

NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

FINANCE AND TAXATION COMMITTEE

Wednesday, August 2, 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, Michael A. Every, Harvey Tallackson, Rich Wardner; Representatives Larry Bellew, Wesley R. Belter, Kari Conrad, David Drovdal, Pam Gulleson, C. B. Haas, Lyle Hanson, Craig Headland, Gil Herbel, Ronald A. Iverson, Phillip Mueller, Kenton Onstad, Arlo E. Schmidt, Dave Weiler, Clark Williams, Dwight Wrangham

Members absent: Senator Ben Tollefson; Representative Mark S. Owens

Others present: See Appendix A

Representative Lois Delmore and Senator David O'Connell, members of the Legislative Council, were also present.

It was moved by Senator Tallackson, seconded by Representative Bellew, and carried on a voice vote that the minutes of the July 19, 2006, committee meeting be approved as distributed.

ELECTRIC UTILITY PROPERTY TAXES

Chairman Urlacher called on committee counsel who said letters were addressed to the committee by representatives of Xcel Energy, Inc., and Otter Tail Power Company to provide comments of those companies relating to testimony received by the interim Finance and Taxation Committee at the two previous meetings regarding electric industry tax issues. Copies of the letters are on file in the Legislative Council office.

EDUCATION PROPERTY TAX RELIEF STUDY

Chairman Urlacher called on committee counsel to review a revised bill draft [\[70102.0300\]](#) to provide property tax relief through allocations to school districts. Committee counsel said four changes were made to the bill draft after the previous committee meeting. He said the first two changes are made on page 1, line 24, of the bill draft. He said the first change is replacing use of the previous year's mill rate for school districts with use of the 2005 taxable year mill rate. He said the second change on that line is to insert use of 60 percent of the statutory maximum number of mills that may be levied by a school district as the basis for determining the adjusted combined education mill rate under the allocation formula.

Committee counsel said the third change is made on page 7, lines 3 through 6, in which the deduction from a school district property tax levy is made for the amount of a property tax relief allocation only to the extent the allocation exceeds the amount of any school district property tax relief allocation received in the base year. He said this change is necessary to avoid a cumulative effect of reductions, which in the second year would make the reduction almost twice as much as the amount of relief allocation.

Committee counsel said the fourth change to this bill draft is a sentence added to the intent statement in Section 7 providing a statement of intent that the Act will produce a reduction in property tax burdens which, with continued efforts of future Legislative Assemblies, will result in reduction of annual property tax bills to not more than one and one-half percent of the true and full value for any parcel of residential property.

Committee counsel said the changes to the bill draft would make the bill draft consistent with the estimated effect reviewed at the previous meeting for a 60 percent adjusted levy cap. A copy of that estimate is attached as Appendix B.

Committee counsel said there are some items that the committee may wish to consider for amendment. He said on page 2, line 9, it is provided that the previous year's taxable valuation of property is used to apply the combined education mill rate. He said the combined education mill rate would be "frozen" in the 2005 taxable year by one of the changes added to the bill draft and the committee may wish to consider whether to freeze the 2005 taxable valuation for application of the mill rate. He said if the taxable valuation is not frozen in 2005, changes in valuation with a frozen mill rate will either increase or decrease the amount of property tax relief for a school district. He said a similar problem exists on page 2, lines 20 and 21, in referring to taxable valuation per student for purposes of the adjustment, the average taxable valuation per student will change each year and the committee may wish to consider whether to freeze the taxable valuation per student adjustment in the formula for the 2005 school year. He said the final point for consideration is the effective date clause of the bill draft. He said the bill draft is effective beginning with the 2007 taxable year and the committee may wish to consider whether to add a sunset clause to expire the statutory changes after

two years because the appropriation is provided only for two years.

Representative Belter said the intent language added to Section 7 of the bill draft is limited to residential property, which he believes was a mistake. He said the stated goal of reducing property taxes for residential property would have the effect of shifting property taxes to other property types.

In answer to a question from Senator Tallackson as to whether anything in the bill draft would affect the mill deduct factor used in the foundation aid allocation formula, committee counsel said nothing in the bill draft would affect the mill deduct.

Representative Guleson asked for an explanation of the effect of reducing the statutory mill levy cap from 185 to 165 mills for school districts. Committee counsel said this reduction in the statutory mill levy cap would not require any school district to reduce its property tax levy. He said school districts have the option of levying based on mills under North Dakota Century Code (NDCC) Section 57-15-14 or basing levy limits on the highest amount in dollars levied in the most recent three years under Section 57-15-01.1. He said a school district levying 185 mills would not have to reduce its levy to 165 mills because it could use the provisions of Section 57-15-01.1 to retain a levy equal to the highest amount levied in dollars in the most recent three years. He said the only significance in reducing the statutory mill levy cap to 165 mills is that under the bill draft, only school boards levying below the statutory mill levy cap would have authority to increase property tax levies. He said current law allows those school districts to increase levies by up to 18 percent each year until they reach the statutory mill levy cap and the bill draft would reduce the statutory mill levy cap to 165 mills and reduce the annual allowable levy increase from 18 percent to 2 percentage points more than the percentage increase in the consumer price index.

Representative Delmore asked how many school districts currently have unlimited levy authority. Mr. Jerry Coleman, Department of Public Instruction, said he believes there are currently three school districts that have unlimited levy authority.

Representative Mueller asked what would happen under the bill draft if the mill levy deduct in the foundation aid formula is not addressed. Committee counsel said the committee chose the approach in the bill draft to avoid recommending changes to the foundation aid allocation formula. He said the committee anticipates that the Governor's Commission on Education Improvement or the interim Education Committee could make recommendations for changes in the foundation aid formula for purposes of enhanced education funding and the committee chose not to interfere with that possibility. He said if enacted the bill draft should not interfere with any recommendations from either of those groups which might provide enhanced school funding.

Representative Haas asked whether there is any chance to reduce funding to school districts after two

years if the provisions in the bill draft do not expire. He said he wants to be sure the committee understands how the optional levy limitation in dollars would apply. Committee counsel said under NDCC Section 57-15-01.1, allowing a levy based on dollar amounts levied in the three previous years, a school district can reach back up to three years to use the highest amount levied in dollars as a basis for calculating the current levy limitation. He said because the bill draft is effective only for two years, a school district would still be able to reach back to a property tax year in which no property tax relief allocation was received and use the amount levied in that year as the basis for computing its levy in 2009. He said this should not force any funding reduction if property tax relief allocations are not continued.

Representative Headland said in reviewing the property tax relief allocations provided by the bill draft, he became concerned about the fairness of the allocation because approximately 38 percent of all of the property tax relief allocation goes to the cities of Fargo and Bismarck and those two school districts have only about 22 percent of the students in the state. He said the high cost of education per student in Bismarck and Fargo is the product of voters allowing unlimited levy authority and that is a local decision that should not require all taxpayers in the state to contribute to providing property tax relief. He said he believes it would be more equitable to limit the allocations to school districts receiving 5 percent or more of the total amount available for statewide allocation so that the percentage of the total allocation for any school district could not exceed that school district's percentage of statewide student enrollment. He distributed copies of an amendment [\[70102.0301\]](#) he had prepared to limit school districts accordingly. He also distributed copies of a revised run showing the effect of the proposed amendment on allocations under the bill draft. A copy of the run showing the effects is attached as Appendix C.

Representative Williams asked why 5 percent of total funding was chosen as the point at which to apply the limitation based on percentage of students. Representative Headland said he believes the limitation should apply only to the largest school districts and 5 percent was chosen because it will apply the additional limitation only to the four largest recipients of property tax relief.

Representative Belter asked whether the districts that would receive a reduced allocation under the amendment would still have the same total revenue for budget purposes. Representative Headland said the school districts would still have the ability to generate the same amount of total revenue but would receive a reduced amount of property tax relief.

Representative Conrad said Minot is one of the four school districts that would be subject to the additional limitation. Representative Headland said that is correct but Minot actually benefits by the change because Minot has a greater percentage of

students in the state than it does of the allocation under the bill draft.

Senator Cook said his first thought in considering the bill draft was that a greater share of property tax relief should go to areas of greatest tax effort. He said he likes the approach in the proposed amendment because the bill draft would provide one-third or more of available property tax relief funds to school districts that have had unlimited levy authority and he believes it would be appropriate to spread the property tax relief more evenly across the state.

It was moved by Representative Headland and seconded by Senator Cook that the committee adopt the proposed amendment to the property tax relief bill draft to limit school districts receiving 5 percent or more of total allocations to a percentage of total allocations not exceeding the school district percentage of statewide student enrollment.

Representative Iverson said he does not support the bill draft and he opposes the amendment. He said the amendment would be unfair to Fargo and Bismarck School Districts by substantially reducing their shares of property tax relief allocations.

Representative Headland said reviewing the printout showing effects of the proposed amendment for the school districts shows that Fargo would still receive 20 mills of property tax relief after the amendment while his school district would receive about 17 mills of property tax relief.

Representative Gulleson said reviewing the effects of the amendment makes her believe that the amendment would serve the purpose of spreading property tax relief more equitably among school districts.

Senator O'Connell said another issue for consideration is that the city of Fargo and Cass County provide discretionary property tax exemptions for over \$1 billion of property.

The question was called and **the motion carried**. Voting in favor of the motion were Senators Urlacher, Andrist, Cook, Every, Tallackson, and Wardner and Representatives Bellew, Drovdal, Gulleson, Haas, Hanson, Headland, Herbel, Mueller, Onstad, Schmidt, Williams, and Wrangham. Voting in opposition to the motion were Representatives Belter, Conrad, Iverson, and Weiler.

Senator Cook said he believes it would be appropriate to use 2005 taxable valuation of property to apply the 2005 combined education mill rate for school districts. **It was moved by Senator Cook, seconded by Senator Every, and carried on a roll call vote that the bill draft be amended by replacing the word "previous" on page 2, line 9, with the words "2005 taxable."** Voting in favor of the motion were Senators Urlacher, Andrist, Cook, Every, Tallackson, and Wardner and Representatives Bellew, Belter, Conrad, Drovdal, Gulleson, Haas, Hanson, Headland, Herbel, Mueller, Onstad, Schmidt, Weiler, Williams, and Wrangham. Voting in opposition to the motion was Representative Iverson.

Senator Cook said it was not intended to cause a property tax shift by including the intent statement about reducing property tax bills to no more than one and one-half percent of true and full value of property. **It was moved by Senator Cook, seconded by Representative Haas, and carried on a roll call vote that the bill draft be amended by removing the word "residential" on page 10, line 24.** Voting in favor of the motion were Senators Urlacher, Andrist, Cook, Every, Tallackson, and Wardner and Representatives Bellew, Belter, Conrad, Drovdal, Gulleson, Haas, Hanson, Headland, Herbel, Iverson, Mueller, Onstad, Schmidt, Weiler, Williams, and Wrangham. No negative votes were cast.

Senator Cook said that with regard to the question of locking in the taxable valuation per student for purposes of the adjustment formula, it might be advisable to use the approach that is already in the bill draft which would reflect updated valuation per student numbers each year. He said this would allow the relief allocations to reflect the large impact of locating a new facility in a school district.

Representative Belter said the committee should be aware when considering increased state funding to political subdivisions that the state already has a large commitment, totaling over \$1 billion for the 2005-07 biennium, for allocations to political subdivisions. He distributed copies of a report of major state appropriations and revenue allocations for direct assistance to political subdivisions from 1995 through 2007. A copy of the report is attached as Appendix D. He said the report illustrates the substantial growth from 1995 to 2007 in state appropriations and revenue allocations to political subdivisions.

Representative Gulleson said Representative Belter makes a good point and state assistance to political subdivisions has increased in recent years. She said it is also important to recognize that there have been sharp increases in property taxes over the same years so there is justification for providing property tax relief.

TESTIMONY

Mr. Cory Fong, Tax Commissioner, commended the committee for its work on the issue of property tax relief. He said he is pleased that the Tax Department staff has been able to assist the committee in gathering information and he hopes the information provided was useful to the committee.

Mr. Fong said while traveling in North Dakota, the issue on the minds of many citizens which has been expressed to him is the need for property tax relief. He said he agrees that property tax relief is appropriate to maintain balance in the tax system.

Mr. Fong said taxable sales in North Dakota have grown substantially. He said total state and local tax collections grew 16 percent in the year ending June 30, 2006. He said the growth in the state economy provides the Legislative Assembly an opportunity to allocate meaningful and responsible property tax relief among North Dakota citizens.

Mr. Fong said the Tax Department stands ready to continue providing assistance during the interim and during the 2007 legislative session as work continues on property tax relief issues.

Mr. Brent Edison, candidate for Tax Commissioner, said as he has traveled throughout the state the No. 1 issue he has heard raised is the need for property tax relief. He said he believes there is a demand among citizens for more property tax relief than the four-biennium property tax relief plan the committee has been working on. He said he would like to see more property tax relief in the bill draft under consideration and he suggested that efforts should be made to achieve better coordination with education funding recommendations that will be coming from the Governor's Commission on Education Improvement.

Mr. Douglas Johnson, North Dakota Council of Educational Leaders, Bismarck, said 2005 House Bill No. 1512 was an effort to provide enhanced funding for education and property tax relief. He said during this interim, the committee objective of enhanced funding has been lost and only property tax relief remains in the bill draft under consideration. He said property tax relief is important but education funding equity and adequacy must also be addressed and should be given greater priority than property tax relief.

Senator Cook said 2005 House Bill No. 1512 contained a substantial tax increase, which was a large part of the reason it failed to pass. He said when the property tax relief provided by the committee bill draft is considered with the anticipated \$60 million education funding enhancement from the Governor's Commission on Education Improvement, there is a possibility for a substantial increase in state funding for education. He asked whether the combined effect of these recommendations would be supported by the North Dakota Council of Educational Leaders. Mr. Johnson said the funding enhancement would be welcomed but the property tax relief bill draft does not result in any gain for school districts.

Representative Herbel said he believes 2005 House Bill No. 1512 should not be characterized as a tax increase but rather as a tax shift. He said the bill would have shifted about \$570 million from property taxes to state tax sources.

Representative Schmidt said as a legislator, he hears many requests for property tax relief. He asked whether Mr. Johnson thinks education funding appropriations other than this bill draft will provide education funding enhancements. Mr. Johnson said the Governor's Commission on Education Improvement is anticipated to recommend \$60 million of enhanced funding. He said the North Dakota Council of Educational Leaders does not believe that is enough enhanced funding. He said that amount of funding would begin to address issues of equity in school funding but would not get to the issue of adequacy of education funding.

Chairman Urlacher said during the committee study, the committee has tried to reach a recommendation that would provide property tax relief but not overlap or interfere with any forthcoming recommendations for enhanced education funding from the Governor's Commission on Education Improvement or the interim Education Committee.

Ms. Bev Nielson, North Dakota School Boards Association, said the School Boards Association would like to get out from under the current level of property tax burden but the association envisions a three-part effort to improve funding for education. She said the first step in education funding improvement is to provide equity of funding among school districts. She said this issue is now being addressed by the Governor's Commission on Education Improvement. She said the second step in improving education funding is providing adequacy of funding for school districts. She said this should be the next focus of funding efforts after equity is addressed. She said the third step to improving education funding should be property tax relief but this should not be addressed until equity and adequacy have been improved.

Ms. Nielson said the committee bill draft being considered would restrict the ability to levy property taxes for school districts before addressing equity and adequacy of funding and would leave school districts in a difficult situation to meet education funding needs. She said the School Boards Association would also like to see stable funding sources from the state for education. She said North Dakota should avoid situations like those that have arisen in Minnesota, where property tax relief is provided when state tax collections are healthy but those allocations are cut off when state revenues are not adequate.

Representative Gulleason asked if the School Boards Association has amounts in mind that would be required to address education funding adequacy. Ms. Nielson said the Augenblick study called for \$240 million additional funding to support education at an adequate level.

Mr. Woody Barth, North Dakota Farmers Union, said the Farmers Union supports the bill draft as amended. He said the Farmers Union believes there are two primary goals in the area of property taxes, which include property tax relief and moving toward a 70 percent level of state funding for education. He said this bill draft would help in both respects. He said the bill draft is a step in the right direction and the Farmers Union hopes this property tax relief would be sustainable in the future. He said the bill draft would provide meaningful property tax reductions and the Farmers Union looks forward to working with the Legislative Assembly on this issue during the legislative session.

Representative Williams said Dr. David Smette, Superintendent, Jamestown Public Schools, is present and he would like to hear Dr. Smette's observations on the committee discussion. Chairman Urlacher called on Dr. Smette who said he thinks the concerns of the North Dakota School Boards

Association are also of concern to him. He said stability of revenue for schools is very important. He said reconsideration should be given to the 185-mill cap on school district levies. He said that cap has been in place for many years and it should be reconsidered in light of increased costs of education. He said he recognizes that the bill draft being considered is targeted to property tax relief but he believes it is important to coordinate the interim Finance and Taxation Committee recommendation with efforts of the Governor's Commission on Education Improvement to reach goals of enhanced equity and adequacy of funding before providing property tax relief.

It was moved by Senator Cook and seconded by Representative Drovdal that the bill draft, as amended, relating to providing property tax relief through allocations to school districts be approved and recommended to the Legislative Council.

Representative Iverson said he would like to restate his opposition to the bill draft. He said the amendment to reduce the allocation of property tax relief to the Fargo School District further increases his opposition to the bill draft.

Senator Andrist said he has had concerns that the bill draft allocates most of the property tax relief to school districts that have had undisciplined spending resulting in higher mill rates. He said he is also concerned about whether it is appropriate to put \$75 million into school district property tax relief with no added funding for schools. He said the Governor's Commission on Education Improvement appears likely to recommend another \$60 million of state spending for education and he is not sure the total of the two recommendations would be affordable for the state. He said he believes there should be an evolution in school funding but not a revolution. He said he believes this bill draft is a revolution in school funding and that it will have unintended consequences.

Representative Conrad said she believes a higher threshold of tax effort should be required to receive property tax relief. She said this could be accomplished by allocating property tax relief only for school districts levying more than 185 mills. She said she requested a run to illustrate the effects of this change and it was prepared by the Department of Public Instruction. She distributed copies of the run to illustrate the changes. A copy is attached as Appendix E.

Representative Weiler said reduction of property taxes is a worthwhile goal. However, he said, no funding source is dedicated to the \$75 million required and he does not believe the property tax relief will be sustainable. He said he also does not believe the property tax relief is equally allocated among school districts.

Representative Williams said it is important to remember that the committee determined to confine its efforts to property tax relief because other groups

were looking at ways to enhance education funding. He said during the upcoming legislative session, the bill draft will be changed and reconciled with enhanced funding considerations. He said he would support approval of the bill draft as a basis for a property tax relief concept and discussion of education funding issues during the legislative session.

Chairman Urlacher said the committee has gone through a thorough process to study possible funding sources and education funding levels to gain a greater understanding of the issues involved in the tax structure and education funding. He said whether or not property tax relief is enacted, the information will serve committee members well during the legislative session.

Representative Herbel said he has heard concerns expressed that a small number of schools would receive too large a share of property tax relief funding. He said the amendment adopted by the committee will help with that criticism and spread property tax relief more evenly across the state. He said if \$74 million appropriated by the bill draft from the state general fund is not returned to taxpayers in the form of property tax relief, it will get spent on something else which will call for further sustained funding. He said property tax relief is a very important issue. He said work is needed from both sides of the aisle during the legislative session but property tax relief must be addressed and this bill draft is a suitable vehicle for that process.

Representative Gulleason said when the Legislative Assembly considers significant changes, concerns are raised. She said she believes the efforts of this interim committee have been worthwhile and although the bill draft may not be perfect at this point, it provides a good basis for legislative session consideration of the issue of property tax relief.

Representative Wrangham said he agrees that the committee has had a good exploration of issues relevant to tax and education funding issues whether or not the bill draft is recommended.

Senator Andrist said he does not believe a bill draft should be recommended just because it can serve as a basis for legislative discussion. He said whether or not the committee will endorse the bill draft in its current form is the issue.

Representative Belter said the comments from the Council of Educational Leaders and the School Boards Association should be noted by committee members. He said political subdivisions must recognize that the state is not an unlimited source of funding. He said efficiency of local government must be encouraged. He said he does not support the bill draft but he compliments those who have brought this issue forward for discussion. He said one of his concerns is that as the states assume a greater share of education funding, there will be increased pressure to increase state taxes.

The question was called and **the motion carried.** Voting in favor of the motion were Senators Urlacher,

Cook, Every, Tallackson, and Wardner and Representatives Bellew, Drovdal, Gullerson, Haas, Hanson, Headland, Herbel, Mueller, Onstad, Schmidt, and Williams. Voting in opposition to the motion were Senator Andrist and Representatives Belter, Conrad, Iverson, Weiler, and Wrangham.

Representative Haas requested that committee counsel send copies of the amended bill draft and supporting documents to committee members.

It was moved by Representative Belter, seconded by Representative Herbel, and carried on a voice vote 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 and that the meeting be adjourned sine die.

The meeting was adjourned at 12:10 p.m.

John Walstad
Code Revisor

[ATTACH:5](#)