the property for the preceding taxable year, and taxes expressed in dollars of taxes per \$1,000 of true and full valuation of the property for the taxable year for which the tax statement applies.

Committee counsel said he was requested to meet with representatives of the North Dakota Association of Counties to discuss alterations to the approach in the bill draft that would be as compatible as possible with tax software systems already in use by counties. He said he has discussed these issues and Mr. Traynor would provide testimony relating to these issues.

Chairman Urlacher called on Mr. Traynor for testimony relating to the study of changes to property tax statements. A copy of Mr. Traynor's testimony is attached as Appendix E.

Mr. Traynor said the association is conducting a survey that is not yet complete regarding current property tax statements and tax software used by counties. He said counties already provide substantially more information on tax statements than

is required by the statutory provision. He said all 26 counties that have so far responded to the survey provide taxpayers with a breakdown of current property tax dollars levied by major taxing district.

Mr. Traynor said county officials can see the value in providing information to contrast current and prior year property taxes to allow comparison of taxes levied by major taxing districts. He said requiring this information would affect formatting of software but is not seen as problematic as adding information based on dollars of taxes levied per \$1,000 of true and full value. Mr. Traynor said attached to his testimony is a "mockup" of a real estate tax statement showing how information could be inserted to show prior year and current year comparison of true and full value and taxes imposed by major taxing districts.

Mr. Traynor said if inclusion of prior year comparisons is to be required on real estate tax statements, allowances will be needed in situations in which comparison of two years could be unavailable, inaccurate, or confusing. He said these situations include properties that are subdivided from one year to the next, properties that become tax-exempt or lose exempt status, property in a new political subdivision, property with a change in homestead credit status, property annexed into a different taxing district, property that has a change in classification from one year to the next, and properties with a new home or new business exemption.

Committee counsel asked whether information requirements for property tax statements like the "mockup" statement attached to Mr. Traynor's testimony would be a major cost item for counties. Mr. Traynor said he is not certain, but some programming changes are needed each year so perhaps these changes could be incorporated and not result in a significant cost increase.

Representative Owens said he does not disagree with the suggestions made in Mr. Traynor's presentation but he would like to keep the requirement for a statement of property taxes per \$1,000 true and full valuation. Mr. Traynor said addition of this information would complicate programming. Representative Owens said he would not object to dropping the requirement of information for the preceding taxable year if that would allow retaining the requirement for statement of taxes per \$1,000 of true and full valuation.

Representative Bellew said he would prefer to receive the previous and current year information on the tax statement. He said he thinks that would be more useful to taxpayers.

It was moved by Representative Owens, seconded by Representative Conrad, and carried on a voice vote that the bill draft be amended to require information for the current taxable year only and retain the required statement of property taxes per \$1,000 of true and full valuation.

STREAMLINED SALES TAX GOVERNING BOARD

Chairman Urlacher said Senator Cook serves as president of the Streamlined Sales Tax Governing Board. He called on Senator Cook for an update on the Streamlined Sales Tax Governing Board's activities. Senator Cook distributed a copy of the first annual report of the Streamlined Sales Tax Governing Board. A copy of the report is attached as Appendix F.

Senator Cook said the Streamlined Sales and Use Tax Agreement was activated on October 1, 2005. He said during the first few months of operation, the Streamlined Sales Tax Governing Board has been extremely active. He said the board has elected officers and appointed committees; appointed a full-time executive director; and provided for selecting, evaluating, and contracting with certified service providers. He said when the agreement was activated, there were 13 member states and 5 associate states. He said since that time, Nevada has also been approved as an associate member and he understands that Vermont, Washington, Hawaii, and Puerto Rico will be applying for membership.

Senator Cook said a very significant recent development is entering contracts with three certified service providers effective June 1, 2006. He said the Streamlined Sales Tax Governing Board has approved a compensation schedule for certified service providers, which is outlined in the report. He said agreement was difficult to achieve on the compensation schedule but the board believes the compensation schedule is a compromise that will be fair to states and certified service providers.

COMMITTEE DISCUSSION

Chairman Urlacher said it is important to move the committee's work forward. He said it will be necessary to provide percentages and numbers for the unspecified amounts in the property tax relief bill draft. He said he will work with the Legislative Council staff to select a range of percentages and numbers for each variable in the bill draft to allow analysis to be done of the effect of different percentages and numbers. He said he hopes the committee can complete its work in two more meetings. The meeting was adjourned at 3:05 p.m.

John Walstad
Code Revisor

[ATTACH:6](#)