NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

TAXATION COMMITTEE

Thursday, October 2, 2008
Roughrider Room, State Capitol
Bismarck, North Dakota

Senator Bob Stenehjem, Chairman called the meeting to order at 9:00 a.m.

Members present: Senators Bob Stenehjem, Dwight Cook, Ben Tollefson, Constance Triplett, Herbert Urlacher; Representatives Larry Bellew, Wesley R. Belter, Glen Froseth, Craig Headland, Gil Herbel, Jim Kasper, Scot Kelsh, Arlo Schmidt, Benjamin A. Vig, Dave Weiler, Dwight Wrangham

Members absent: Representatives David Drovdal, Mark S. Owens

Others present: Representative Shirley Meyer, member of the Legislative Council, was also in attendance.

See Appendix A for additional persons present.

It was moved by Representative Bellew, seconded by Senator Cook, and carried on a voice vote that the minutes of the July 2, 2008, meeting be approved as distributed.

INCOME TAX STUDY

Chairman Stenehjem called on committee counsel for presentation of a bill draft [90018.0200] to eliminate individual income tax Form ND-2. Committee counsel said the bill draft has only minimal changes from the version previously reviewed by the committee. He said the previous version would have repealed North Dakota Century Code (NDCC) Sections 57-38-02 and 57-38-03 and it was suggested by the Tax Department that these sections not be repealed because they might be useful in administration of remaining income tax laws. He said the sections were removed from the repeal. He said the committee requested that the bill draft be adjusted to make it revenue-neutral. He said the estimated fiscal effect of the bill draft was a revenue gain of approximately $150,000. He said a very small rate change on the lowest income tax brackets in Section 57-38-30.3 is included in the bill draft, which would reduce the lowest bracket tax rate from 2.10 percent to 2.099 percent. He said this is a very small rate change because of the small fiscal effect. He said the income amounts in the income brackets on the five filing categories under Section 57-38-30.3 appear to be substantial increases. He said the reason the increases appear so large is that the statutory income amounts in the brackets are from taxable year 2001 and the underscored income amounts are for taxable year 2009. He said the income brackets are indexed for inflation and nine years of income increases from indexing account for the apparent sizable income increase.

In response to a question from Representative Belter, committee counsel said the bill draft eliminates all of the deductions in NDCC Section 57-38-01.2 which apply only on Form ND-2. He said those exemptions are not transferred by the bill draft to Form ND-1.

Representative Froseth said he receives inquiries from constituents about why they are unable to use their income tax deduction. He said because some deductions are available only on Form ND-2, taxpayers cannot use the deduction on Form ND-1, and they are disappointed that the deduction is not usable.

Committee counsel said the bill draft was prepared to be revenue-neutral, based on current income tax rates. He said if the initiated measure to reduce income tax rates on the November general election ballot is approved by the voters, the income tax bracket changes in the bill draft could be eliminated because revenue neutrality will not be an issue if the Form ND-1 rates are reduced by 50 percent.

Chairman Stenehjem called on Ms. Kathy Strombeck, Research Analyst, Tax Department, for a presentation of information (Appendix B) on the estimated fiscal effect if initiated measure No. 2 is enacted by the voters. Ms. Strombeck said the estimated biennial fiscal impact is a revenue reduction of $414,237,000, which is a revenue reduction for individual income tax of $375,983 and for corporation income tax of $38,254,000.

Ms. Strombeck said the information provided also has statistics relating to the potential effect of initiated measure No. 2 if there is a continuation of the property tax relief income tax credit in 2007 Senate Bill No. 2032. She said through September 30, 2008, 28,613 property tax certificates have been issued to taxpayers. She said if a property tax credit program is continued and initiated measure No. 2 is enacted by the voters, the number of certificates would increase to approximately 43,118.

Ms. Strombeck said of the estimated corporate income tax reduction that would be provided by enactment of initiated measure No. 2, approximately 42 percent of the tax relief would go to the top 25 corporations. She said approximately 93 percent of the tax reduction would go to multistate and multinational corporations. She said this effect is because these corporations pay the greatest share of corporate income taxes.

Ms. Strombeck said the tables provided on the information she distributed to committee members show the approximate tax reduction for taxpayers in each designated income bracket if initiated measure No. 2 is enacted.

In discussion of the bill draft to eliminate Form ND-2, Senator Cook asked whether taxpayers making contributions or other expenditures for which a deduction is available in February or March 2009 would lose that deduction if the bill draft is enacted by the 2009 Legislative Assembly. Committee counsel said the effective date of the bill makes it apply to the 2009 taxable year and if taxpayers make contributions or expenditures in February or March in anticipation of a tax deduction on Form ND-2, the deduction would be lost for that taxable year if the bill is enacted. He said taxpayers making contributions or expenditures in anticipation of deductions on Form ND-2 already face the possibility that the deduction will not be available if their tax liability on Form ND-1 ends up being lower at the end of the tax year.

Senator Cook said he believes it is inappropriate to recommend the bill draft and make it effective for the 2009 tax year if taxpayers might qualify for deductions that would be taken away by passage of the bill.

It was moved by Senator Cook, seconded by Senator Triplett, and carried on a voice vote that the effective date of the bill draft be amended to be effective for taxable years beginning after December 31, 2009.

Representative Kasper asked Ms. Strombeck what savings would exist for the Tax Department by elimination of Form ND-2. Ms. Strombeck said savings to the Tax Department would total about $25,000 per biennium. Representative Kasper said it appears there would be minimal savings to the state from elimination of Form ND-2. He said he does not see the problem that would be solved by eliminating Form ND-2.

In response to a question from Senator Stenehjem, Ms. Strombeck said many individuals who file the Form ND-2 return do so in error. She said they would be helped by eliminating that filing approach because they would have to file on the correct form to minimize income tax liability. She said eliminating Form ND-2 would reduce tax preparation confusion and expenses for taxpayers.

Representative Kasper asked whether any taxpayer would have to pay more income tax without Form ND-2. Ms. Strombeck said some taxpayers would pay more income taxes without Form ND-2.

Senator Triplett asked whether it would be possible to move deductions and credits available on Form ND-2 to make them available on Form ND-1. Committee counsel said deductions and credits could be moved individually or as a group from Form ND-2 to Form ND-1. He said the bill draft does not move any deductions or credits currently available only on Form ND-2 and all of those deductions and credits are eliminated by the bill draft.

Representative Kasper said he would not favor elimination of Form ND-2. He said eliminating that filing option amounts to a tax increase for certain citizens, many of whom are retired.

Representative Wrangham said many people do not get to use deductions or credits because they are available only on Form ND-2. He said these individuals would benefit from moving those deductions or credits to Form ND-1. Senator Stenehjem said that is true but the deductions and credits available only on the long form would have a substantial fiscal impact from moving them to the short form. He said this is where it becomes difficult for the Legislative Assembly to make a judgment about the appropriateness of each credit or deduction and whether it should be available on Form ND-1, which has a lower tax rate.

Representative Kasper said if the bill draft addressed moving deductions to Form ND-1, it would be more appropriate but without that change he cannot support the bill draft.

Representative Belter said each deduction or credit is an individual issue. He said each deduction or credit has been approved separately by the Legislative Assembly at some time in the past. He said it would not be appropriate to move all of the deductions or credits to Form ND-1 without individual consideration of each one.

AGRICULTURAL ASSESSMENT

Chairman Stenehjem called on committee counsel to review a bill draft [90249.0100] to extend the deadline for county implementation of use of soil survey data in agricultural property assessments. Committee counsel said a provision was added to NDCC Section 57-02-27.2 by 2007 legislation to impose a penalty of 5 percent of the county's allocation from the state aid distribution fund if the county has not fully implemented use of soil type and soil classification data from soil surveys for taxable years after 2009. He said the bill draft extends the deadline through taxable year 2011. He said the committee has received information on county efforts to implement use of soil survey data in assessments. He said the information received indicates that all counties are at least in the process of trying to implement use of soil surveys but it appears some counties will not be able to meet the 2010 deadline.

Senator Urlacher said a few counties remain which have not implemented use of soil surveys. He said if an extension of time is warranted that is fine with him, but the Legislative Assembly needs to keep the penalty requirement in the law to achieve uniform assessment of agricultural property in the state.

In response to a question from Senator Stenehjem, Ms. Sara Hewson, Tax Department, said she has completed a recent review of county efforts to implement use of soil surveys in assessments. She said 19 counties are in the early stages of implementation, 13 counties are in the transition stage, and 21 counties are compliant with the required use of soil surveys and agricultural assessments. In response to a question from Senator Cook, Ms. Hewson said she is in the process of contacting counties regarding the current status of implementation. She said information on current status will be available during the 2009 legislative session.

Senator Cook said he believes it is important to keep moving counties forward toward soil survey implementation to provide uniformity across the state.

Senator Urlacher said soil survey use has been required by law for many years. He said it was necessary to force compliance and it is important to keep the penalty provision in law to encourage completion of the assessment improvement.

Representative Schmidt said he thinks the bill draft is a good bill. He said this will give counties additional time to complete the necessary work to upgrade assessments.

It was moved by Senator Triplett, seconded by Senator Urlacher, and carried on roll call vote that the bill draft to extend the deadline for county implementation of soil survey use in agricultural property assessments be approved and recommended to the Legislative Council. Voting in favor of the motion were Senators Stenehjem, Cook, Tollefson, Triplett, and Urlacher and Representatives Bellew, Belter, Froseth, Headland, Herbel, Kasper, Kelsh, Schmidt, Vig, Weiler, and Wrangham. No negative votes were cast.

INCOME TAX STUDY

It was moved by Representative Headland and seconded by Representative Froseth that the bill draft to eliminate income tax Form ND-2 be approved and recommended to the Legislative Council.

Representative Schmidt said some taxpayers benefit from the existence of Form ND-2 so he would not support eliminating use of that form.

In response to a question from Representative Herbel, committee counsel said if initiated measure No. 2 is approved, there would be no need for Form ND-2 because the initiated measure only reduces the rates on Form ND-1 and the resulting reduction would make use of deductions and credits on Form ND-2 of no benefit. He said if that happens, the rate changes in the bill draft could be removed because revenue neutrality would no longer be an issue.

Representative Belter said he believes many taxpayers pay too much for tax preparation of alternative income tax forms. He said he believes the benefit of eliminating that cost for all taxpayers outweighs the loss to the few taxpayers who benefit from the existence of Form ND-2.

Representative Kasper said he cannot support the bill draft because it amounts to a tax increase for some taxpayers.

Senator Urlacher said the existence of Form ND-2 is always a minor consideration in income tax legislation. He said elimination of Form ND-2 would focus attention of taxpayers and legislators on Form ND-1 where the attention should be focused.

Senator Stenehjem said he believes that taxpayers can direct tax preparers to just prepare Form ND-1 to avoid the additional cost of preparing alternative forms.

Senator Tollefson said this bill draft could be introduced by individual legislators if initiated measure No. 2 is approved and makes Form ND-2 obsolete. He said he does not think the committee should approve this bill draft at this time.

The motion failed on a roll call vote. Voting in favor of the motion were Senators Triplett, and Urlacher and Representatives Belter, Froseth, Headland, Herbel, Weiler, and Wrangham. Voting in opposition to the motion were Senators Stenehjem, Cook, and Tollefson and Representatives Bellew, Kasper, Kelsh, Schmidt, and Vig. The chairman declared the motion failed for lack of a majority.

STREAMLINED SALES TAX PROJECT

Chairman Stenehjem called on Senator Cook for presentation of an update on activities of the Streamlined Sales Tax Governing Board. Senator Cook distributed a copy of the *2008 Annual Report* (Appendix C) of the Streamlined Sales Tax Governing Board.

Senator Cook said there are 19 states in full compliance under the Streamlined Sales Tax Agreement compared to 15 states in 2007. He said there were 1,100 remote sellers registered with the Streamlined Sales Tax Governing Board at the end of June and those sellers collected more than $135 million in sales taxes in streamlined states during the fiscal year. He said the governing board has amended the agreement to provide an alternate origin sourcing rule that will greatly assist several states in becoming members.

Senator Cook said Congress has under consideration two bills that would overturn the *Quill v. North Dakota* decision, which prevents states from collecting sales taxes from remote sellers. He said it appears the biggest impediment to passage of legislation by Congress is the small business exemption. He said an exemption is provided to small businesses, defined as businesses with less than $5 million in sales. He said the governing board is working on that issue. He said it appears the chances of passage of legislation by Congress to overturn *Quill* are improving.

OIL AND GAS TAX REVENUE ALLOCATION STUDY

Chairman Stenehjem called on Mr. Jeff Engleson, Director, Energy Development Impact Office, for a presentation (Appendix D) relating to the 2008 oil and gas impact grant round.

Mr. Engleson said the 2008 grant round consisted of 265 grants totaling $3 million to 241 political subdivisions. He said 376 grant requests were received totaling $29.1 million.

Mr. Engleson said financial need is the primary factor in determining grant allocations. He said most county governments received no grants this year because they received the largest share of gross production tax revenue allocations. He said disqualifying factors applied in evaluating grant applicants include a large cash balance on hand, a low mill levy, or large amounts of unused grants from previous years. He said transportation and fire protection needs have historically received the majority of grants. He said during the 2008 grant round, over 75 percent of funds were allocated to transportation projects and over 17 percent went to support fire protection services. He reviewed the historical data he provided relating to grant awards by government function for the years 2002 through 2008 and grant requests and awards by political subdivision from 1999 through 2008.

Senator Urlacher asked whether grants are made to counties where oil industry traffic exists but there is not a significant level of oil production. Mr. Engleson said grants are made according to impact and not production. He said Golden Valley and Slope Counties received grant funding but have little oil and gas production. He said the grants to those counties were attributable to traffic from oil industry activity related to production in other counties.

Chairman Stenehjem called on committee counsel for presentation of a memorandum entitled *Oil-Producing States' Funding Allocation to Political Subdivisions*.

Committee counsel said examination of laws of oil-producing states shows a wide range of tax and revenue allocation structures. He said it appears each state has developed a unique structure for delivery of revenues to political subdivisions affected by oil and gas development and production. He reviewed provisions for revenue allocation in Kansas, Colorado, Wyoming, and Montana. He said North Dakota has developed a very sound approach to allocating revenue to political subdivisions. He said North Dakota's approach involves direct statutory allocation of a share of oil and gas tax revenues to producing counties for allocation among the county and cities and school districts in the county. He said the other important component of North Dakota funding is the impact grant program, which allocates funds among political subdivisions based on applications that demonstrate need attributable to oil and gas development. He said the impact grant program provides flexibility to address funding needs that change as impacts and needs change, which is impossible to do through a statutory allocation formula. He said the allocation formula and grant program work well together and the issue that requires legislative monitoring is whether the appropriate amounts of revenue are available through these programs.

Chairman Stenehjem called on committee counsel for presentation of a bill draft [90317.0100] to remove limits on amounts the oil impact fund and counties may receive under the oil and gas gross production tax. Committee counsel said under current law the first 1 percent of gross value at the well of oil and gas gross production tax is allocated one-third to the impact grant fund, but not exceeding $6 million per biennium, and the remainder is allocated to the state general fund. He said the bill draft eliminates the $6 million per biennium limit on deposits in the oil and gas impact grant fund. He said there is a statutory allocation formula to divide oil and gas gross production tax revenue between the producing county and the state general fund. He said limitations are placed on the statutory allocation formula so that producing counties may not receive more than the statutory dollar amount, which is based on the population of the county. He said the most a county may receive under these limitations is $4.6 million per year plus an additional $1 million per year if the county levies 10 mills or more for road purposes. He said all of the limitations on the amount counties may receive based on population are eliminated by the bill draft. He said some counties have not reached their statutory allocation limits based on current production levels, but some counties have exceeded their statutory allocation limits and would benefit substantially from eliminating the caps. He said the Tax Department will provide information on the fiscal effect of the bill draft.

Chairman Stenehjem called on Ms. Strombeck for a presentation of information (Appendix E) on estimated fiscal effect of the bill draft to remove caps on county allocations and impact grant fund allocations. Ms. Strombeck said removing caps on statutory allocations of revenue to producing counties would reduce state general fund or permanent oil tax trust fund revenue from the oil and gas gross production tax by $42 million per year. She said most of the benefit of the increased revenues to counties would be received by Bowman and Mountrail Counties, which would receive a combined total of more than $30 million per year additional revenue. She said eliminating the $6 million cap on deposits in the oil and gas impact grant fund would increase revenues to the impact grant fund by $28.4 million per biennium, with a corresponding reduction in permanent oil tax trust fund revenue. She said the impact of the changes would be a reduction in permanent oil tax trust fund revenue because revenues will exceed the $71 million general fund limit under current law and the $100 million general fund limit under the proposed constitutional amendment to establish a permanent oil tax trust fund.

Senator Tollefson asked whether passage of initiated measure No. 1 in the general election would affect the estimated allocations. Ms. Strombeck said the allocations would still occur because the allocations are made before deposit of revenues in the state general fund, which is the triggering event for determining allocations to the permanent oil tax trust fund.

Senator Cook said it appears likely that the amount of additional revenue to Bowman County would wipe out the need for property taxes in Bowman County.

Representative Kasper asked whether counties receiving additional revenue by removing the caps would be required by law to reduce property taxes. Committee counsel said the bill does not require property tax reductions and existing law probably would not mandate property tax reductions, but politically the voters of the county may expect a property tax reduction if the additional revenues are received.

Senator Triplett said there is a serious need for additional funding to address costs political subdivisions in the oil impact area are experiencing. She said the amount of additional funds required is arguable but the current allocation is inadequate.

Representative Froseth said oil-producing counties would appreciate the removal of caps on deposits in the impact fund. He said it is important to enhance this source of funding to address oil development impact.

In response to a question from Senator Triplett, Mr. Engleson said the $29 million in grant funds requested was for one year and grant requests could total approximately $60 million per biennium.

Senator Urlacher said the needs of political subdivisions must be addressed if they are to provide the services required by their residents and the oil industry. He said the oil industry is an important component of the economy of the state and adequate funding to political subdivisions will continue to be an issue in the future.

Representative Kasper asked whether the committee knows what the oil-producing counties would request in additional funding and whether that agrees with the added amounts they would get under the bill draft.

Senator Urlacher said funding to oil-producing counties needs to be addressed by the Legislative Assembly. He said the need for additional funding is there.

Senator Stenehjem said the elimination of caps on allocations to counties would provide no additional revenue to several counties, such as Slope and Bottineau Counties.

Representative Meyer said oil development impacts occur and change very quickly. She said counties that would receive added revenue under the bill draft are the counties where the impact is occurring.

Representative Froseth said he would urge committee members to visit the oil development areas in the state to see firsthand the level of impact being experienced.

Senator Triplett said Senator Stenehjem is correct that some counties would receive no additional revenue under the allocation formula but those counties would benefit from eliminating the cap on the impact grant fund, which may be of benefit to them when greater levels of oil development occur.

In response to a question from Representative Meyer, Ms. Vicky Steiner, Association of Oil and Gas Producing Counties, said the recent study reviewed at the previous committee meeting estimated impact needs in the oil and gas-producing counties at an additional $35 to $46 million per year. Ms. Steiner said oil and gas-producing counties appreciated the increase by 25 percent in funding provided by 2007 legislation, but the counties experiencing the greatest impact require additional funding to meet impact costs.

Representative Froseth asked Ms. Steiner if oil companies are helping local governments with oil development impact costs and whether estimates would be available on their direct contributions. Ms. Steiner said the association can investigate that issue but there are many instances of oil companies providing funding for specific projects.

Representative Headland asked if there is a more efficient way to move petroleum than by truck. Ms. Steiner said during the initial boom of oil exploration there is a traffic problem. She said after production settles in an area, road traffic will diminish. She said the exploration phase has the heaviest levels of impact from traffic.

Representative Kasper said his concern with the bill draft is that some counties would receive more funds than they need and some would receive not enough funds by removing all caps on allocations to counties. He said more careful consideration is needed to adequately allocate funds instead of simply removing caps.

Senator Cook said it would be interesting to see data on the location of wells that are in the first five years of production. He said he believes a recent study reported in the news indicated a cost of $8 million per year in road impacts from the Spiritwood malting plant. He said the state needs a program for road impacts across the state that is consistent and provides additional funding wherever it is needed. He said there is a need for additional funds for oil impact to roads but part of the consideration should include examining the local property tax effort for roads and that approach should be applied statewide.

Representative Meyer said the oil industry is different from other industries. She said oil companies are paying combined oil taxes of 11.5 percent that other industries do not pay. She said she thinks it is reasonable for residents of the production area and oil companies to expect some of those taxes to come back to the area to address impact from development.

Representative Belter said the Legislative Assembly will have to address oil impact funding and the issue appears to be how to determine the appropriate amount of money necessary. He asked

Ms. Steiner whether the members of the Association of Oil and Gas Producing Counties are in agreement among themselves on what is fair. Ms. Steiner said the association had an annual meeting last week but will be having more meetings before the legislative session to discuss that issue.

Senator Triplett said as an oilfield develops and pipelines are put in place, roads will still be needed to carry industry traffic. She asked whether Bakken Formation wells will have to be refractured at some point. Mr. Ron Ness, North Dakota Petroleum Council, said the industry does not know yet how refracturing might be used in the future for Bakken wells. Mr. Ness said the general rule is that money from tax revenues follows the areas of production and impact follows the drilling rigs. He said that is why the impact fund is important.

Senator Cook asked whether it is possible to identify young wells. Mr. Ness said young wells can be identified but that still will not locate where drilling is taking place and impact is occurring. Mr. Ness said the Petroleum Council would support additional funding to the impact fund and possibly emergency allocation of additional impact funds. He said it is likely that large impact and funding demand will be coming in new areas of the state.

Senator Tollefson asked whether Mr. Ness would recommend the removal or adjustment of caps on county and impact funding. Mr. Ness said it appears clear an increase is necessary but it is hard to determine exactly how much.

Chairman Stenehjem called on Mr. Dan Brosz, Bowman County engineer, for comments on the committee's study. Mr. Brosz said the end of drilling for oil is not the end of road impact. He said there are several secondary drilling rigs operating in Bowman County and infrastructure related to oil production often gets moved. He said county impacts from oil development involved more than road impact. He said in Bowman County, the county has agreed to help with necessary improvements to a township road to the tune of $1.1 million because the need is there and the township cannot afford the cost of the road improvement.

It was moved by Senator Triplett, seconded by Representative Froseth, and carried on a roll call vote that the bill draft relating to eliminating caps on the amount the oil impact fund and counties may receive under the oil and gas gross production tax be approved and recommended to the Legislative Council. Voting in favor of the motion were Senators Stenehjem, Tollefson, Triplett, and Urlacher and Representatives Bellew, Belter, Froseth, Headland, Herbel, Kasper, Kelsh, Schmidt, Vig, Weiler, and Wrangham. Voting in opposition of the motion was Senator Cook.

PROPERTY TAX STUDY

Chairman Stenehjem called on Ms. Marcy Dickerson, State Supervisor of Assessments, Tax Department, for presentation of testimony (Appendix F) relating to information requested by the committee at the previous meeting. Ms. Dickerson said she was requested to extend by five additional taxable years the information presented on the graph attached to her testimony relating to the trend in true and full valuation for agricultural, residential, and commercial property. She said the graph covers the taxable years 1999 through 2008.

Ms. Dickerson said the second attachment to her testimony presents data on statewide effective tax rates for agricultural, residential, and commercial property from 1983 to 2007. She said for agricultural property, the data shows the estimated tax rate based on the statutory agricultural valuation formula and the estimated tax rate on estimated market value of agricultural land as determined from results of the sales ratio study.

Ms. Dickerson said the third attachment to her testimony is based on comparison of two sample parcels of agricultural property in Morton County for the years 1982 through 2007. She said the information presented shows the valuation, mill rate, and property taxes for each year for the two sample parcels.

Ms. Dickerson said the fourth attachment to her testimony shows the reported number of residences for counties that responded to a question on this topic, which were formerly exempt as farm residences but have been added to the tax rolls for 2008. She said the question was asked how many farm residences have been sold by a farmer to a nonfarmer and to the extent that has occurred, it is reflected in the information provided. She said the information provided also includes residences of farmers who formerly qualified for the farm residence exemption but no longer qualify for reasons such as an increased amount of nonfarm income. She said it appears from the information received from counties that some county tax officials are more diligent than others in identifying residences that no longer qualify for the farm residence exemption.

Senator Cook said there appears to be a shift of property tax burden among property classes. He asked how that shift can be controlled without altering how properties are assessed and whether control of political subdivision budgets would control the shift. Ms. Dickerson said it is very difficult to address those questions. She said much of the difference in valuation that tends to shift property tax burdens over time is attributable to valuation of residential and commercial property based on market value and valuation of agricultural property based on a statutory productivity valuation formula.

Senator Cook said the shift of property tax burden among property classifications when valuations change is a concern. He said the question that must be determined is how to keep that from happening. He said this is a difficult issue to address under current assessment laws. He said market value does not affect the valuation for tax purposes for agricultural land. He said because market value does affect other property types, there is a difference that adds to the shift of property tax burdens to those property classifications. He said he is not sure that there is any way the budget process could control that shift.

Chairman Stenehjem invited committee discussion relating to conclusion of the committee property tax study. Committee counsel said it appears the committee has been unable to reach a consensus recommendation regarding property tax relief because of external considerations. He said the most viable options for consideration appear to be providing funding to political subdivisions to reduce property tax levies or following the approach of 2007 Senate Bill No. 2032 and providing income tax credits for a portion of property taxes paid. He said each of these options became complicated by developments during this interim. He said the Governor has announced the intention to introduce legislation to provide $200 million or more in the 2009-11 biennium for statewide school district mill levy reductions. The Governor's proposal is intended to replace the current property tax relief allocation based on the income tax system. To assure that property tax relief will result, the Governor's proposal calls for reduction in school district general fund levy authority equal to $200 million. The Governor also recommends $100 million additional funding for allocation to school districts without the requirement of property tax levy reduction. He said the details of how the funds will be allocated among school districts and how property tax levy authority limitations will be imposed have not been made public. He said this makes it difficult for the committee to either react to the proposal or initiate consideration of a similar proposal. He said the option of providing property tax relief through the income tax system is complicated by the pending initiated measure No. 2 on the general election ballot, which would reduce individual income tax rates by 50 percent. He said the committee has monitored implementation and administration of the income tax credit for property tax relief under 2007 Senate Bill No. 2032 and one of the significant difficulties with that approach is the number of certificates issued to taxpayers who have property tax credits exceeding income tax liability. He said the number of individuals who would be in that situation would be greatly increased by approval of initiated measure No. 2, which would make the income tax credit option much less attractive. Senator Urlacher said he would agree that those considerations have limited the options for consideration by the committee.

Senator Cook said a portion of the study directive to the committee called for pursuing a goal of reducing each taxpayer's annual property tax to an amount that is not more than 1.5 percent of the true and full value of property. He said that goal has not been met. He said there is a need to address why three property classifications are subject to different statutory valuation factors that lead to a shift in property tax burden among classifications.

COMMITTEE DISCUSSION

It was moved by Representative Weiler, seconded by Representative Bellew, and carried on a roll call vote that the chairman and the staff of the Legislative Council be requested to prepare a report and the bill drafts recommended by the committee and to present the report and recommended bill drafts to the Legislative Council. Voting in favor of the motion were Senators Stenehjem, Cook, Tollefson, Triplett, and Urlacher and Representatives Bellew, Belter, Froseth, Headland, Herbel, Kasper, Kelsh, Schmidt, Vig, Weiler, and Wrangham. No negative votes were cast.

Representative Belter said he has had a bill draft prepared which he intends to introduce in 2009 to provide a sales tax exemption for clothing purchases. He distributed copies of the bill draft [90183.0100] to committee members. He said he wants to provide committee members advance notice of the proposal. Senator Cook asked whether the exemption for clothing is compliant with the Streamlined Sales Tax Agreement. Committee counsel said the bill draft was prepared to follow the Streamlined Sales Tax Governing Board definition of clothing.

Representative Kasper said he has been working with the Legislative Council staff on two separate bill drafts intended to address property tax reform and property tax relief. He said he wants committee members to know that he intends to introduce proposals on these topics in 2009.

Representative Herbel said he hopes the Legislative Assembly will consider legislation similar to the early versions of 2007 Senate Bill No. 2032 during the next legislative session. He said he believes the early versions of the bill draft followed the correct approach in allocating funds to school districts based on tax levies and requiring reduction in levy authority.

It was moved by Representative Belter, seconded by Senator Cook, and carried on a voice vote that the committee be adjourned sine die. Chairman Stenehjem adjourned the committee sine die.

John Walstad
Code Revisor

ATTACH:6