

NORTH DAKOTA LEGISLATIVE MANAGEMENT

Minutes of the

EDUCATION FUNDING AND TAXATION COMMITTEE

Tuesday, July 26, 2011
Harvest Room, State Capitol
Bismarck, North Dakota

Representative RaeAnn G. Kelsch, Chairman, called the meeting to order at 9:00 a.m.

Members present: Representatives RaeAnn G. Kelsch, Bette Grande, Craig Headland, Bob Hunskor; Senators Dwight Cook, Tim Flakoll, Joan Heckaman, Gary A. Lee

Others present: See [Appendix A](#)

At the request of Chairman Kelsch, committee counsel reviewed the [Supplementary Rules of Operation and Procedure of the North Dakota Legislative Management](#).

BACKGROUND - EDUCATION FUNDING

At the request of Chairman Kelsch, committee counsel presented a background memorandum entitled *State Involvement in the Funding of Elementary and Secondary Education - Background Memorandum* ([Appendix B](#)).

BACKGROUND - TAX REFORM

At the request of Chairman Kelsch, Mr. John Walstad, Code Revisor, Legislative Council, presented a memorandum entitled *Property Tax Reform and Relief - Background Memorandum* ([Appendix C](#)). Mr. Walstad said when the Legislative Assembly decided to become involved in the provision of property tax relief, various mechanisms were considered. He said there are only two kinds of taxing districts that everybody lives in--counties and school districts--and because some counties were levying zero mills for property taxes, school districts were the entity chosen as the vehicle for property tax relief.

Mr. Walstad said in 2009 the Legislative Assembly decided that the state would not replace dollars at the level that voters had approved in the case of certain school districts having unlimited taxing authority and that the state would not buy taxes down to zero mills in the case of school districts having only minimal taxing efforts. He said the mechanism chosen was based on a 185-mill levy limitation. He said it was decided that up to 75 mills of that amount would be bought down by the state. He said if a school district was levying 185 mills, its tax rate would become 110 mills. He said if a school district was levying more than 185 mills, the excess mills would remain a local responsibility. He said if a school district was levying fewer than 185 mills, the district would be bought down to 100 mills. He said the Legislative Assembly also eliminated the authority for voters to

approve an unlimited school district general fund levy. He said that bill has an expiration date of 2015. He said school districts could still seek voter approval for a mill levy increase, but it could not be for an unlimited amount. He said the number of mills would have to be stated, and the approval would be valid for only five years.

Mr. Walstad said in 2011 the property tax relief program was continued, and the pricetag went from \$295 million to \$341.8 million. He said the sustainability of the program, in light of property tax valuation increases, is being considered by the interim Taxation Committee. He said in 2011 the Legislative Assembly also provided that the grant to a school district cannot increase by more than the average percentage increase of valuation in the state. He said some school districts were experiencing enormous valuation increases, which would have generated substantially more relief money while at the same time allowing the districts to greatly diminish their general fund levies.

Mr. Walstad said when the 2009 legislation was put into place, the 2008 school district general fund levy was used as a basis. He said that is still being used, and it is being perceived as being inequitable. He said the interim Taxation Committee is looking at that as well.

In response to a question from Senator Cook, Mr. Walstad said in 1981 the state had to restructure the entire property tax system after a lawsuit. He said the most significant change was in the manner that agricultural land was assessed. He said the state went to a productivity formula rather than using a market value approach.

In response to a question from Representative Grande, Mr. Walstad said unlimited levy authority has been approved by the voters in Bismarck, Williston, and Grand Forks. He said Fargo's unlimited authority was in existence at the time the enabling legislation was enacted. However, he said, Fargo's unlimited levy authority was recently removed by its voters.

EDUCATION FUNDING FORMULA

At the request of Chairman Kelsch, Mr. Jerry Coleman, Director of School Finance, Department of Public Instruction, distributed a document entitled *School Finance Facts* (on file in the Legislative Council office). Mr. Coleman said page A-2 of the document sets forth the local, county, state, and

federal revenue sources as of June 2010. He said the state's share of education funding is now 62 percent. He said the state's share for the previous year was 47 percent. He said the difference is attributable to the property tax relief program.

Mr. Coleman said beginning July 1, 2007, the state's education funding formula combined numerous funding lines into one. He said the main funding formula is based on the number of students, i.e., a school district's average daily membership. He said additional weights are added to adjust for special characteristics, special programs, and school district size.

Mr. Coleman said there are 181 school districts. He said about 75 school districts are not subject to any further adjustments. He said, as for the others, equalization adjustments are made based on school district valuation and local revenues such as oil and gas revenues. He said those are considered imputed valuations per student. He said the ending fund balance offset is applied to all school districts carrying more than 45 percent of their annual expenditures. He said that amounts to a dollar-for-dollar reduction in a district's state aid.

Mr. Coleman said the mill levy reduction program provides school districts with up to 75 mills for levy buydowns. He said if a school district was levying 165 mills, its levy was reduced to 100 mills. He said if the district now raises its mills to 110, its new cap would be 175 mills, not 185 mills like other districts. He said this is being viewed as an inequity. He said the property tax reduction program now costs \$342 million. He said the cost increase is a result of property valuation increases. He said some property in Mountrail County has increased by as much as 80 percent.

Mr. Coleman said the state has wide variation in the size of school districts, the number of enrolled students, and the districts' resource needs. He said capital outlay is currently a school district responsibility. He said if initiated measure No. 2 should pass, capital outlay will become a state obligation. He said the state would be in a position of making decisions about local construction needs. He said it raises interesting questions regarding the future of "local control."

In response to a question from Senator Heckaman, Mr. Coleman said tribal land does not have a very high taxable valuation. He said Bureau of Indian Education funding and impact aid are the two principal forms of federal funding for the tribes.

TAXATION OF REAL PROPERTY

At the request of Chairman Kelsch, Ms. Marcy Dickerson, State Supervisor of Assessments and Director of the Property Tax Division, Tax Department, presented testimony regarding the taxation of real property and taxes levied in lieu of property taxes ([Appendix D](#)).

In response to a question from Senator Cook, Ms. Dickerson said the rural electric cooperatives pay

an electric generation distribution and transmission tax in lieu of property taxes. She said if initiated measure No. 2 would leave in lieu of taxes in place, the rural electric cooperatives would be obligated to continue paying in lieu of taxes, whereas Montana-Dakota Utilities Company, Xcel Energy, Inc., and the Otter Tail Power Company would be relieved of their property tax obligation.

Senator Flakoll said there is discussion that if school boards incur debts or raise salaries to exorbitant levels, the language of the initiated measure would make those debts a state obligation. He said some are also suggesting that school boards could expend the money in their ending fund balances, under the assumption that all future obligations would be state obligations.

INITIATED MEASURE NO. 2

At the request of Chairman Kelsch, Ms. Charlene Nelson, Chairman, Empower the Taxpayer, presented testimony regarding initiated measure No. 2.

Ms. Nelson said several years ago a group of individuals concluded that the property tax system needed to be reformed. She said every kind of reform that the group considered only brought with it more problems. She said since 1981 the Legislative Assembly has introduced 134 changes to the state's property tax system. She said the system today is not any better than it was 20 years to 30 years ago. She said the property tax system is broken and unfixable.

Ms. Nelson said in 2009 House Concurrent Resolution No. 3046 was introduced. She said it failed to pass, and therefore, in March 2010 the group turned in nearly 30,000 signatures to have what is now initiated measure No. 2 placed before the electorate.

Ms. Nelson said initiated measure No. 2 provides a far more diverse manner of funding schools, and it does so with much less negative impact than the current system. She said property taxes are the most harmful of all the taxes that governments use. She said a recent Beacon Hill study shows that in the first year after passage of initiated measure No. 2, personal income will increase by 3.6 percent and the number of jobs in the state will increase by more than 4 percent.

Ms. Nelson said property taxes are also the most expensive to administer. She said it costs approximately \$50 million to administer the state's property tax system. She said property taxes are most harmful to the elderly, the disabled, and the unemployed or underemployed. She said property is taxed on a mythical assessed value. She said most people cannot afford the taxes on property with rapidly increasing valuations. She said too often people have to sell their homes because they can no longer afford the taxes. She said young families are often unable to afford home ownership because of property taxes. She said people may own their own homes, but they are always subject to having those homes taken away because of an inability to pay the property taxes. She

said abolishing property taxes will increase income, attract new businesses, and increase home ownership.

Ms. Nelson said she will respond to the following questions which were put to her via a letter sent on behalf of the interim Education Funding and Taxation Committee:

1. Does the initiated measure in any way limit the reorganization or dissolution of school districts, whether self-determined or state-directed?

Ms. Nelson said the answer is no.

2. Does the initiated measure require a specific level of per student funding? Could that level ever be decreased, even in cases of financial exigency?

Ms. Nelson said the initiated measure does not address funding. She said that is solely within the purview of the Legislative Assembly and the school boards.

3. If a school district's student enrollment decreases, must its total funding remain at least the same as it was in 2012?

Ms. Nelson said the initiated measure does not address funding. She said that is solely within the purview of the Legislative Assembly and the school boards.

4. Because the language of the initiated measure prohibits the state from "conditioning" the expenditure of state funding in any manner and because the initiated measure gives school districts sole discretion in the allocation of state funding, does the measure preclude the state from requiring teacher licensure, minimum curricular offerings, or even a minimum school calendar?

Ms. Nelson said the initiated measure addresses only that portion of funding currently coming from property taxes. She said the other 70 percent comes with strings, conditions, and requirements. She said the 30 percent coming from property taxes has a "no strings attached" clause. She said this gives districts flexibility.

5. Does the initiated measure preclude the state from requiring that school buildings meet fire and safety standards, that school districts carry insurance, or that school districts provide their share of Teachers' Fund for Retirement contributions?

Ms. Nelson said the initiated measure does not impact such requirements. She said it merely provides that the state cannot place conditions on the replacement dollars for the 30 percent local share of funding that was generated through property taxation.

6. Would the state be solely responsible for funding any school construction that a school district determines is appropriate for its future?

Ms. Nelson said the state is responsible for funding infrastructure, as prescribed in the

state constitution. She said if a school board wanted to provide a building that the Legislative Assembly believed was in excess of the constitutional requirement, the school board would have to raise the additional funds. She said this could be accomplished by seeking the permission of local taxpayers through a school bond issue.

7. Will the state be responsible for construction debt incurred by a school district prior to the effective date of the measure?

Ms. Nelson said all local debt will be the responsibility of the school district, as it is now. She said such debt is almost always subject to a school bond issue that required voter approval. She said a school bond issue is a special assessment and special assessments are not affected by the initiated measure.

8. Will passage of the initiated measure increase or decrease educational equity and adequacy in the short term or longer term?

Ms. Nelson said the issue of equity has been debated in the legislative and judicial arenas.

In response to a question from Senator Cook, Ms. Nelson said if there is a desire on the part of patrons to build a school, they would come to the Legislative Assembly, and if they wished to build something that was not approved or was in excess of a legislatively approved project, the school district would have a bond vote and pay for that obligation using special assessments, sales taxes, or whatever other mechanism they chose.

In response to a question from Senator Cook, Ms. Nelson said the language of the initiative is designed to allow school districts the flexibility they need to determine and address their needs. She said, for instance, when the state conditioned dollars on school districts increasing teacher salaries, there may have been school districts that would have preferred to provide advanced placement classes or student transportation, rather than teacher pay increases. She said while the state may have to condition its share of the dollars, there are always peculiarities in individual districts and giving them flexibility with respect to how they use their dollars allows for those peculiarities to be addressed.

Senator Cook said he is concerned that the unanswered questions will result in litigation.

In response to a question from Senator Cook, Ms. Nelson said the only taxes that the initiated measure will affect are those taxes based on the value of property. She said it will not affect oil gross production taxes.

In response to a question from Senator Flakoll, Ms. Nelson said she has been unable to obtain accurate information on the number of out-of-state property owners. She said it is important to remember that even property owned by individuals from out-of-state produces revenue.

In response to a question from Senator Flakoll, Ms. Nelson said "full and proper" funding includes statutory obligations and court-imposed obligations. She said the Legislative Assembly might very well have to redefine what constitutes the state's legal obligations.

In response to a question from Senator Flakoll, Ms. Nelson said the federal income tax deduction for property taxes is very small compared to the overall property tax burden that would be removed from citizens.

In response to a question from Senator Flakoll, Ms. Nelson said there are a variety of taxes with which to fund schools. She said the funding for other political subdivisions is broader. She said she is not aware of why income tax is mentioned in subsection 1 of section 4 but not in subsection 2. She said this measure is almost a verbatim version of 2009 House Concurrent Resolution No. 3046.

Senator Flakoll said if for some reason oil and gas production taxes are not available to fund school districts, the total of the tobacco tax, the financial institutions tax, and lottery revenue probably does not exceed \$100 million.

In response to a question from Senator Flakoll, Ms. Nelson said the initiative will abolish all property taxes for any purpose. She said the medical school would have to be funded from other sources.

In response to a question from Senator Lee, Ms. Nelson said the initiated measure does not put the state in the position of control over what happens at the local level. She said it only makes the state an agent for political subdivisions and requires the state to ensure that funds are made available. She said that is why the language specifically requires that there be no state control over the funds.

In response to a question from Senator Lee, Ms. Nelson said township or county governments will still need to exist because they are most responsive to local needs. She said what is good for one political subdivision might not be good for another. She said that is why the Legislative Assembly will have to craft a formula that ensures all legal requirements are met, while allowing the political subdivisions the flexibility to address their own needs.

In response to a question from Representative Headland, Ms. Nelson said she cannot imagine that the Legislative Assembly would want the funding to stay at the 2012 levels forever. She said each legislator represents the will of a particular district, and they understand that the political subdivisions in each of their legislative districts have to be fully and properly funded. She said she envisions a formula for political subdivisions that is very similar to that which the Legislative Assembly put together for elementary and secondary education.

Representative Headland said there is probably not a lot of political will to increase income or sales taxes.

In response to a question from Senator Flakoll, Ms. Nelson said school districts will face the issue of

supplanting existing federal programs when the federal revenues are reduced regardless of whether or not the initiated measure passes.

In response to a question from Senator Flakoll, Ms. Nelson said the state constitution requires that the state provide funding for the education of our children. She said that includes having buildings and transportation, etc. She said 70 percent of that is currently being funded by the state and 30 percent is being funded by the local school districts. She said if a school district wants to build something that is beyond the norm, the district would have to raise the funds for that project.

Senator Flakoll said the state has basically taken away the ability to raise income taxes at the local level. He said most districts do not have the ability to significantly increase sales taxes. He said he is still confused with respect to what constitutes "specials."

Ms. Nelson said "specials" refers to residents of the district voting with respect to whether or not they want to issue a bond. She said the residents can pay for that bond obligation through sales taxes or by special assessments. She said special assessments do not need to be based on the value of property. She said they could be based on the benefit to homeowners rather than the value of property. She said the voters would have to decide how to base the assessment.

In response to a question from Senator Flakoll, Ms. Nelson said the "no strings attached" requirement applies only to the 30 percent local share that would be supplanted by state resources. She said the state can continue to place strings on its 70 percent share of funding.

In response to a question from Senator Cook, Ms. Nelson said she is not familiar with all of the legal ramifications in the measure. She said she does not know why it was worded the way it was. She said the initiated measure was taken verbatim from a resolution that was introduced in 2009.

In response to a question from Representative Kelsch, committee counsel said she does not know whether this language was written by one of the Legislative Council's staff members or whether it came through the system as a "form and style" measure. She said under that procedure Legislative Council staff take a document prepared by someone else and place it in proper bill form, but they do not review the content.

Senator Flakoll said the reference to the school board having sole discretion to expend the local share is confusing in light of the fact that now there are requirements for school district residents to vote on certain school construction proposals. He said it would appear that the language of the initiative, which gives sole discretion to the board regarding expenditures, would in effect remove the requirement that there be a vote of the people.

In response to a question from Representative Headland, Ms. Nelson said the House of Representatives in considering the 2009 resolution did

not believe that property taxes should be abolished. She said she and others believe differently. She said she and others believe that there was not a full debate on the issue. She said this is affecting people throughout the state. She said people are losing their homes or having to sell their homes in order to avoid a seizure for nonpayment of taxes. She said the current property tax system is impeding new businesses from coming into the state. She said they felt that the proposal needed to have a full and open debate among the people of North Dakota, and the best way to do that was to put it on the ballot.

Chairman Kelsch said the issue regarding whether or not the initiated measure precludes a vote of the people might be moot. She said if all of the money is coming from the state level and no one is required to pay property taxes anymore, there is no reason to ask the patrons of a school district if they are willing to assume a financial obligation.

COMMENTS BY OTHERS

With the permission of Chairman Kelsch, Mr. Mitch Carlson, Superintendent, LaMoure School District, presented testimony ([Appendix E](#)) regarding use of a school district's 2008 levy as the baseline for determining property tax relief.

With the permission of Chairman Kelsch, Mr. Brandt Dick, Superintendent, Hazelton-Moffitt-Braddock School District and Underwood School District, presented testimony ([Appendix F](#)) regarding use of a school district's 2008 levy as the baseline for determining property tax relief.

With the permission of Chairman Kelsch, Mr. Pat Feist, Superintendent, Enderlin Area School District, presented testimony ([Appendix G](#)) regarding use of a school district's 2008 levy as the baseline for determining property tax relief.

With the permission of Chairman Kelsch, Mr. Steve Holen, Superintendent, McKenzie County School District No. 1, presented testimony regarding use of a school district's 2008 levy as the baseline for determining property tax relief. Mr. Holen said in 2008 his school district was experiencing declining enrollment. He said the school district had around 500 students, and they were looking at reductions in staff. He said, at that time, the district levied what it needed. He said by 2011 there was a 25 percent increase in the number of students, and the school board was looking at ways to fund that change. He said they do receive in lieu of taxes, but those are capped at 6.38 mills. He said the district's mill levy is therefore 166.38 mills. He said, in theory, the district cannot go to 185 mills, although they may have to look at doing exactly that so they can address their changing needs.

IMPACT OF 2011 FLOODING

With the permission of Chairman Kelsch, Ms. Tamara Uselman, Superintendent, Bismarck School District, presented testimony ([Appendix H](#))

regarding the impact of 2011 flooding on school district property, school district staff, and student placement.

Ms. Uselman said with respect to the discussion regarding the role of property taxes in education funding, everyone would like to have good services at an efficient price. She said Minnesota removed local property taxes as a funding source for education. She said, because the state is broke and cannot afford to fund its obligations, 60 percent of the state aid is being forwarded to school districts and 40 percent is being held back in order to meet state operational expenses. She said there is always some value to local control. She said local property taxes provide people with a vested interest in building a good school system. She said when that is taken away, the local people, especially those without children in the system, no longer have the same level of interest in their schools.

With the permission of Chairman Kelsch, Mr. Mark Vollmer, Superintendent, Minot School District, provided a PowerPoint presentation (on file in the Legislative Council office) regarding the impact of 2011 flooding on school district property, school district staff, and student placement.

In response to a question from Representative Hunsakor, Mr. Vollmer said one of their greatest challenges is housing. He said housing was at a premium in Minot before the flood, and now, after the flood, 4,200 additional residences have been taken out of the mix.

Mr. Vollmer said with respect to the discussion regarding the role of property taxes in education funding, he believes that taxation for the betterment of society is a three-legged stool. He said property taxes are one leg of the stool. He said property taxes are a way for the people to have a say in their local community--whether it is school districts or park districts, etc. He said any issues can be addressed legislatively.

CONCUSSION MANAGEMENT IN YOUTH ATHLETICS

At the request of Chairman Kelsch, committee counsel presented a background memorandum entitled *Concussion Management - Background Memorandum* ([Appendix I](#)).

With the permission of Chairman Kelsch, Dr. Wayne Sanstead, Superintendent of Public Schools, distributed a document entitled *North Dakota High School Activities Association Concussion Management Procedure* ([Appendix J](#)). He said the document reflects the High School Activities Association's response to the requirements that were put into 2011 Senate Bill No. 2281. He said the document will be placed before the board at its August 2011 meeting.

With the permission of Chairman Kelsch, Mr. John Vastag, Director, Legislative Affairs, Sanford Health, presented testimony ([Appendix K](#)) regarding

concussion management in youth athletics. He distributed a document entitled *Concussion Legislation: Focus on Youth Activities* (on file in the Legislative Council office).

With the permission of Chairman Kelsch, Mr. Jack McDonald, Board of Physical Therapy, presented testimony regarding concussion management in youth athletics ([Appendix L](#)). He said Senate Bill No. 2281 provided that if a student is removed because the student presented signs or symptoms of a concussion, that student must be examined by a health care provider whose scope of practice includes the diagnosis and treatment of concussion. He said the Board of Physical Therapy passed a motion indicating that diagnosing and treating concussions is within a physical therapist's scope of practice.

With the permission of Chairman Kelsch, Mr. Andy Dahl, Executive Director, Missouri Valley YMCA, Bismarck, presented testimony ([Appendix M](#)) regarding concussion management in youth athletics. He said because the YMCAs rely heavily on volunteers who, unlike school coaches, do not generally have a prolonged period of time within which they can get to know the youth participants, there is concern that a short course on concussions would not provide such volunteers with training sufficient to enable them to identify a mild concussion.

COMMITTEE DISCUSSION - STAFF DIRECTIVES

Senator Cook requested that committee members receive an e-mail regarding the types of "in lieu of taxes."

Senator Cook said issues of equity will exist in several different forms. He said we will have to

discuss educational equity and funding equity and equity with respect to taxes that individuals will be asked to pay in order to replace the property taxes. He said there are great inequities in the amount of sales tax that can be raised locally.

Senator Cook said Mr. Coleman will need to provide the committee with detailed information regarding state aid to districts under two scenarios--the first dealing with the addition of \$295 million to \$340 million new dollars in place of the existing property tax relief and the second dealing with the state supplanting local property tax revenues.

Senator Flakoll requested a report regarding the fiscal impact of the initiated measure.

Senator Flakoll said he believes that having smaller school districts with declining enrollment, come to the Legislative Assembly and request dollars for buildings will be a very large hurdle--especially so with discussions regarding reorganization.

Senator Flakoll said there are currently a large number of tax exemptions that exist. He said they cover everything from medical supplies to farm machinery and various things for churches. He said they would all be on the table.

No further business appearing, Chairman Kelsch adjourned the committee at 3:00 p.m.

L. Anita Thomas
Committee Counsel

ATTACH:13