

NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

FINANCE AND TAXATION COMMITTEE

Tuesday, November 15, 2005
Roughrider Room, State Capitol
Bismarck, North Dakota

Senator Herb Urlacher, Chairman, called the meeting to order at 9:00 a.m.

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

Members absent: Senator Michael A. Every; Representatives Larry Bellew, Ronald A. Iverson, Mark S. Owens

Others present: See Appendix A

It was moved by Representative Drovdal, seconded by Representative Haas, and carried on a voice vote that the minutes of the August 10, 2005, committee meeting be approved as distributed.

EDUCATION FUNDING AND PROPERTY TAX STUDY

Concept Paper

Chairman Urlacher said a motion was approved at the previous committee meeting to prepare a concept paper to serve as a guideline for committee efforts to obtain information on the education funding and property tax study. He called on Representative Haas for comments relating to the preparation of the concept paper. Representative Haas said he provided information to the Legislative Council staff for preparation of the concept paper. He said the concept paper is intended to provide direction to committee requests for information and research. He said the points listed in the concept paper are not final committee decisions but are intended to provide a starting point for committee discussion of the information needed to complete the committee study. He said the directive to the committee was to examine options to enhance education funding and reduce reliance on property taxes. Chairman Urlacher called on committee counsel to review a memorandum entitled [Concept Paper for Committee Consideration Regarding Property Tax Reduction and Enhanced State Funding for Elementary and Secondary Education](#). Committee counsel said the

memorandum sets out six primary considerations for committee discussion and there are bullet points associated with each primary consideration to identify information the committee needs to obtain and determinations the committee will have to make to properly address the primary considerations.

Committee counsel said the first primary consideration calls for analysis of the results if elementary and secondary education funding is shared 70 percent by the state and 30 percent by school districts, excluding consideration of federal funding. He said the memorandum states that total cost of education is based on Fund Group 1 expenditures as identified in *School Finance Facts* as prepared by the Department of Public Instruction. He said it will be necessary to determine the estimated cost of elementary and secondary education state-wide for the 2007-08 and 2008-09 school years.

Committee counsel said that the second primary consideration listed in the concept paper calls for determination of property tax savings that might result and how those savings would be equitably allocated among taxpayers. He said there are several associated questions that must be addressed, including how to assure that property tax savings will be received and maintained, how to avoid creating incentives for current or future tax increases, how school district property tax levies will be limited and how to add a growth factor to keep the 70-to-30 ratio, whether allocation of property tax savings could be used to equalize school funding, and whether to allow voter approval of excess levies. He said the next primary consideration is to determine whether school spending growth can and should be limited and whether there is an index of education costs that would be appropriate to use for that purpose. He said the next primary consideration calls for a two-year hold harmless funding floor for school districts.

Committee counsel said the fifth primary consideration in the concept paper relates to examination of appropriate means of meeting the added funding responsibility of the state from the potential shift in education funding. He said this will require examination of state tax rates, exemptions, and burdens and how they compare to neighboring states. He said this requires consideration of relative

reliance on the "big 3" taxes--property, income, and sales.

Committee counsel said the final primary consideration in the concept paper relates to how the 70-to-30 funding model could be maintained in the future if it is initially established. He said consideration should be given to how future budget requests for education funding will be initiated and how and to whom reports on funding compliance and future cost estimates should be directed.

Representative Haas said there is an added issue that should probably be considered regardless of funding sources. He said allocation of state funds to school districts is critical and the decision must be addressed as to whether to use the allocation formula now in place with the mill deduct and weighting factors or to go to use of another method, such as an adequacy-based formula.

Senator Tollefson asked how property taxes became the basis for education funding. Committee counsel said before 1919 there were no income or sales taxes imposed by the state and property taxes were the funding source for education. He said North Dakota's current tax structure is built on the foundation established by imposition of property taxes. Senator Tollefson said he believes the element of local control was a large part of education funding through the property tax and he believes the property tax should continue to be a basis of education funding to provide local control of education.

Representative Herbel said the issue of local control versus providing state aid for education is a large part of the issue this committee is addressing. He said the committee will need to debate those issues in the future.

In response to a question from Representative Guleson, committee counsel said if the committee chooses to pursue the 70 percent state funding level as described in the concept paper, the committee would still have to address the issue of allocation of state aid either on the basis current state aid is allocated or on a different basis that could include many factors to address equity or adequacy of funding.

Senator Cook said the committee study involves consideration of two major issues--property tax reform and education funding. He said if the state funds 70 percent of elementary and secondary education costs, the question arises concerning what decisionmaking authority shifts from local control to state control. He said it appears the Education Committee and Finance and Taxation Committee have a shared interest in the committee study. He said it might be necessary for any major changes to be the product of joint work from these two committees. He asked Representative Haas whether he believes the Education Committee would have a role in any proposed education funding and property tax reform recommendations. Representative Haas

said there must be communication with the interim Education Committee and the Education Committee should at least be informed of the activity of the Finance and Taxation Committee.

Senator Andrist said if the 70 percent funding is based on current spending levels of school districts, it would reward school districts currently spending at a higher level. He said a question must be considered about the appropriate level of education spending in which the state will participate.

Representative Schmidt said several school districts have a pending lawsuit against the state. He said he would like to see those school districts back off on the lawsuit until this committee completes its study.

Representative Haas said legislators have known for years that the education funding formula is flawed. He said he believes the committee should move forward with its study without consideration of the pending lawsuit.

Senator Andrist said he believes the Legislative Assembly must cure education funding inequities with new dollars and not by shifting money from one district to another.

Representative Haas said if the Legislative Assembly keeps the same distribution formula that currently exists, the adequacy and equity issues will not be addressed and there will be winners and losers among school districts. He said state aid distribution decisions become complex when adequacy and equity issues are included.

Senator Cook said he believes the concept paper merits testimony from interested parties and consideration by the Education Committee. Senator Urlacher said input from the Education Committee would be welcomed.

Representative Mueller said he believes it would be appropriate for the committee to work on these concepts and gather the suggested information, whether or not the concept paper is adopted.

Senator Tallackson said he sees no harm in adopting the concept paper as a committee study approach. He said the concept paper just sets out what needs to be determined during the committee study. **It was moved by Senator Tallackson and seconded by Representative Williams that the Finance and Taxation Committee adopt the concept paper as a starting point in its education funding and property tax study.** Representative Haas said it would be appropriate to adopt the concept paper as a starting point. He said the concept paper would not limit committee considerations and there will be many more issues for consideration as the committee moves forward.

Representative Belter asked what would be accomplished by adopting the concept paper. He said if the concept paper is not adopted, the committee would still continue to study the issues.

Chairman Urlacher said he views the concept paper as a guide to lay out issues on which information must be gathered and presented to the committee.

It was moved by Senator Cook and seconded by Representative Herbel that the motion be amended to add that the concept paper also be forwarded for consideration to the Education Committee.

Representative Haas said the concept paper is a framework for gathering information to move the committee toward its study goals. He said it is not a final action and more considerations are appropriate as the study proceeds. He said he believes the concept paper should be considered by the Education Committee.

Representative Belter said he believes it might be necessary to obtain approval from the Legislative Council chairman to communicate this concept paper to the Education Committee.

Senator Cook withdrew his motion to amend and Representative Herbel withdrew his second to that motion.

The question was called regarding the motion to adopt the concept paper and **the motion carried on a voice vote.**

TAX DEPARTMENT PRESENTATIONS

Chairman Urlacher called on Mr. Cory Fong, Tax Commissioner, for comments relating to information requested from the Tax Department staff for the committee. Mr. Fong said the Tax Department staff prepared a substantial amount of information for this committee meeting which would be presented by Ms. Kathy Strombeck, Research Analyst; Ms. Marcy Dickerson, State Assessments Supervisor and Property Tax Division Director; and Mr. Gary Anderson, Income, Sales, and Special Taxes Division Director.

Ms. Strombeck distributed copies of her prepared testimony, a copy of which is attached as Appendix B.

Ms. Strombeck said she was requested to provide information on the "three-legged stool" of state property, income, and sales tax collections. She said over the past 30 years property tax collections have increased at a greater rate than sales or income taxes. She said over the past 20 years residential property tax collections have increased at a greater rate than agricultural, commercial, or centrally assessed property.

Ms. Strombeck reviewed information compiled from a survey by the Tax Department comparing property taxes on a \$70,000 home and a \$100,000 home in selected cities in North Dakota, South Dakota, Montana, and Minnesota.

Ms. Strombeck reviewed a comparison done by the city of Washington, D.C., to compare income, property, sales, and automobile taxes at various income levels for the largest city in each state. She

said from the information in this survey, North Dakota fares very favorably with income tax burdens, moderately well with sales tax burdens, and is higher than the national average burden in property taxes.

In response to a question from Senator Cook, Ms. Strombeck said the sales tax data in the report does not include local sales taxes.

Representative Gulleon said the "three-legged stool" has gotten out of balance in North Dakota with a growing reliance on property taxes. She asked if Ms. Strombeck can point out factors that have caused this situation. Ms. Strombeck said she cannot specify all of the factors that have influenced this change but one implication is that local funding needs have grown faster than funds to local government from state or federal sources.

Representative Belter asked Ms. Strombeck whether it is possible to provide a breakdown to illustrate what level of local government is receiving the revenue from the rapid increase in property tax collections for residential property. Ms. Strombeck said it should be possible to provide information on those issues.

Representative Herbel said it appears from the data presented that residential property taxes have really exploded since 1993. He asked whether the reasons can be identified for this increase.

Representative Mueller asked whether factors can be identified that contribute to the reduction of agricultural property taxes as a percentage of total property taxes. Ms. Strombeck said there has been a loss in the number of farms but that land has been absorbed by other farmers and remains taxable. She said undoubtedly the most significant factor is the large and rapid growth in valuation of residential commercial property in the state due to both new construction and increased values of existing property.

Senator Andrist asked if it would be possible to provide an inflation-adjusted comparison of the data on income, sales, and property taxes levied over the past 30 years. Ms. Strombeck said she can provide that information.

Representative Wrangham requested statistics on the increase in the number of commercial property parcels.

Representative Headland asked whether it is possible to break out the nonresident ownership of agricultural land. Ms. Strombeck said Ms. Dickerson could provide the committee information on what is known about nonresident ownership.

Chairman Urlacher called on Ms. Dickerson. Ms. Dickerson distributed copies of her prepared testimony, a copy of which is attached as Appendix C. Ms. Dickerson said she was requested to estimate tax savings to property owners if there were a 10 percent statewide property tax reduction and how much of that benefit would go to nonresident property owners. She said a 10 percent reduction to 2004 property

taxes levied would amount to a tax savings of \$61,806,569. She said a survey that received responses from 29 counties based on 2003 property taxes showed 7.22 percent of property taxes were billed to nonresidents. She said the survey found that 90 percent of nonresident-owned property was agricultural property. She said that if centrally assessed property is also considered to be nonresident-owned property, another 6.8 percent of property taxes is paid by nonresidents. She said that based on these estimates approximately 14.02 percent of property taxes is paid by nonresidents and nonresidents would receive \$8,665,281 in property tax relief if a 10 percent reduction totaling \$61,806,569 is provided to all taxpayers.

Ms. Dickerson said she was also requested to provide information on how local assessors may adjust valuation of agricultural property to account for the impact of adverse weather. She said weather is a component of the valuation formula for agricultural property and the effects of this year's weather will be reflected in future years' county average agricultural value per acre. She said if weather conditions result in land being inundated to an extent making it unsuitable to grow crops or graze farm animals for two consecutive growing seasons or more, a statutory provision provides for that land to be valued at 10 percent of the average agricultural value per acre of noncropland for the county. She said weather conditions are not to be used as a modifier of agricultural property values. She said modifiers are not cyclical conditions and weather is cyclical. She said it is possible to modify valuations for wet conditions if those conditions are excessive for the type of soil.

Senator Tallackson said some of the property that shows up as being owned by nonresidents belongs to parents whose children farm the land. Ms. Dickerson said determination of nonresidents' ownership is inexact because it is based only on where the tax statement is mailed.

Representative Hanson asked whether it would be possible to provide detailed information from the 29 counties that responded to the survey request on ownership of property by nonresidents. Ms. Dickerson said more detailed information could be provided.

Representative Herbel said the 7.22 percent ownership of property by nonresidents includes all property types and he asked whether it would be possible to get this information for only agricultural land. Ms. Dickerson said it would be necessary to survey counties to obtain that information.

In response to a question from Representative Mueller, Ms. Dickerson said the estimate of 7.22 percent of property taxes paid by nonresident ownership was based on the average determined from a survey of 29 counties but that percentage was

applied to statewide statistics as the best available means of estimating property taxes paid by all nonresidents.

Representative Gulleon said the value of obtaining these statistics is significant because the apparent trend is an increase in nonresident ownership of agricultural property.

Representative Herbel asked whether use of modifiers in valuation of agricultural property is allowed by statute. Ms. Dickerson said use of modifiers is not a statutory provision but is based on an Attorney General's opinion and use of modifiers is discretionary with local assessment officials.

Senator Cook asked whether it would be possible to put the 2004 information on the chart presented by Ms. Strombeck showing historical property, income, and sales tax collections. Ms. Dickerson said it should be possible to update that information.

Senator Cook said in considering relative property tax burdens of agricultural and residential property, if all other factors remain constant and interest rates rise, there is a shift in property tax burden from agricultural property to residential and commercial property. Ms. Dickerson said that is correct. Senator Cook said interest rate changes will also affect taxable valuation per student for education funding purposes.

Senator Andrist asked why centrally assessed property has not experienced much increase in property taxes. Ms. Dickerson said since 1998 telecommunications property is not subject to property taxes because a gross receipts tax was imposed by 1997 legislation in lieu of property taxes. She said that revenue is allocated like property taxes but does not show up in the statistics. She said in the 1980s North Dakota lost the authority to impose personal property taxes on railroads.

Representative Herbel said he would hope the committee does not focus on differing amounts of reductions for certain property types.

Representative Schmidt said he believes the sharp increase in residential property taxes could have a lot to do with migration in recent years of people from farms to cities. Ms. Dickerson said that probably has a considerable effect on the data.

Chairman Urlacher called on Mr. Anderson. Mr. Anderson presented testimony and statistics on revenue effects of sales and use tax exemptions and the impact of sales tax rates and exemption differences on cross-border shopping. A copy of the statistical information and comparisons distributed by Mr. Anderson is attached as Appendix D.

Mr. Anderson said the data on revenue effect of sales and use tax exemptions is being updated and will probably be available for the next committee meeting.

Mr. Anderson said determination of influences on cross-border shopping are very difficult. He said the information presented shows general state sales and

use tax rates for North Dakota, Minnesota, South Dakota, Wyoming, and Montana. He said the information shows the taxable or exempt status of individual products or services. He reviewed the information on sales tax imposition on services among the 50 states.

Senator Cook said the Legislative Assembly debated expanding North Dakota sales and use tax bases to match the tax base in South Dakota. He said information should be obtained on the revenue effect of expanding the North Dakota sales and use tax bases to tax services and products taxable under South Dakota law.

Ms. Strombeck presented testimony on tax year 2004 income tax returns for which there was no net tax liability. A copy of her prepared testimony is attached as Appendix E. She said 68,852 returns had zero net tax liability which represents approximately 22 percent of the total individual income returns filed.

AGRICULTURAL LAND VALUATION

Chairman Urlacher called on Mr. Dwight Aakre, Department of Agribusiness and Applied Economics, North Dakota State University, for testimony relating to the operation of the property tax valuation formula for agricultural property. A copy of the information distributed by Mr. Aakre is attached as Appendix F.

Mr. Aakre said valuation and assessment of agricultural land for property tax purposes is determined by operation of a formula intended to determine the capitalized average annual gross return for the land. He described the data used to determine annual gross return for cropland and grazing land and the adjustment for irrigated land production. He said production data is gathered for the most recent 10 years and the high- and low-production years are dropped and the remaining 8 years are averaged. He said the landlord's share of gross return is divided by the capitalization rate to derive land valuation.

Mr. Aakre said the National Agricultural Statistics Service gathers data based on acreage for each crop grown and summerfallow in each county, yield per acre for each crop, and price for each crop. He reviewed determination of value of rangeland and pastureland based on livestock-carrying capacity.

Mr. Aakre said one question that always arises is how conservation reserve program (CRP) land impacts the property valuation formula. He said the Farm Services Agency provides the number of acres enrolled in the CRP program by county and the total CRP program payments made in each county. He said one-half of the total CRP payments are entered as gross revenue from CRP. He said government program payments other than CRP payments are also provided by the Farm Services Agency and entered in the computation. Mr. Aakre said the capitalization rate used in the formula is based on the Agribank rate of interest for the most recent 12 years, with the high year and the low year dropped out, and the remaining

10 years averaged to determine the capitalization rate. He said the 2003 Legislative Assembly amended the capitalization rate formula to set a minimum rate of 9.5 percent and in 2005 again amended the capitalization rate formula to set a minimum rate of 8.9 percent for 2006 and 8.3 percent for subsequent years. For 2005, he said, this resulted in a capitalization rate of 8.9 percent, which would have been 7.73 percent without the statutory changes setting a minimum capitalization rate.

Mr. Aakre reviewed how the cost of production index in the formula is determined.

Mr. Aakre said the projected trend in agricultural property values under the formula is for a decrease of 1 to 2 percent per year. He said interest rates are likely to remain low for several years, resulting in the minimum capitalization rate being used in the formula. He said the cost of production index is expected to increase by 2 to 3 percentage points each year. He said a rising cost of production index puts downward pressure on land values. He said large increases in 2005 prices for fuel, fertilizer, and other inputs will be reflected in the model for the 2007 assessment.

Representative Herbel said in some counties the soil type of the land is the determining factor in whether it is considered cropland or noncropland and the actual use of the property is not considered. He asked whether Mr. Aakre believes the actual use of the property should be the basis for assessment. Mr. Aakre said in his opinion, the actual use of the property should be the basis for assessment but others would disagree with that opinion because the use of the property is a management decision. Senator Cook asked whether it is possible to obtain a comparison of market value of agricultural property compared to valuation of agricultural property under the valuation formula. Ms. Dickerson said she could provide data on that issue for the committee. After the luncheon recess, Ms. Dickerson distributed copies of a chart from the recently completed 2005 sales ratio study. A copy of the table is attached as Appendix G. Ms. Dickerson said the table shows a comparison of actual sales price per acre for agricultural land in the state with true and full value of the property as determined under the valuation formula. She said the column showing median ratio is the percentage determined by dividing the formula valuation by the actual sales price per acre. She said the table shows that for 1,390 agricultural sales, the assessed valuation under the formula is 57.5 percent of the average sales price per acre statewide for agricultural land.

Senator Cook said the information on the table shows a wide variance among counties of approximately 40 to 90 percent of the comparison of assessed value to sales prices. He asked whether it would be possible to determine why the range is so wide between assessed valuation and sales price among counties.

Senator Andrist asked whether comparisons are based on taxable valuation or market valuation when discussions focus on poor versus rich districts for school funding purposes. Senator Cook said poor versus rich school district comparisons are based on taxable valuation per student.

DEPARTMENT OF PUBLIC INSTRUCTION

Chairman Urlacher called on Mr. Tom Decker, Director of School Finance, Department of Public Instruction, for a presentation of information requested by the committee. Mr. Decker said the department was requested to provide a substantial amount of information. He said representatives of school districts would begin the presentation of information on school funding issues.

Mr. Mark Lemer, Business Manager, West Fargo School District, said he was requested to provide the committee a walk-through of the school district budgeting process. A copy of an overview of the budgeting process prepared by Mr. Lemer is attached as Appendix H.

Mr. Lemer said the budget process is an 18-month effort for each school year. He said the process is initiated by developing a five-year budget projection, which is followed by development of preliminary budget numbers for all accounts for the school year. He said state law requires adoption of the school district budget by August 15 but the West Fargo School District sets a target of July 15 to finalize budget figures for all accounts. He said October 10 is the deadline set by statute to finalize adjustments to the property tax levy for the school district. He said a major budget revision is completed in November to reflect the actual mill levy for the school year, adjusted foundation aid allocations, and salary negotiations.

Mr. Lemer said the budget process begins with establishment of budget parameters through the school district administration. He said teaching staff and school principals review and make recommendations on budget items. He said budget parameters are used to develop the budget book, which lays out items of budget input and each input request receives hearings and a decision by the school district administration. He said some of the items in the budget book must be based on estimates for items such as federal funding to be received and similar uncertain amounts. He said the preliminary budget established in July does not have salary increases for staff included because that information is not available until November.

Mr. Lemer said he was requested to provide information relating to ending general fund balances. He said the West Fargo School District has adopted a target range of 7.5 to 10 percent of expenditures as an ending balance. He said experience has shown that this amount is necessary because property tax

revenue does not begin to become available to a school district until the period from January to March.

Mr. Lemer distributed and reviewed copies of the West Fargo School District budget projections for 2004 through 2010.

Mr. Gordon Davis, Superintendent, New Salem School, reviewed how the New Salem School District budget is established. A copy of an overview of the budget process distributed by Mr. Davis is attached as Appendix I.

Mr. Davis said the budget process for the New Salem School District is a continual process. He said he is constantly making budget notes as things arise that must be reflected in the budget for the school year. He reviewed the budget process and the procedures to establish the 2005-06 budget adopted by the New Salem School Board.

Senator Cook said it appears the New Salem School District carries an ending fund balance of approximately 22 percent and he asked why the amount is that high. Mr. Davis said the New Salem School District is a relatively small district with a smaller than average budget. He said the goal is to maintain an ending fund balance of 15 to 20 percent. He said in past years, the district has not been able to meet its funding needs for the last two months of the school year which makes it necessary to borrow funds. He said because the budget is smaller, it is necessary to maintain a larger ending fund balance because unexpected costs can have substantial impact on the budget and the district wants to avoid the added expense of borrowing money.

Mr. Joe Sykora, Business Manager, Jamestown Public School District, reviewed the budget process followed by Jamestown Public School District. A copy of an overview of the budget process prepared and distributed by Mr. Sykora is attached as Appendix J.

Representative Mueller asked whether the Jamestown Public School District has determined the cost to the district of implementing the No Child Left Behind Act. Mr. Sykora said no dollar amount of cost to the district per se has been determined.

Mr. Brian Nelson, Superintendent, Lewis and Clark School District, presented information on budgeting and the consolidation process he experienced in the consolidation of Berthold, North Shore, and Plaza School Districts into the Lewis and Clark School District. Representative Gulleon asked whether the incentive bonus provided by the state for consolidation is a major influence. Mr. Nelson said the incentive bonus is a major influence for some districts. He said in the Lewis and Clark School District consolidation, some of the preexisting districts gave property tax rebates to taxpayers.

Representative Gulleon asked what the biggest obstacles are to school district consolidation. Mr. Nelson said communities would like to maintain independent school districts and the people involved in districts to be consolidated do not work with or

know one another so there can be problems that must be overcome in working together on a consolidation project.

Mr. Decker distributed and reviewed budget information prepared by administrators of the reorganized Mott-Regent School District. A copy of the prepared testimony is attached as Appendix K. The testimony describes cost-savings resulting from reorganization in administration, teachers, and operations and maintenance.

Senator Cook asked whether school district reorganization allows some districts to refund balances to taxpayers while other districts are required to bring their existing fund balance into the new district. Mr. Decker said that is correct. He said contributions of preexisting districts are based on the lowest balance among participating districts, determined on a per student basis, and districts with any amount exceeding that lowest balance amount are allowed the option of refunding the excess amount to taxpayers.

Dr. Don Piper, University of North Dakota, said he has about 20 years of experience working with approximately 50 school districts on efforts to make education more efficient and to enhance education opportunities. He said consortiums were an effort by the Legislative Assembly to achieve efficiency in education. He said consortiums incorporated about five or six school districts. He said these arrangements received funding for up to three years but this approach did not result in many school district reorganizations. He said school district reorganization results in consolidation of school districts under one school board and one superintendent. He said reorganization has proven successful in saving school expenses in many instances.

Dr. Piper said as a practical matter, school districts will consider reorganization only if the districts are losing students or running out of money. If neither situation exists, it is unlikely that consolidation will occur.

Dr. Piper said if the goal of school districts is to significantly reduce costs, consortiums and joint powers agreements will not do that. He said reorganization is the only available option that will save significant costs for school districts.

Dr. Piper said school costs are approximately 75 to 85 percent personnel costs so any real reduction in education cost comes from reduced personnel needs. He said reduced personnel needs also result in recurring savings for school districts.

Dr. Piper said that to encourage reorganization of school districts he would recommend reinstating bonuses for reorganization but provide for reduction of the size of the student body for eligibility from 525 to 250. He said he would recommend graduated reorganization bonuses of \$250,000 for a 250-student-level reorganization, \$350,000 for a

350-student-level reorganization, and \$450,000 for a 450-student-level reorganization. He said he also recommends a public vote at any time of year, rather than the current limited timeframe, to approve reorganization. He said he also recommends making sure that reorganizing school districts would not lose state aid.

Representative Williams asked what happens with regard to transportation costs in school district reorganizations. Dr. Piper said in his experience, reorganizing districts have contracted with private companies to provide transportation service or looked into contracting with private owner-operators.

Representative Onstad asked whether plans are made to use buildings for another purpose when school buildings are closed as a result of reorganization. Dr. Piper said that is always an issue and in some cases the building may be used for office space or alternative uses.

Senator Andrisc said western North Dakota is more sparsely populated and he asked whether geographic size of an area may be too large for reorganization. Dr. Piper said the most advantageous size for reorganization is limited to 10 to 25 miles. He said a district any larger than that size would require too much transportation expense and there are no good options to solve that problem.

Mr. Jerry Coleman, Department of Public Instruction, reviewed several reports he prepared relating to education funding for the committee. He reviewed state and local shares of education funding in North Dakota and other states. He said state revenues in North Dakota account for approximately 37 percent of education funding. He said the average for the United States is approximately 49 percent state funding for education and within this region only South Dakota, at 34 percent, provides a lower proportion of education funding from state sources. He said Minnesota provides state revenues for 74 percent of education funding and Montana and Wyoming provide 46 percent and 51 percent, respectively.

In response to a question from Senator Cook, Mr. Coleman said the data on state funding for education on the chart includes school construction costs and that is why the North Dakota state share of funding is only 37 percent.

Mr. Coleman reviewed the state aid allocation formula for the 2005-07 biennium. He reviewed the supplemental payments to the school districts formula and 10-year enrollment statistics, taxable valuations, and instructional expenditures. He reviewed a 10-year history of enrollment and expenditures by category. He reviewed statistics on enrollment, taxable valuation per pupil, general fund levy, and education costs per pupil for each school district. He reviewed statewide school district financial report information for the 2004-05 school year. A copy of

the information provided by Mr. Coleman is attached as Appendix L.

Mr. Decker reviewed a study prepared for the Department of Public Instruction by Augenblick, Palaich and Associates, Inc. A copy of the report is attached as Appendix M.

Mr. Decker said the equity approach to school funding relies on allocation of equal dollars to each student. He said the adequacy approach bases allocation on the cost of providing educational adequacy for each student. He said the Augenblick study was commissioned to determine the cost of adequacy in education funding in North Dakota. He said there are different approaches to address the question and for North Dakota the professional judgment approach was chosen, which generally results in the highest cost result among all approaches. He said the report is based on six hypothetical school districts based on data from the 2001-02 school years. The report concludes that 2001-02 funding was approximately \$205.8 million underfunded to meet adequacy of funding considerations.

LEVIES IN MILLS STUDY

Chairman Urlacher called on committee counsel to review a memorandum entitled [*Property Taxpayer Bill of Rights Provisions of Other States Compared to North Dakota Law*](#). Committee counsel said the memorandum contrasts provisions of property taxpayer bill of rights provisions in Florida, Arkansas, New York, and Maryland with comparable North Dakota law. He said mailed notice of current assessments or increased assessments is required in Florida, Arkansas, New York, and Maryland but mailed notice is only required in North Dakota for an assessment increase of 15 percent or more and no notice is required if the increase is less than \$3,000. He said the states considered provide a statutory right to a conference with the assessor to review valuation determinations. He said the states reviewed require notice of the right to petition for appeal of an assessment decision. He said North Dakota law does not provide these rights by statute, although the right to seek review of an assessment exists and taxpayers would probably be allowed an opportunity for a conference with the assessor. He said the memorandum reviews the information that must be provided to taxpayers to allow them to understand valuation and tax imposition determinations. He said Maryland law provides a right for a taxpayer to obtain at no charge an assessment worksheet for the taxpayer's own property and the sales analysis for the area in which that property is located and, for a reasonable fee, copies of assessment worksheets for similar property.

COMMITTEE DISCUSSION AND DIRECTIVES

Chairman Urlacher requested committee counsel to review issues referred by the State Board of Equalization to the interim Finance and Taxation Committee. Committee counsel said the committee was informed at its previous meeting about discussions before the State Board of Equalization suggesting that limitations should be imposed on property assessment increases and property taxes in general. He said the committee did not provide directives on whether or not to take up those issues. Senator Cook said assessment levels and property tax issues are really a part of what the committee is already working on with regard to education funding and property tax relief.

Senator Cook said he believes the committee should obtain information on how much property tax relief would be provided to taxpayers if no taxpayer pays more than an annual property tax total exceeding 1.5 percent of true and full valuation of the property.

Representative Haas said with regard to issues of limiting assessments and property taxes, he does not believe state law should limit assessments because assessments should be determined by market value.

Representative Haas said examination of options should be undertaken to find an index of education costs as a basis for growth in education funding.

Senator Andrist said property taxes are local taxes and he believes complaints about property taxes should be made to local officials.

Representative Herbel said it seems to be a universal complaint of taxpayers that property taxes are too high and he believes the prime reason is the lack of adequate funding to schools.

Senator Tollefson said if the law does not cap valuation of property for tax purposes, tax revenues of political subdivisions can still increase without the necessity of raising the mill rate.

Senator Cook said he hopes that at the end of the interim this committee can move forward legislation. To reach that point, he said, several important decisions must be made, including how much money should be shifted from property taxes to state funding, how to distribute relief from the state to school districts, and where new money for education funding comes from. He said this is very deliberate work and the committee needs to keep gathering facts and considering options.

Representative Hanson said a survey should be conducted through county recorders to find the percentage of property owned by nonresidents. During the 1970s, he said, Representative Robert Reimers had a bill introduced to provide for state funding of certain components of education. He said that bill and its concepts should be reviewed by the committee.

Chairman Urlacher called on Ms. Sandy Clark, North Dakota Farm Bureau, Bismarck, for comments on the committee's study activities. Ms. Clark said the information reviewed by the committee based on property taxes paid by the four types of property indicates that residential property taxes have grown faster than agricultural property taxes. She said the Farm Bureau thinks too much property tax is imposed on all property types. She said the graph makes it appear that residential property tax burdens have risen faster than agricultural property tax burdens. She said the Farm Bureau believes it is more accurate to say that the residential property tax base has grown very fast since 1990, while agricultural property is still approximately the same acreage. She said the Farm Bureau believes growth in cities is a

great thing and there is a substantial increase in the value and cost of new homes and these are the primary reasons the data makes it look like residential property has had a faster growth in tax burden.

Chairman Urlacher said he plans to schedule the next committee meeting as soon as possible, perhaps in December.

The meeting was adjourned at 4:30 p.m.

John Walstad
Code Revisor

[ATTACH:13](#)