

## **SPECIAL ASSESSMENT REVENUE REPLACEMENT STUDY - BACKGROUND MEMORANDUM**

Section 1 of House Bill No. 1474 (2019) ([appendix](#)) directs the Legislative Management to study options for replacing revenue generated by special assessments with revenue from an alternative local funding source. The study must include a review of the purposes for which special assessments are imposed, the revenue generated from the imposition of special assessments, local revenue sources that could be used as an alternative to imposing special assessments, and the manner in which fees for an alternative local revenue source would be calculated and imposed as compared to the manner in which special assessments are calculated and imposed.

As introduced, House Bill No. 1474 would have provided authority for a city or county to levy an infrastructure tax in lieu of special assessments on all residential and commercial utility bills for payment of infrastructure maintenance costs. The bill was amended in the House to prohibit the infrastructure tax from being imposed on communication company bills and to allow the electors of a municipality to submit a proposed ordinance to the governing body of the municipality for submission to the voters upon a petition signed by at least 60 percent of the voters who voted at the last municipal election. The bill was amended in the Senate to remove the substantive provisions and to provide for this study.

### **SPECIAL ASSESSMENT BACKGROUND AND STATUTORY AUTHORITY**

Cities were the first political subdivision in North Dakota to receive authority to levy special assessments for improvements. Cities have had authority to levy special assessments since 1897, and as a result, the statutory provisions relating to special assessments in cities are the oldest and most detailed. Recreation service districts were the second political subdivision to receive special assessment levy authority in 1975, followed by water resource districts in 1981, counties in 1983, and townships in 2001.

Several chapters of North Dakota Century Code Title 40 govern improvements by special assessment in cities. Recreation service districts and counties glean authority to levy special assessments for improvements by adopting the provisions relating to cities by reference. Special assessment levy authority and related procedures for water resource districts are contained in Chapter 61-16.1 and township special assessment levy authority is governed by an abbreviated statutory procedure in Chapter 58-18.

### **Purposes for Which Special Assessments Are Imposed**

Pursuant to Section 40-22-01, a city may defray the expenses related to a number of improvements by levying special assessments. Improvement costs for which special assessments may be levied include costs for new water supply or sewage systems, or the extension or replacement of existing systems; improvements to a municipal street system, broadly ranging from paving and resurfacing streets to installing Christmas streetlighting decorations; improvements to boulevards or other public places and the maintenance of those improvements; the acquisition of land and easements for flood protection purposes and the construction of necessary works; and the acquisition or leasing of property and easements for parking lots, ramps, and garages and associated construction costs. A city also may establish a special assessment district pursuant to Chapter 40-22.1 for the promotion of business activity and new business development.

For a defined area outside the limits of an incorporated city, the board of county commissioners may initiate a special assessment district and levy special assessments for improvements. Pursuant to Section 11-11-55.1, a county is given all the authority and duties pertaining to special assessments which belong to cities in Chapters 40-22 through 40-28.

Townships may defray expenses of improvements through special assessment districts pursuant to Chapter 58-18. The board of township supervisors may create an improvement district upon petition of at least 60 percent of the property owners in a proposed improvement district area. Each improvement district must be of a size and form to include all properties the township board of supervisors believes will be benefited by the improvement project.

A recreation service district may levy special assessments to provide services, including police protection, sewer and water, garbage removal, and public road construction and maintenance. Pursuant to Section 11-28.2-04.1, a recreation service district is deemed to be a "municipality" for purposes of the special assessment provisions in Chapters 40-22 through 40-27.

Chapter 61-16.1 governs the administration of special assessments by water resource districts. Pursuant to Section 61-16.1-15, a water resource board may provide for the cost of construction, alteration, repair, operation, and maintenance of a water resource district project through issuance of improvement warrants or with funds raised by special assessments, a general tax levy, issuance of revenue bonds, or a combination of these methods.

### **Manner in Which Special Assessments Are Calculated**

Section 40-23-01 requires the executive officer of a city to appoint three "reputable residents and freeholders" of the city to the city's special assessment commission. Pursuant to Section 40-23-07, the special assessment commission is required to determine the lots and parcels of property that will benefit from the improvement and the amount in which each lot and parcel will be benefited. The commission is required to assess against each lot and parcel a fair portion of the total cost of the improvement, which may not exceed the amount each property will benefit from the improvement. As an alternative, Chapter 40-23.1 provides the city governing body may assess benefits against property on a per-square-foot basis and considering the distance of the property from the marginal line of the public way or area improved.

Sections 40-23-09 and 40-23.1-07 require the special assessment commission or the city auditor to prepare a complete list of benefits and assessments showing each lot, tract, or parcel benefited by the improvement and the amount assessed against it. Section 40-23-25 requires the special assessment commission to prepare a list of estimated future assessments on property presently located outside the corporate limits of the city, but likely to be annexed, which the commission determines is potentially benefited by the improvement. Sections 40-23-10 and 40-23.1-08 require the special assessment commission or the city auditor to publish the assessment list in the official newspaper of the city once each week for 2 consecutive weeks and include notice of the time and place the commission or the city auditor will meet to hear objections to assessments by any interested party. The special assessment commission or the city auditor may alter assessments at the hearing, as may be just or necessary, pursuant to Sections 40-23-11 and 40-23.1-09. Sections 40-23-07 and 40-23.1-06 provide property of political subdivisions is not exempt from special assessments.

Any person still aggrieved after consideration by the commission or city auditor may file a written notice of appeal stating the grounds for the appeal pursuant to Sections 40-23-14 and 40-23.1-12. At the regular meeting of the city governing body at which the assessment list is to be acted upon, in accordance with Sections 40-23-15 and 40-23.1-13, any person that has appealed may appear and present the reasons why the action of the commission or city auditor should not be approved. The governing body of the city may increase or diminish any assessment as it deems just.

### **PRIOR LEGISLATIVE MANAGEMENT STUDIES OF SPECIAL ASSESSMENTS**

The 2017-18 interim Taxation Committee reviewed special assessments as part of the committee's larger studies relating to the property tax system. The committee reviewed the procedures for the imposition of special assessments by cities, counties, townships, water resource districts, and recreation service districts. The committee reviewed information relating to the prevalence of special assessments and the amount of special assessments levied by the 10 most populous cities in the state. Fargo had the highest ratio of special assessments to property tax for the 2017 tax year, certifying \$32,081,933 in special assessments and levying \$31,526,029 in property tax. The committee reviewed the types and amounts of special assessment fees charged in the 20 highest population cities in the state and received testimony regarding the use of special assessments from representatives of multiple cities. The testimony indicated the types and amounts of fees charged by cities for special assessments varies widely. The use of city engineers or external engineering services for special assessment projects also varies by city.

The committee reviewed the use of special assessments in other states and reviewed 2001-02 and 2011-12 interim studies relating to special assessments. Based upon legislation discussed during the 2001-02 interim to exclude property owned by a political subdivision from consideration in protests against the formation of a special improvement district, the committee considered a bill to remove property owned by a political subdivision from the total area within an improvement district for purposes of calculating whether protests were received from the owners of a majority of the area of the property included in the proposed district. Testimony regarding the bill noted protests from the owners of a majority of the property area within the proposed districts is required to bar the formation of a district. The committee determined a district could be drawn with more than 50 percent of the property area within the district owned by the political subdivision that would benefit from the creation of the district, thus effectively barring private property owners from protesting the formation of the district. The committee concluded the bill would safeguard against that result. The committee also noted the fairness principal the bill seeks to achieve is sound, but there may be some unintended consequences to excluding property owned by political subdivisions from consideration during the protest period.

The committee received information from representatives of the Bismarck-Mandan Chamber of Commerce and Bismarck-Mandan Development Association regarding a task force formed to address issues relating to infrastructure funding and special assessments. The task force recommended requiring future developers pay the aboveground and belowground costs of a project and build the costs into the purchase price of the lot, rather than using the current system that only requires the developer to pay the belowground costs, leaving the aboveground costs to be assessed to the purchaser. The new approach would eliminate special assessment districts and allow homeowners to amortize the additional lot costs over the life of their mortgage. In regard to special assessments for ongoing maintenance costs, the task force recommended the imposition of a street utility tax to replace special assessment revenue. The tax would appear as a monthly charge on all residential and commercial utility bills. The charge would be determined based on the city's road and street budget needs for each upcoming year. The task force noted the use of a street utility tax would require a legislative change because Section 11-09.1-05 prevents political subdivisions from seeking voter approval of any funding mechanism not in a city's home rule charter before August 1, 2017. Committee members expressed concerns regarding a taxpayer's ability to weigh in on the fee in the future and that a ballot question may be structured so the fee is easy to sell on the front end but could lead to future liability. Committee members indicated legislation should require the ballot language to include certain protections.

The committee reviewed a bill draft that would have required money remaining in a special assessment fund be credited to the property owners in the special assessment district. The committee received testimony from various city representatives regarding the difficulty in administering the bill draft.

The committee reviewed a bill draft that would have increased the amount of the homestead tax credit for special assessments from \$6,000 to \$15,000 and reduced the interest rate charged on the credit from 9 to 6 percent. A second bill was revised to retain the same credit increases from \$6,000 to \$15,000, but linked changes in the interest rate charged on the credit to changes in the consumer price index. The committee received information from a representative of the Tax Department indicating the estimated fiscal impact of the bill would be less than \$5,000 for the 2019-21 biennium. According to the testimony, existing special assessment liens may not be satisfied when property is transferred from parent to child, or in other situations involving transfers using a quitclaim deed. It was noted additional safeguards may need to be added to protect the state's lien.

The committee also reviewed bill drafts to remove the requirement for at least 60 percent voter approval before the governing body of a park district may issue bonds. The bill drafts sought to make bonding a more economical and viable financing option for park districts to allow park districts to move away from using special assessments. The committee considered a bill that would have allowed the issuance of bonds without an election and a bill that allows the issuance of bonds without an election but provides taxpayers with a formal protest period.

### **RECENT LEGISLATION PERTAINING TO SPECIAL ASSESSMENTS**

The 2017-18 interim Taxation Committee recommended three bills relating to special assessments for introduction during the 2019 legislative session. The committee recommended House Bill No. 1041, to increase the amount of the homestead tax credit for special assessments and tie the interest rate applied to the credit to a moving index; Senate Bill No. 2040, to exclude property owned by a political subdivision from consideration in protests against the formation of a special improvement district; and Senate Bill No. 2041, to allow park districts to issue bonds without an election but provide for a formal protest period.

House Bill No. 1041 passed in substantially the same form as the bill as introduced. The only change to the bill following introduction was a reversion of the \$15,000 increased credit limit per property back to the original \$6,000 credit limit per property. Senate Bill No. 2040 also was amended following introduction to further specify that property owned by a political subdivision only is included for purposes of calculating whether the names of the owners of a majority of the area in the proposed district filed a protest if the political subdivision filed a protest. Senate Bill No. 2041 was amended following introduction to eliminate the repeal of provisions allowing a park district to seek voter approval before the issuance of bonds.

Bills introduced during the 2019 legislative session relating to special assessments which failed to pass include House Bill Nos. 1488 and 1307. House Bill No. 1488 would have required a governing body that levied special assessments for improvements to complete an annual review of special assessment revenues and discontinue levying special assessments once collections of special assessment revenues were sufficient to repay debt related to the improvement. House Bill No. 1307 would have required special assessments to be uniformly applied among the same class of property within a single district and would have prohibited the amount assessed against the property from exceeding the special benefit received by the property. The special benefit would have been defined as the increase in the market value of the parcel due the improvement.

## STUDY APPROACH

In reviewing special assessment revenue replacement options, the committee may find it helpful to receive:

1. Information regarding the amount of revenue generated by various special assessment districts;
2. Testimony from property owners regarding the benefits and burdens derived from the imposition of special assessments;
3. Testimony from representatives of the Bismarck-Mandan Chamber of Commerce and the Bismarck-Mandan Development Association regarding the proposed imposition of a street utility tax in lieu of special assessments; and
4. Testimony from representatives of political subdivisions in which special assessments are imposed regarding additional special assessment revenue replacement options.

ATTACH:1