PROPERTY TAX SYSTEM - BACKGROUND MEMORANDUM

House Concurrent Resolution 3019 (2013) provides the Legislative Management shall study the property tax system. The resolution states the Legislative Assembly must closely monitor the property tax system and examine options for improvements that could reduce the property tax burden and enhance the fairness and uniformity of the property tax system.

PROPERTY TAX DETERMINATION

The property tax liability of a property owner is determined by multiplying combined mill rates for all taxing districts in which the property is located times the taxable value of the property. Although this formula is relatively simple, complexities are involved in determining the mill rate, taxable value, and tax status for the property.

In addition, state-aid property tax relief in various forms has been provided by constitutional and legislative provisions, which will reduce the tax burden for individual properties in varying degrees.

All locally assessed property taxes are collected by the county and distributed among appropriate taxing districts. Property taxes are due January 1 following the year of assessment and are payable without penalty until March 1 of the year they are due. If property taxes are paid in full by February 15, the taxpayer is entitled to a 5 percent discount. Penalties begin to accrue if property taxes are not paid by March 1. Taxpayers have the option of paying property taxes in installments.

Determination of Mill Rate

The mill rate for a taxing district is established through the budget process. Each taxing district prepares a proposed budget based on anticipated expenditures for the upcoming fiscal year. Hearings are held on the proposed budget and adjustments are made as determined by the governing body. The deadline for amendments to budgets and for sending copies of the levy and budget to the county auditor is October 10.

The amount budgeted by a taxing district may not result in a tax levy exceeding levy limitations established by statute. Levy limitations for political subdivisions are summarized in the Schedule of Levy Limitations prepared biennially by the Tax Commissioner's office. A copy of the July 2013 Schedule of Levy Limitations has been distributed to the members of the Taxation Committee and the Schedule is available on the Tax Commissioner's website. Review of the levy authority provided by law reveals 245 grants of authority for specific purpose levies by the state and political subdivisions. The number of such grants of authority by taxing entity is as follows:

State Medical Center (constitutional)	1
Garrison Diversion Conservancy District	11
County	71
Township	31
City	62
City park district	12
Rural ambulance service district	8
Rural fire protection district	9
Hospital district	8
School district	11
Recreation service district	7
Soil conservation district	6
Southwest Water Authority	6
Irrigation district (levied only by special assessment)	1
Water district (levied only by special assessment)	1
Total	245

Since 1981 the Legislative Assembly has provided optional authority to levy taxes with a maximum amount determined by comparison with a base year levy in dollars. This method is an alternative to the use of statutorily established mill levy limitations. From 1981 through 1996, percentage increases were allowed by law over the base year levy in dollars. The compounding of these increases allowed taxing districts to increase levies beyond the amount they would be able to levy under mill levy limitations. For taxable years after 1996, taxing districts may use the optional method to levy up to the amount levied in dollars in the base year without a percentage increase. The most significant difference between the two kinds of levy limits is that under mill levy limits a taxing district gains additional dollars of levy authority from new taxable property and increased assessed values of existing property, while under limits based on dollars levied in prior years only new taxable property increases dollars of levy authority.

To determine the mill rate for a taxing district, the county auditor determines whether the amount levied is within statutory levy limitations and, if it is, the county auditor divides the total property taxes to be collected for the taxing district by the taxing district's total taxable valuation. This generates a percentage that is the mill rate for the district. This percentage or mill rate is applied to the taxable valuation of property to determine the owner's property tax due to the taxing district.

From October 10 to December 10, the county auditor prepares tax lists, which must be delivered to the county treasurer by December 10 and the treasurer must prepare and mail the tax statements to property owners by December 26.

Assessment of Locally Assessed Property

All property in this state is subject to taxation unless expressly exempted by law (North Dakota Century Code Section 57-02-03). Real property must be assessed with reference to its value on February 1 of each year (Section 57-02-11). All property must be valued at the "true and full value" of the property (Section 57-02-27.1). True and full value is defined as the value determined by considering the earning or productive capacity, if any; the market value, if any; and all other matters that affect the actual value of the property to be assessed. For purposes of agricultural property, this includes farm rentals, soil capability, soil productivity, and soils analysis (Section 57-02-01). The assessed value of property is equal to 50 percent of the true and full value of the property (Section 57-02-01). Taxable valuation of property is determined as a percentage of assessed valuation, which is 9 percent for residential and 10 percent for agricultural, commercial, and centrally assessed property. The taxable valuation is the amount against which the mill rate for the taxing district is applied to determine the tax liability for individual parcels of property.

Residential and commercial property true and full value is established by local assessors. True and full value of railroad, public utility, airline property, and all oil or gas pipeline property is centrally determined by the State Board of Equalization.

True and full value of agricultural property is based on productivity as established through computations made by the North Dakota State University Department of Agricultural Economics based on the capitalized average annual gross return of the land. Annual gross return is determined from crop share rent, cash rent, annual gross income, or annual gross income potential. Average annual gross return for each county is determined by taking annual gross returns for the county for the most recent 10 years, discarding the highest and lowest annual gross return years, and averaging the remaining 8 years. Statistics from the most recent 10 years for prices paid by farmers are used to adjust annual gross return. Annual gross return is then capitalized using a 10-year average of the most recent 12-year period for the gross agribank mortgage rate of interest. However, the minimum capitalization rate under the formula was set at 9.5 percent for tax year 2004, 8.9 percent for tax year 2005, and 8.3 percent for tax years 2006 through 2008. Under a 2009 amendment, the minimum capitalization rate was 8 percent for 2009, 7.7 percent for 2010, and 7.4 percent for 2011. After 2011, there is no minimum capitalization rate. Replacement of the statutory capitalization rate with a market-based capitalization rate caused a greater than average increase in agricultural property values in 2012. Personnel from North Dakota State University determine an average agricultural value per acre for cropland and noncropland on a statewide and countywide basis. This information is provided to the Tax Commissioner by December 1 of each year and then provided by the Tax Commissioner to each county director of tax equalization. The county director of tax equalization provides each assessor within the county an estimate of the average agricultural value of agricultural lands within the assessor's assessment district. The local assessor must determine the relative value of each assessment parcel within that assessor's jurisdiction. In determining relative values, local assessment officials are to use the following considerations, in descending order of significance--soil type and soil classification data, a schedule of modifiers approved by the state supervisor of assessments, and actual use of the property by the owner.

If the assessment for a parcel of property increases the true and full valuation of the parcel by $3,000 or more and is an increase of 10 percent or more from the previous year, the assessor must send written notice of the increase to the property owner at least 15 days before the meeting of the local board of equalization (Section 57-12-09). The property owner has the right to contest the assessment to the local, county, and state boards of equalization or through the tax abatement process.

Assessment of Centrally Assessed Property

The owner of centrally assessed property must file an annual report with the Tax Commissioner by May 1. The Tax Commissioner prepares a tentative assessment for the property by July 15. Notice of the tentative assessment is sent to the property owner at least 10 days before the State Board of Equalization meeting. On the first Tuesday in August, the board meets to receive testimony on the value of centrally assessed property and to finalize assessments. The Tax Commissioner certifies the finalized assessments to the counties to reflect the portion of centrally assessed property for each property owner which is taxable in that county.

Airlines serving North Dakota cities pay a property tax computed by averaging mill levies in all the cities served by an airline and applying the average levy against the taxable valuation of property of the airline in North Dakota. Taxes imposed on an airline are collected by the State Treasurer and distributed to the cities in which the airline operates to be used exclusively for airport purposes.

Payments In Lieu of Taxes

State law provides some enterprises make payments in lieu of taxes rather than paying property taxes. Mutual or cooperative telephone companies and investor-owned telephone companies pay a tax of 2.5 percent of adjusted gross receipts. This tax is paid to the Tax Commissioner and allocated among counties.

Through 2009 rural electric cooperatives paid a 2 percent gross receipts tax in lieu of property taxes for all property except land. Beginning in 2010, enactment of 2009 Senate Bill No. 2297 changed taxation of rural electric cooperatives from a gross receipts tax to a transmission line mile tax of $50 to $600 per mile and a tax of $1 per megawatt-hour for retail sales to consumers in this state. Revenues from the tax are still considered payments in lieu of taxes and will be allocated to political subdivisions based on location of transmission lines and, for distribution lines, based on location of distribution lines and sales from those lines. Rural electric cooperatives with generating facilities are subject to a transmission line tax of $225 to $300 per mile in lieu of property taxes on transmission lines of 230 kilovolts or more.

Coal conversion facility taxes and oil and gas gross production taxes are paid in lieu of property taxes. These taxes are allocated by state law and provide revenues to affected taxing districts.

Property owned by certain state agencies, nonprofit entities, and agencies and instrumentalities of the federal government are subject to payments in lieu of property taxes. Mobile homes, certain pipelines, certain transmission lines, and certain forest lands are subject to payments in lieu of property taxes. New and expanding business may be granted the right to make payments in lieu of property taxes under Section 40-57.1-03.

PROPERTY TAX STATISTICS AND POLITICAL SUBDIVISION REVENUES

In taxable year 2012, statewide property and special taxes totaled almost $829.2 million. This amount is an increase of 7.6 percent from the 2011 total. The constitutional one-mill levy for the State Medical Center was imposed in the amount of $2.8 million which is included in this total. This amount is an increase of 14.3 percent from the 2011 total. Because the State Medical Center levy is always imposed at a rate of one mill, the 89 percent increase shown in the table for the State Medical Center can be assumed to be approximately equal to the 2012 increase in taxable valuation in property statewide. The following table shows the percentage of the 2012 amount levied by each type of political subdivision and the percentage increase in property taxes and special taxes levied by each type of political subdivision from 2003 through 2012.

	Percentage of Statewide Property Taxes and Special Taxes[1] Levied in 2012	Percentage Increase in Property Taxes and Special Taxes[1] Levied 2003 Through 2012
School districts	46.18%	15.8%
Counties	29.30%	71.1%
Cities	13.61%	52.5%
City park districts	5.29%	73.3%
Townships	2.53%	81.9%
Rural fire protection	0.91%	109.6%
Garrison Diversion	0.26%	84.9%
Soil conservation districts	0.37%	201.0%
State Medical Center	0.34%	89.0%
Other[2]	0.24%	253.0%
Tax increment districts	N/A[3]	89.1%
Statewide	N/A	39.2%

[1]"Special taxes" include mobile home taxes, rural electric cooperative taxes, woodland taxes, and payments in lieu of taxes.

[2]"Other" includes West River/Southwest Water Authority, hospital districts, rural ambulance districts, and recreation service districts.

[3]Tax increment district collections are included in city levies in this table. They are listed here only to show the relative rate of increase.

State Funding to Political Subdivisions

A schedule showing major state appropriations and revenue allocations for direct assistance to political subdivisions covering biennial assistance from 2003-05 through 2013-15 is attached as an appendix. Comparison of appropriations and revenue allocations for 2003-05 and 2013-15 bienniums shows an increase of $2.74 billion or 271 percent in state appropriations and revenue allocations to political subdivisions over that time period. This can be compared with an increase of about 39 percent in political subdivisions' property taxes and special taxes levied from 2003 to 2012. The Legislative Assembly has taken action by providing property tax relief and other assistance to reduce the property tax burden. Appropriations by the state in 2009 marked the first time in many years state appropriations and revenues to political subdivisions increased at a faster rate than political subdivisions' property taxes and special taxes levied. For example, from 1994 to 2007, property taxes and special taxes levied by political subdivisions increased 95.9 percent while state appropriations and revenue allocations to political subdivisions increased by 83.6 percent.

Home Rule Sales Taxes

Another significant source of revenue for 136 cities and five counties is revenue from home rule sales taxes. Grand Forks imposed the first city home rule sales tax in 1985. In 1990 six cities imposed home rule sales taxes. By 1996 home rule sales taxes had become a significant revenue source. Currently, more than 110 cities and 4 counties impose a home rule sales tax. The following table illustrates the growth in home rule sales tax collections:

Fiscal Year	Local Sales and Use
1996	$36,534,413
1997	$45,184,127
1998	$48,929,646
1999	$54,058,001
2000	$58,711,263
2001	$66,961,363
2002	$65,368,838
2003	$73,666,551
2004	$68,644,864
2005	$78,761,154
2006	$87,563,544
2007	$92,143,032
2008	$96,566,720
2009	$108,174,716
2010	$118,767,582
2011	$143,467,447
2012	$191,754,625
2013	$206,247,609

SPECIAL ASSESSMENTS

A significant source of revenue to cities is from special assessments imposed. From 2003 to 2012, special assessments imposed statewide increased by 59 percent, and it appears there are varying levels of reliance on special assessments revenue among cities. For example, on a statewide basis more than $9 in property taxes is collected for each $1 in special assessments. In Stark County, the ratio is 43.8-to-1, Ward County 39.2-to-1, Ramsey County 32.5-to-1, Grand Forks County about 10.2-to-1, Morton County about 6.5-to-1, Cass County about 4.6-to-1, and Traill County about 4.7-to-1.

RESOURCES

The statistical information in this memorandum was drawn from the *2012 Property Tax Statistical Report* and *State and Local Taxes 2012* (Red Book) prepared by the Tax Commissioner's office. These publications contain a wealth of information about property taxes and other tax types in North Dakota.

PROPERTY TAX RELIEF LEGISLATION

2007 Senate Bill No. 2032

Senate Bill No. 2032 (2007) was the first legislative venture into direct property tax relief and was the subject of extensive discussion and amendments. The bill as enacted contained the following provisions regarding property taxes and income taxes:

1. Homestead property tax maximum income eligibility for persons 65 years of age or older or permanently and totally disabled was increased from $14,500 to $17,500. The maximum value of property exempt under the homestead property tax credit was increased from $67,511 to $75,000.

2. The amount of an assessment increase for property which triggers the requirement for written notice to a property owner was reduced from a 15 percent increase to a 10 percent increase. The time the notice of assessment increases must be delivered to property owners was increased from 10 days to 15 days before the meeting date of the local board of equalization.
3. After June 30, 2007, in any school district election for approval by electors of unlimited or increased general fund levy authority, the ballot must specify the number of mills, percentage increase in dollars levied, or that unlimited levy authority is proposed for approval and the number of taxable years for which the approval is requested. The length of time electors can authorize unlimited or increased school district general fund levy authority was limited to not more than 10 taxable years. The number of petition signatures required to place the question of discontinuing increased or unlimited school district general fund levy authority on the ballot was reduced from 20 percent of the persons in the school census to 10 percent of the number of electors who cast votes in the most recent school district election.
4. Real estate and mobile home tax statements must include, or be accompanied by a separate sheet with, three columns showing for the year of the tax statement and the two preceding tax years the property tax levy in dollars against the property by the county and school district and any city or township that levied taxes against the property.
5. An income tax marriage penalty credit of up to $300 per couple was provided to offset any marriage penalty incurred for couples with incomes up to $154,200. The credit is determined by comparing the tax on the couples' joint North Dakota taxable income and the tax that would apply if the couples' income were separated and taxed at the single filer rate.
6. A homestead income tax credit was provided for individuals for taxable years 2007 and 2008 in the amount of 10 percent of property taxes or mobile home taxes that became due during the tax year and were paid on the individual's homestead. This credit was effective only for the 2007 and 2008 taxable years and was not extended by any 2009 legislation. It appears this credit can now be repealed. Property taxes eligible for the credit did not include special assessments. For purposes of the credit, "homestead" means the dwelling occupied as a primary residence in this state and any residential or agricultural property owned by the individual in this state. The amount of the homestead income tax credit for a year could not exceed $1,000 for married persons filing a joint return or $500 for a single individual or married individuals filing separate returns.

   The amount of the homestead income tax credit exceeding the taxpayer's income tax liability could be carried forward for up to five years or the taxpayer could request that the Tax Commissioner issue the taxpayer a certificate in the amount of the excess. A certificate issued to a taxpayer could be used by the taxpayer against property or mobile home tax liability during the ensuing taxable year by delivering the certificate to the county treasurer of the county in which the taxable property or mobile home is subject to taxes. The county treasurer was to forward certificates redeemed in payment of tax obligations to the Tax Commissioner, who issued payment to the county in the amount of the certificates.

   Persons owning property together were entitled to only one credit for that parcel of property, so the credit may be shared between or among them. Persons owning property together were each entitled to a percentage of the credit for a single individual equal to their ownership interests in the property. There was no limit on the number of parcels of taxable property for which an individual could claim the credit.
7. A commercial property income tax credit was provided for an individual or corporation for taxable years 2007 and 2008 in the amount of 10 percent of commercial property taxes or commercial mobile home taxes that became due during the income tax year and have been paid. This credit was effective only for the 2007 and 2008 taxable years and was not extended by any 2009 legislation. It appears this credit can now be repealed. Property taxes eligible for the credit did not include special assessments. The amount of the credit for commercial property for a year could not exceed $1,000 for any taxpayer and was limited for individuals to $1,000 for married persons filing a joint return or $500 for a single individual or married individuals filing separate returns.

   The amount of the commercial property income tax credit exceeding the taxpayer's tax liability was allowed to be carried forward for up to five years.

   Persons owning property together were entitled to only one credit for that property, so the credit may be shared between or among them. Persons owning property together were each entitled to a percentage of the credit equal to their ownership interests in the property. There was no limit on the number of parcels of taxable property for which a corporation or individual could apply.

A passthrough entity entitled to the commercial property income tax credit was required to allocate the amount of the credit to the partners, shareholders, or members in proportion to their respective interests in the passthrough entity.

2009 Senate Bill No. 2199

Senate Bill No. 2199 (2009) was not introduced at the request of the Governor but was the product of the Governor's previously announced intention to introduce legislation to provide funding from the state for statewide school district mill levy reductions.

Senate Bill No. 2199 provided property tax relief by appropriating $295 million for the 2009-11 biennium for allocation to school districts to reduce school district property taxes. The bill provided for a reduction of up to 75 mills in school district property tax levies and replacement of the revenue to school districts through mill levy reduction grants. The bill eliminated authority for unlimited levy approval for school districts. The bill established a deadline of 2015 for school districts with existing voter-approved excess levies or unlimited levies to obtain voter approval for continuation of a levy of up to a specific number of mills. If voter approval is not obtained by 2015, the school district levy limitation will be subject to statutory provisions allowing the option of a levy based on the number of dollars levied by the school district in the highest of the most recent three years or a levy within the 185-mill general fund levy limitation.

The bill also provided for transfer of $295 million in 2010 from the permanent oil tax trust fund to the property tax relief sustainability fund to be used for property tax relief allocations after the 2009-11 biennium.

2011 House Bill No. 1047

The 2009-10 interim Taxation Committee recommended extension of the 2009 property tax relief legislation, and the recommendation was introduced as 2011 House Bill No. 1047. The bill was amended by the Legislative Assembly to incorporate income tax and financial institution tax relief provisions.

House Bill No. 1047 provided property tax relief by appropriating $341,790,000 for the 2011-13 biennium for allocation to school districts to reduce school district property taxes. The bill provided for a reduction of up to 75 mills in school district property tax levies and provides for replacement of the revenue to school districts through mill levy reduction grants. The bill provisions were essentially the same as the 2009 provisions except the 2011 bill limited the grant to a school district so the current year grant to a school district may not exceed the grant in the preceding school year by more than the percentage increase in statewide taxable valuation, provided for recognition and adjustment for certain property types that are not subject to traditional property taxes but which provide revenue to school districts, and made clear that a school district that does not receive voter approval for extension of authority to levy in excess of statutory mill levy limitations may retain the authority to levy based on the highest dollar amount levied in the most recent three previous years.

House Bill No. 1047 was amended to reduce individual income tax rates by 17.9 percent, which was expected to reduce state general fund revenues $120 million for the 2011-13 biennium. The bill reduced corporate income tax rates by 19.5 percent, resulting in an anticipated reduction state general fund revenues of approximately $25 million for the 2011-13 biennium. The bill reduced the financial institutions tax rate from 7 percent to 6.5 percent. Only the state general fund share of tax revenue was impacted by the financial institutions tax rate change, resulting in an estimated state general fund revenue reduction of approximately $2,125,000 for the 2011-13 biennium.

2013 Property Tax Legislation

House Bill No. 1013 provides a substantial expansion of state funding for elementary and secondary education. The funding enhancement includes a property tax relief component to provide for state payment of up to an additional 50 mills of school district property tax levies and incorporates the previous mill levy reduction grant property tax relief program, which provided a reduction of up to 75 mills in school district property tax levies. The result of combining the relief programs is estimated to provide more than $650 million in property tax relief for the 2013-15 biennium. The bill reduces school district general fund levy authority to 60 mills and allows 12 mills for miscellaneous expenses and allows a 12 percent increase in dollars per year, to a maximum combined levy of 82 mills.

Senate Bill No. 2036 provides a new approach to property tax relief funding that provides a state-paid credit against property taxes and mobile home taxes in the amount of 12 percent of the taxes levied by all taxing districts against the property. The relief provided by Senate Bill No. 2036 is estimated to provide $200 million in property tax relief for the 2013-15 biennium. The bill requires the Tax Commissioner to prescribe the form of notice of increased assessments for property owners and the form of the property tax statement. The bill requires individuals who previously received notice of increased assessments to also receive mailed notice to inform them of a public property tax levy hearing if the taxing district is considering a property tax increase.

Senate Bill No. 2171 expands eligibility and qualifying income limits for the homestead property tax credit for individuals 65 years of age or older or permanently or totally disabled. The bill increases the maximum income to qualify for the credit from $26,000 to $38,000. The bill increases the amount of assets of an applicant for eligibility for the credit from $75,000 plus $100,000 of the unencumbered value of the homestead to a combined total assets of $500,000. The combined property tax relief provided for the homestead credit and disabled veterans homestead credit by House Bill Nos. 1015 and 1036 and Senate Bill No. 2171 is estimated to be more than $27 million for the 2013-15 biennium.

House Bill No. 1015 adds an additional income category to qualify for the homestead property tax credit, to allow individuals with income from $38,000 to $42,000, which entitles the owner to reduction of 10 percent of taxable valuation up to a maximum reduction of $450 of taxable valuation.

House Bill No. 1306 increases the amount of the credit for the homestead of a disabled veteran from $5,400 to $6,750 of taxable valuation.

House Bill No. 1300 changes the basis of the property tax exemption for religious organization from buildings used for religious "services" to buildings used for religious "purposes." The bill also increases from two acres to five acres the amount of adjoining land of a religious organization deemed to be used for religious purposes and exempt from property taxes. The measure is retroactively effective to apply to tax years beginning after 2010.

Senate Bill No. 2338 provides for conditional exemption and payments in lieu of taxes for affordable rental residential property and eliminates a restriction to disallow a charitable buildings property tax exemption for property leased to tenants based on income levels to enable the owner to receive a federal low-income housing income tax credit. The bill provides residential rental property used as affordable housing is eligible for a property tax exemption for the property's period of affordability. Property is eligible for the exemption if the Housing Finance Agency certifies to the county director of tax equalization the property is subject to a land use restriction agreement providing mandatory income and rent restrictions, the property is owned by a qualified nonprofit entity, project owners are required to make a payment in lieu of taxes equal to 5 percent of the rents collected in the preceding calendar year, and the property continues to be operated in compliance with rent and household income restrictions.

Senate Bill No. 2162 increases the state matching grant for county senior citizen services and programs from a state match of 75 percent to a state match of 85 percent of the amount generated by levy of up to one mill in property taxes in the county for senior citizen services and programs. The bill makes an equivalent increase in the portion of state sales, use, and motor vehicle excise tax collections to be deposited in the senior citizen services and programs fund by the State Treasurer.

House Bill No. 1178 provides enhanced penalties for failure and continued failure by a public utility company to furnish reports to the Tax Commissioner required by law for assessment and property taxation of public utility property. The bill also changes the filing date from May 1 to March 15 for reports on public utility property description and location by county.

Senate Bill No. 2093 makes clear information obtained by the Tax Commissioner for purpose of valuation and assessment of centrally assessed property may be used by the Tax Commissioner to determine and enforce tax liability under any other tax law administered by the Tax Commissioner.

House Bill No. 1107 provides the withholding of state aid distribution fund allocations from counties as a penalty for failure to implement soil type and soil classification data in assessments continues until the Tax Commissioner certifies to the State Treasurer that the county has fully implemented use of soil type or soil classification data.

House Bill No. 1136 provides for electronic filing of information in the central indexing system relating to property liens and tax liens and relating to taxpayer identification number or social security number inclusion in filed documents.

ATTACH:1