NORTH DAKOTA LEGISLATIVE MANAGEMENT

Minutes of the

TAXATION COMMITTEE

Wednesday, February 3, 2010
Roughrider Room, State Capitol
Bismarck, North Dakota

Senator Dwight Cook, Chairman, called the meeting to order at 9:00 a.m.

Members present: Senators Dwight Cook, Jim Dotzenrod, Joe Miller, George Nodland, Tracy Potter, Bob Stenehjem; Representatives Wesley R. Belter, David Drovdal, Robert Frantsvog, Glen Froseth, Jim Kasper, Louis Pinkerton, Arlo Schmidt, Gary R. Sukut, Dave Weiler, Dwight Wrangham

Members absent: Senators John M. Andrist, Constance Triplett; Representatives Larry Bellew, Craig Headland, Scot Kelsh, Lonny Winrich

Others present: Senator David O'Connell and Representative Shirley Meyer, members of the Legislative Management, were also in attendance.

See Appendix A for additional persons present.

It was moved by Representative Drovdal, seconded by Senator Stenehjem, and carried on a voice vote that the minutes of the previous meeting be approved as distributed.

LIGNITE ENERGY COUNCIL

Chairman Cook called on Ms. Sandi Tabor, Vice President of Administration and Policy Development, Lignite Energy Council, to provide information (Appendix B) on the potential impact of pending and proposed federal legislation and regulations on the lignite industry.

Ms. Tabor said Congress is having a hard time finding common ground on proposed cap and trade legislation. She said proposed federal legislation and regulation is the No. 1 issue to the lignite industry. She reviewed the features of the Waxman-Markey bill, the Kerry-Boxer bill, and the Senate energy bill.

Ms. Tabor said economic analysis of the effects of the Waxman-Markey bill projects job loss in North Dakota in the year 2030 in the range of 5,310 to 7,234 jobs. She said the analysis estimates a decrease in disposable income of $116 to $234 per year per household in North Dakota in 2020, which would become a decrease in disposable income per year per household of $762 to $1,252 in the year 2030. She said the proposal threatens the viability of the lignite industry and the economic health of North Dakota.

Senator Cook asked where our electricity will come from when the lignite industry ceases to be able to provide electricity. Ms. Tabor said that is a good question. She said proponents of the legislation forecast replacement through increases in renewable energy production. She said the issues will be how much money the industry can afford to spend to generate replacement energy and whether that energy will be affordable to the public.

Senator Potter said he understands that wind energy cannot stand alone as a power source. Ms. Tabor said that is correct and the reason is that wind energy cannot be stored. She said energy storage technologies must be improved to make wind energy viable and those technologies are the basis of current study efforts.

Representative Pinkerton said North Dakota coal, Wyoming coal, and West Virginia coal have differing qualities and Btu content. He asked whether North Dakota lignite will remain competitive as the tax and regulatory climate changes. Ms. Tabor said it is commonly understood that lignite is low-grade coal with high moisture content. She said efforts are underway to improve lignite quality and Btu value by removing moisture or making other physical changes. She said if these efforts are successful, North Dakota lignite will become more competitive with other coal varieties.

Ms. Tabor said the economic impact of the Waxman-Markey bill would impose a much heavier cost to central and southern states than to the other states of the United States.

Ms. Tabor said cap and trade is not the only issue of concern. She said Environmental Protection Agency (EPA) regulation of the lignite industry is another potential threat to the viability of the industry. She said in December 2009 the EPA made the "endangerment finding" that carbon dioxide is a greenhouse gas. She said sulfur dioxide, ozone, and nitrogen oxide have also been identified by the EPA as greenhouse gases. She said these findings set the stage for EPA regulation of the coal industry.

Ms. Tabor said new regulations by the EPA would cause dramatic increases in compliance spending by the coal industry. She said the lignite industry has already spent substantial amounts to reduce emissions and is scheduled to make further expenditures that will result in reduced emissions and capture of carbon dioxide. She said at some point, there are diminishing returns on these investments by the industry.

Ms. Tabor said the Murkowski resolution would effectively veto the endangerment finding made by the EPA. She said the measure could come to the Senate floor for a vote in late February or early March.

She said Representative Earl Pomeroy has introduced similar legislation in the House of Representatives, which has not been scheduled for hearing. Ms. Tabor said other pending federal issues include proposals to regulate coal combustion products as hazardous waste. She said another proposal is a stream buffer zone rule that would prohibit mining coal within 100 yards of a stream. She said this also would include streams with intermittent flow of water during spring runoff. She said the proposed rule is aimed at mountaintop mining in Appalachia, but it would also seriously impact North Dakota mining operations. She said the Clean Water Restoration Act, also known as the "birdbath law," would change the historical definition of navigable waters to give the federal government jurisdiction of all waters, including small, isolated wetlands. She said this would result in a huge expansion of federal control and potential impact.

Representative Pinkerton asked how much of the opposition at the federal level to coal-fired generation comes from the natural gas industry. Ms. Tabor said it is uncertain how much opposition comes from the natural gas industry. She said there is a current excess capacity of natural gas and there will be a probable increase demand for natural gas in the future.

Ms. Tabor said another area of concern is use of the court system to attack coal-fired electric generation. She said two circuit courts have allowed states and individuals to sue greenhouse gas emitters on nuisance grounds. She said a similar suit is pending in the Ninth Circuit. She said suits of this kind pose another danger of substantial expenditures for the industry.

Representative Froseth asked what developments have occurred after legislative approval of the beneficiated coal legislation. Ms. Tabor described efforts that led to a patented beneficiated process. She said the significant issue for consideration is marketing beneficiated coal and the Lignite Energy Council is undertaking study of marketing.

Representative Belter said he recently attended a meeting at which the apparent consensus was that there will be a shift from emphasis on cap and trade legislation through Congress and the President of the United States to increase efforts at the EPA and court regulation and restriction of the coal industry. He said EPA regulation is likely to decimate the energy and agriculture industries. He said he believes we need Congress to keep jurisdiction and not abdicate its authority to the EPA and the courts.

Senator Potter asked if the forecasted loss-of-jobs data provided by Ms. Tabor are estimates of net employment changes which also consider jobs created by growth in renewable energy and carbon storage employment. Ms. Tabor said she believes that is the case but she will check.

OIL INDUSTRY

Chairman Cook called on Mr. Lynn Helms, Director, Department of Mineral Resources, Industrial Commission, for a presentation of mineral development information (Appendix C) requested by the committee.

Mr. Helms said uranium deposits in North Dakota are found within 1,500 feet of the surface. He displayed a map identifying known uranium deposits in North Dakota. He said uranium prices reached approximately $140 per pound in 2007, which spurred an increase in exploration activity. He said the price of uranium is currently in the range of $40 to $50 per pound, but interest in exploration persists.

Mr. Helms said at this time only exploration has occurred in North Dakota with regard to uranium. He said there are two active exploration permits for Billings and Slope Counties. He said he expects exploration work will be finished in 2010. He said his best guess for initiation for uranium mining activity is three years to five years, and 2013 would be the earliest he would expect uranium mining to begin. He said numerous state and federal permits are required before the initiation of uranium mining, which will delay the initiation of mining activity.

Mr. Helms provided information on uranium severance tax rates in Colorado, Montana, Nebraska, South Dakota, and Wyoming.

Mr. Helms said dramatic increases in potash prices spurred interest in potash deposits in North Dakota. He said potash prices have dropped from approximately $850 per ton to $400 per ton in the last 12 months. He said potash permitting and discussions of leasing have occurred. He said he expects one or more potash exploration permits to be issued in 2010. He said his best guess for initiation of potash mining activity is that mining would begin in 2013 at the earliest.

Representative Meyer asked whether uranium mining in the state would be surface mining or in situ leach mining. Mr. Helms said perhaps both mining methods could be used in North Dakota. He said recently shallow uranium deposits have been identified that could be surface-mined.

In response to a question from Representative Weiler, Mr. Helms said from 1963 to 1968 there was mining of uranium in North Dakota but there were no taxes imposed by the state.

Representative Drovdal asked whether extensive supplies of fresh water would be needed for extraction of potash. Mr. Helms said water is needed for potash mining and there is not a substantial supply of fresh water along the northern border so there could be a water cost and permitting issue for potash mining.

Mr. Helms said in the oil and gas industry, growth is strong, and the prospects are good for future development. He said 92 drilling rigs are operating in the state, and the number of producing wells continues to increase. He said the Industrial Commission has established new records for action on drilling permits in each of the last two years. He said he has met with the most active drilling operators in North Dakota, and as a result of these discussions, he expects North Dakota to be at approximately 120 drilling rigs by the end of 2010.

Mr. Helms said review of well completion reports shows that the oil industry continues to improve its efficiency in drilling. He said drilling time per well has been reduced to approximately 20 days. He said at that rate, each drilling rig could complete 15 wells per year and 100 to 120 drilling rigs could complete 1,500 to 1,800 new wells per year. He said that rate of drilling new wells could continue for the next 10 years to 15 years.

Mr. Helms said the substantial number of new wells that are likely to be drilled in the next 10 years to 15 years will increase water demands. He said water use is approximately 1.5 million to 4 million gallons per well. He said drilling operations do not require treated water, but the water source must provide a uniform supply in terms of mineral and sediment content. He said ground water supplies are not adequate for drilling use because of variable mineral and sediment content.

Mr. Helms said North Dakota oil production is expected to peak in the range of 300,000 to 400,000 barrels of oil per day and remain in that range for several years. Representative Kasper said the graph displayed by Mr. Helms shows oil production leveling off in about 2011. He asked why the production levels off. Mr. Helms said at some point the production decline from existing wells catches up to the production increase from new drilling and at that point total production will level off.

Mr. Helms said the oil and gas development on the Fort Berthold Reservation has been rapid since the Legislative Assembly authorized the agreement between the Governor and the Three Affiliated Tribes to govern regulation and taxation of oil and gas activity. He said only one well was completed in the 20 years preceding the effective date of the agreement of July 1, 2008. He said since the agreement took effect, 160 new wells have been completed on the Fort Berthold Reservation, including 40 new wells on trust lands. He said new wells on trust lands are producing approximately 6,200 barrels of oil per day. He said there are currently 19 rigs drilling within the Fort Berthold Reservation, including 9 on trust lands.

Mr. Helms said pipeline capacity for movement of crude oil was a concern, but North Dakota currently has excess export capacity. He said existing pipeline capacity and the additional carrying capacity of the EOG rail facility from Stanley provide excess capacity and projects in planning and development should keep carrying capacity ahead of projected oil production.

Senator Stenehjem asked how North Dakota compares to Montana in development of oil resources of the Bakken Formation. Mr. Helms said North Dakota is far ahead of Montana in this respect, and the Montana field has declined in production. He said Montana producers will go back to drilling in the Bakken Formation with improved technology, which should increase Montana production.

Mr. Helms said natural gas pipeline expansions have provided significant capacity for exporting natural gas. He said he hopes natural gas processing will increase to take advantage of the pipeline capacity, but production is not at that level yet.

Representative Meyer asked whether the drilling rigs moving into North Dakota bring their own drilling crews or hire local employees. Mr. Helms said they try to hire locally but also bring their own crews because experienced operators are necessary. He said lack of housing is a growing issue in the oil production area.

Chairman Cook called on Mr. Ron Ness, President, North Dakota Petroleum Council, for presentation of information (Appendix D) in response to committee requests. Mr. Ness said we can look at 2007 as a historic year for North Dakota legislation to benefit development and marketing North Dakota oil and gas. He said in 2007 legislation was enacted to authorize the tribal agreement which has led to new activity in the Fort Berthold Reservation and the North Dakota Pipeline Authority was established which has helped bring North Dakota oil and gas pipeline capacity to levels sufficient to transport substantial increased production.

Mr. Ness said with regard to federal legislation and rules, oil and gas refining and marketing is under stress. He said refiners have invested billions of dollars to reach 1990 emission levels and federal legislation rules under consideration would require greatly increased expenditures. He said proposed legislation would impose substantial additional costs, which is essentially a tax on refiners. He said the net effect of the Waxman-Markey bill would be an estimated increase of 70 cents per gallon for retail gasoline sales in North Dakota.

Mr. Ness said EPA regulation of hydraulic fracturing in the Bakken Formation is a great concern to the industry. He said additional taxes in the President's budget and the repeal of federal expensing costs for wells and exploration are projected to reduce investment in development of the Bakken Formation resource by 30 percent to 40 percent. He said the result is fewer jobs, tax revenues, wealth, and energy production. He said another concern is reduced access to federal lands because of imposition of greenhouse gas restrictions on permits and other restrictions on leasing. He said another concern is increased concern for endangered species and whether the presence of species such as Sprague's Pipit will reduce access to attractive drilling areas.

Mr. Ness said the EPA end-run on climate regulation is a big concern to the oil and gas industry. He said the EPA is proliferating new regulatory proposals faster than the industry can keep up. He said the combination of federal proposals on legislation and regulation are very concerning to the oil and gas industry.

Mr. Ness said with regard to North Dakota infrastructure issues, there are several topics of concern. With regard to workforce, he said, there is a need for many more employees, and the need is growing. He said a new workforce survey is being conducted. He said housing in western North Dakota is extremely hard to find and expensive. For road transportation, he said, additional planning and improved safety is needed. He said access to an adequate water supply for drilling operations is a growing concern.

Mr. Ness said up to 1.5 million gallons of water is required for each fracturing operation for a Bakken oil well. He said for comparison, the approximate volume of water used to irrigate a quarter-section of land using a center pivot system is about 1.38 million gallons per day. He said typical daily water use for a 50,000-person midwestern city is about 10 million gallons. He said the industry hopes to be able to utilize the Lake Sakakawea water resource. He reviewed the water needs and plans for the segments of the oil development area. He said development projects are planned for a regional water supply from a Williston regional water plant to Watford City at a capacity of 4 million gallons per day, and a total project cost of $24 million. He said the project would serve long-term residential needs in McKenzie County and the current and future needs of the oil industry. He said it is anticipated the project would be completed in three phases. He said a system for the Alexander service area is anticipated to cost approximately $4.5 million, and a system to expand the existing rural water system to 100 additional rural users in the Watford City service area is projected to cost $2.45 million.

Mr. Ness said the North Dakota Petroleum Council is working to identify an oil tax structure that is competitive, fair, predictable, and easier to understand and administer. He said it will take time to arrive at a consensus recommendation among members, but it is hoped that a recommendation will be developed this year. He said the triggered horizontal well incentive enacted in 2009 was beneficial at a time of low oil prices and has paid huge dividends for North Dakota.

Senator Potter said oil produced in North Dakota is subject to a discount from the price of West Texas Crude. He asked whether the discount is attributable to transportation costs. Mr. Ness said the discount is primarily because of transportation costs, and the discount is substantially less than it has been in previous years. Senator Potter asked whether establishing a refinery in North Dakota could eliminate the transportation differential and generate substantial added revenue for investors and in tax collections. Mr. Ness said a new refinery would reduce transportation costs but someone would have to invest $2 billion to $4 billion to establish a new refinery, so it is not clear at this point whether prices for North Dakota crude would increase. He said a refinery study is being done to determine feasibility and identify markets for refined products.

MINING EMPLOYMENT

Chairman Cook called on Mr. Michael Ziesch, Job Service North Dakota, for presentation of information (Appendix E) requested by the committee relating to employment issues. Mr. Ziesch said mining employment data became important to tax allocations with the addition of provisions in 2009 to the oil and gas gross production tax formula which provide enhanced funding to cities with more than 7,500 population and with stages of more than 2 percent or 7 percent of private covered employment engaged in the mining industry. He said the table provided shows Williston and Dickinson to be the two cities that qualify under this requirement. He said Williston has 28.4 percent of private covered employment in the mining industry and Dickinson has 4.9 percent of private covered employment in the mining industry. He said the data is from 2008 but the next round of new data will not affect the stages of employment in the allocation formula for Williston, Dickinson, or Minot.

Mr. Ziesch said oil and gas employment in North Dakota rose sharply beginning in 2007 and it appears it peaked in November 2008. He said the decline in employment may have a lot to do with the harsh winter of 2008-09.

Mr. Ziesch said Slope County now ranks highest among counties in annual average wage. He said Slope County two or three years ago was ranked No. 47 among counties in average annual wage. He said this change shows the impact of oil industry employment in counties with smaller populations.

Mr. Ziesch said he was asked whether employment and wage increases in the oil industry have increased wages in affected communities for jobs outside the oil industry. He said it appears Dickinson employers have not had to raise wages, but in Williston employers have had to increase wages outside the oil industry.

In response to a question from Senator Cook, Mr. Ziesch said the lowest unemployment rates among counties are for oil counties. He said unemployment tax rates do not vary based on the county but on the employer's industry, history, and reserves.

Senator Nodland asked for current estimates of job openings in oil country. Mr. Ziesch said a recent check with western offices showed about 150 job openings in western North Dakota about one month ago. He said the number of job openings is affected by the season, and job openings are lower in winter months.

IMPACT FUNDING

Chairman Cook called on Mr. Jeff Engleson, Director, Energy Development Impact Office, for presentation of information (Appendix F) in response to committee questions regarding oil impact funding.

Mr. Engleson said for the 2007-09 biennium, $6 million was available for impact grants and the funding was increased to $8 million for the 2009-11 biennium. He said the impact grant program provides flexibility in administration to adapt the program to changing needs of political subdivisions.

Mr. Engleson said the amount of grant requests has increased substantially over the past 10 years. He said grants awarded to counties have decreased in the last 10 years while awards to townships have increased. He said this results from increased revenue allocations to counties and the fact that statutory allocations were not made to townships until enactment of 2009 legislation. He said grant awards have shifted among counties in the state depending on the location of development activity. He said 85 percent to 90 percent of grants have been awarded for transportation and fire and ambulance funding. He said the program recognizes that these government services are probably most directly impacted by oil development.

Mr. Engleson said 2009 legislation increased direct funding to counties, cities, and school districts by an estimated $28 million for the 2009-11 biennium. He said 2009 legislation directed a portion of revenue allocations to be placed in an infrastructure fund for counties to provide assistance to townships. He said the 2009 impact funding changes go into effect for the beginning of fiscal year 2010 and the Energy Development Impact Office is just getting started on the 2010 impact grant round. He said there are issues that need to be worked out. He said it appears from 2009 legislation that the Legislative Assembly intended to substantially increase tax allocations to counties and cities and hold school district allocations at approximately the previous levels. He said it appears the Legislative Assembly intends the impact program to fill in the gaps in funding for entities that receive either no funding or inadequate funding from the direct distribution formula.

Mr. Engleson said one thing that will be required by the 2009 changes is that the Energy Development Impact Office will need to work closer than ever with counties to coordinate efforts. Each oil producing county will have an infrastructure fund for grants to townships within the county and it will be important for the Energy Development Impact Office to coordinate grant funds with county funding.

Senator Potter asked if there is oil development impact to tribal government that we do not address in funding. Mr. Engleson said tribal government is not eligible for grant funding but cities on, and counties containing, reservation lands are eligible.

OIL TAX COMPARISONS AND STATISTICS

Chairman Cook called on Mr. Ryan Rauschenberger, Tax Department, for presentation of information (Appendices G, H, and I) requested by the committee relating to tax rate comparisons and statistics for oil taxes.

Mr. Rauschenberger said a comparison was made of the combined taxes for oil produced in Montana, Wyoming, and North Dakota. He said the information (Appendix G) is a simplistic summary for comparison purposes, and each state has provisions for reduced rates or exemptions for qualifying production. He said the combined oil tax rates are 10.23 percent for Montana, 12.70 percent for Wyoming, and 11.50 percent for North Dakota. He said information is attached providing a summary of reduced rates and exemptions available for oil production in the comparison states.

Senator Potter asked how many North Dakota wells currently classified as stripper wells are producing more than the daily production amount limit for stripper wells at the time of recertification. Mr. Rauschenberger said he has no information available, but the Tax Department can investigate and provide information on that question.

Senator Cook asked what is the average combined production and extraction tax for all wells in North Dakota, considering all exemptions or rate reductions currently in effect. Mr. Rauschenberger said the effective tax rate for all oil production is in the range of 9.8 percent to 10 percent.

Mr. Rauschenberger said information was requested to illustrate the effect of 2009 House Bill No. 1304 on oil and gas gross production tax allocations to political subdivisions. He said the comparison is made on Appendix H, which includes distributions for five months of revenue under the new distribution formula. He said the table was prepared to show actual distributions by county and to show the share within each county received by county government, cities, schools, and the new infrastructure fund. He said for this five-month period, the net change due to the 2009 legislation is an increase of allocations to counties exceeding $3 million, an increase for cities exceeding $2 million, and almost $1.9 million new revenue to county infrastructure funds. He said school districts have received the same level of funding they would have received under previous law. He said the net effect is an increase of over $7.2 million to political subdivisions, when compared with what they would have received under previous law.

Senator Nodland said a 2009 legislative change removed the cap that applied to county allocations and replaced it with an allocation amount at which the county would receive only 10 percent of production tax revenue produced within the county. He asked if any counties have reached the level at which they will receive only 10 percent of revenue collections. Mr. Rauschenberger said Mountrail County production has already reached that level.

Mr. Rauschenberger said information was requested on oil tax revenue collections and allocations from oil production within the Fort Berthold

Reservation. He said the information on Appendix I provides the statistics.

Representative Meyer said when the 2007 legislation authorizing an oil and gas tax production agreement between the Governor and the Three Affiliated Tribes was adopted, many legislators believed there was a "hold harmless" provision for counties to allow them to receive the same share of tax collections from reservation production as from production outside the reservation. She requested that the committee obtain information to estimate what amount would have been received by Mountrail County from production within the reservation if the "hold harmless" provision had been contained in the 2007 legislation, compared to what Mountrail County has actually received from that production.

WATER ISSUES

Chairman Cook called on Mr. Todd Sando, Assistant State Engineer, State Water Commission, with regard to questions of the committee to the State Water Commission. Mr. Sando said the committee requested information on water resource needs in the oil production area and funding sources and commitments of the State Water Commission. He said we are seven months into the biennium and the State Water Commission has been active in funding allocations and commitments for projects. He said members of the State Water Commission staff would provide detailed information. He said the State Water Commission is also aware that funding needs may develop in relation to potential spring flooding.

Mr. Bob Shaver, Water Appropriations Division, State Water Commission, provided a factsheet (Appendix J) on water needs in oil development. He said an estimated 1,400 new oil wells will be drilled in North Dakota in the next year. He said each new well will require about 3 million gallons of water for fracturing operations. He said the total water demand for estimated new wells is about 4.3 billion gallons of water per year, which is 13,258 acre-feet. He said this amount of water is roughly equivalent to the water needs for about 132 quarter-sections of agricultural center pivot irrigation.

Mr. Shaver said the only reliable water supply to meet oilfield demand for quantity and quality is the Missouri River and Lake Sakakawea. He said for visualization purposes, on average about 59,177 acre-feet of Missouri River water flows through Bismarck per day and the annual estimated oilfield demand would be about 22 percent of the average flow through Bismarck for one day. He said there are currently 370 acre-feet of water appropriations approved from Lake Sakakawea and 30,800 acre-feet for which applications have been made from Lake Sakakawea for water depots. He said two permits are needed, from the Corps of Engineers and State Water Commission, for water appropriations from Lake Sakakawea. He said approval of permits by the Corps of Engineers is a slow process.

Senator Cook asked what are the chances the oil industry will get all approvals needed for use of water from Lake Sakakawea. Mr. Shaver said he cannot speak for the Corps of Engineers, but the State Water Commission believes the water supply in Lake Sakakawea is plentiful for oil industry needs and industry use is a beneficial use.

Representative Meyer asked whether the permitting processes are coordinated to obtain water permits from the Corps of Engineers and the State Water Commission. Mr. Shaver said applicants need approval from both entities and the procedures are separate.

Representative Froseth said there is an excess of water in the Devils Lake Basin and asked whether that could provide a water source for oil development. Mr. Shaver said the cost of transportation for water from the Devils Lake Basin would be prohibitive, especially with the existence of a viable water supply in Lake Sakakawea.

Mr. Dave Laschkewitsch, Director, Administrative Services Division, State Water Commission, distributed copies of fiscal information (Appendices K and L) on the resources trust fund and the State Water Commission projects, grants, and contract fund for the 2009-11 biennium.

URANIUM TAXATION

Senator Cook called on committee counsel for presentation of a memorandum entitled *Uranium Severance Taxes in Other States*. Committee counsel reviewed the memorandum and said the states in the comparison impose property taxes on uranium. He said North Dakota does not impose property taxes on minerals in place in the ground. He said uranium prices are very volatile and have led to boom and bust production in other states.

Senator Cook said there is no uranium mining activity in North Dakota at this time and he is of the same opinion others have expressed, that it would be better to have tax policy in place before the industry makes investments in mining activity.

Representative Froseth said he agrees with Senator Cook, and it would be a good idea to explore tax policy to put in place before development begins. He suggested the committee consider a bill draft for a uranium severance tax. He suggested that for initial discussion purposes, the bill draft should provide a 3 percent severance tax rate with an exemption for $5 million of initial production by a producer. Committee counsel asked if the exemption amount would be an annual exemption or a one-time exemption. Representative Froseth said the bill draft should be prepared to provide a one-time exemption.

Chairman Cook requested committee counsel to prepare a uranium severance tax bill draft for committee consideration.

Representative Meyer said a member of the staff of the Council of State Governments has done a lot of study on uranium mining activity in the states. She said this individual would be a good resource person.

PROPERTY TAX RELIEF

Chairman Cook called on Mr. Joe Becker, Tax Department, for presentation of information (Appendix M) requested by the committee to summarize the total income tax credits under 2007 Senate Bill No. 2032 and 2009 House Bill No. 1448 and the fiscal impact of the Military Spouses Residency Relief Act.

Mr. Becker said the estimated fiscal effect of 2007 Senate Bill No. 2032 was approximately a $112 million revenue reduction to the state general fund from the income tax credits provided. He said the total income tax credits claimed for both years totaled approximately $83.4 million. He said $75.6 million of the credits went to owners of residential and agricultural property and approximately $7.8 million of credits went to owners of commercial property. He said individuals obtained credits of $82.8 million and approximately $600,000 in credits went to C corporations.

Mr. Becker said the 2007 legislation provided for issuance of property tax relief certificates for unused credits for residential and agricultural property. He said approximately 60,000 certificates were issued, with a total revenue effect of about $12 million.

Mr. Becker said 2009 House Bill No. 1448 was intended to provide retroactive property tax relief for the 2007 income tax credit to certain taxpayers that were ineligible for the property tax relief program under 2007 Senate Bill No. 2032. He said the fiscal impact cannot be determined yet because the returns are currently being filed for which taxpayers may claim the credit under the 2009 legislation. He said the unclaimed amount from the $112 million estimated for the impact of the 2007 legislation would cover the amount of retroactive credit claimed on the 2009 returns.

Mr. Becker said the Military Spouses Residency Relief Act provides an income tax exemption for nonmilitary earnings of the spouse of military personnel stationed in North Dakota. He said the estimated fiscal impact to North Dakota is approximately $118,000 per year.

SCHOOL DISTRICT LEVY REDUCTIONS

Chairman Cook called on Mr. Jerry Coleman, Department of Public Instruction, for presentation of information (Appendix N) on the effects of the 2009 property tax legislation on school district property tax levies.

Mr. Coleman said the first page of the information is a chart to illustrate how the school district maximum general fund levy is determined and what options are available to school districts.

Mr. Coleman said the information provided shows for each school district in the state the 2009 and 2010 taxable valuation, general fund levy in mills, high school tuition levy in mills, high school transportation levy in mills, and total combined education mill rate in mills. He said the total statewide data shows that in 2010 there is a 7 percent increase in statewide taxable valuation and a 37 percent decrease in school district general fund and combined education mill levies. He said the 2009 legislation was intended to compress mill rates of school districts into a lower range. He said it appears the intended effect has occurred and only 14 school districts are levying more than 110 mills for the 2009 fiscal year and 73 percent of school districts now levy in the range of 100 mills to 110 mills.

Representative Kasper asked whether Mr. Coleman can identify the valuation increase attributable to only new property in Fargo. Mr. Coleman said the Department of Public Instruction receives only total taxable valuation and it is not possible from that data to determine how much of the valuation increase is attributable to new property.

Representative Froseth asked whether it appears the total $295 million appropriation for property tax relief will be expended in this biennium. Mr. Coleman said it appears to be very close and it looks like there might be about $1 million left over at the end of the biennium.

WISCONSIN PROPERTY TAX RELIEF PROGRAMS

Chairman Cook called on committee counsel for presentation of a memorandum entitled *Wisconsin Property Tax Relief Programs*. Committee counsel said Wisconsin has several property tax relief programs aimed at reducing the burden of school property taxes. He said the programs are structured differently and some target relief to lower-income taxpayers. He said Wisconsin provides three property tax credits that allocate funds to school districts to reduce school property tax levies. He said the programs are the school levy credit, lottery and gaming credit, and first dollar credit. He said the Wisconsin homestead credit is a refundable income tax credit limited to renters and homeowners with income less than $24,500. He said renters and homeowners are entitled to an additional income tax credit for a portion of school property taxes paid. He said agricultural property owners are entitled to income tax credits under two alternative agricultural property tax relief credits.

PROPERTY TAX RELIEF BILL DRAFT

Chairman Cook said it would be appropriate for the committee to begin consideration of a bill draft based on the approach in 2009 Senate Bill No. 2199. He requested committee counsel to prepare a bill draft for committee consideration based on the 2009 bill, with updates appropriate for the 2011-13 biennium and to rectify any technical problems that have been identified.

Chairman Cook said one committee study directs investigation of providing a homestead credit for all North Dakota residential property owners and occupants and another directs consideration of reducing each taxpayer's property tax bill to not more than 1.5 percent of the true and full value of property. He said information should be gathered on how those objectives could be accomplished and what cost to the state would be involved.

Representative Pinkerton said Florida has a cap of 3 percent for increases in property valuation from the previous year. He said consideration could be given to the feasibility of such a limitation in North Dakota. He said another issue that should be examined is whether the state of North Dakota will pick up the difference when valuation increases occur, under the approach in the 2009 property tax relief legislation. Chairman Cook requested committee counsel to research the issues.

TAX INCREMENT FINANCING

Chairman Cook called on committee counsel for presentation of a memorandum entitled *Tax Increment Financing to Develop Property*. Committee counsel said tax increment financing is a development tool for urban renewal purposes. He said creation of a tax increment financing district freezes property tax valuations for any political subdivision except the city. He said taxes continue to be levied against the full value of the property, but the tax revenue from the incremental value of the property is segregated in a special fund and used only to repay the cost of bonds or other financing for the tax increment financing project. He said other taxing districts, such as a school district, continue to receive property tax revenue at the level they received before improvements and, if the improvements include residential property, a school district will have increased costs because of a greater number of students. He said one issue that has come up in North Dakota is whether a blighted area, for purposes of the tax increment financing laws, would include undeveloped agricultural property. He said that was part of the issue in development of property within the city of Fargo which is also in the West Fargo School District. He said the situation led to introduction of 2003 legislation, to exclude use of tax increment financing to develop unimproved agricultural land. He said the bill failed to pass.

Chairman Cook asked Ms. Connie Sprynczynatyk, Executive Director, North Dakota League of Cities, on the number of cities that have established tax increment financing districts. Ms. Sprynczynatyk said there are 27 districts. Chairman Cook asked whether a city may have more than one tax increment financing district. Ms. Sprynczynatyk said a city may have multiple districts. Chairman Cook asked Ms. Sprynczynatyk if the North Dakota League of Cities can provide information to the committee to identify each tax increment financing district, the city in which it is located, the year it was established, and where any unexpended funds will go when the improvements are completed. Ms. Sprynczynatyk distributed copies of a report (Appendix O) from the North Dakota League of Cities identifying the cities having a tax increment financing district.

Ms. Sprynczynatyk said the North Dakota League of Cities conducts an annual study on taxable valuation and tax levies in North Dakota cities. She said Mr. Jerry Hjelmstad prepared the current report (Appendix P) based on 2009 taxable valuation and tax levies.

BUILDING AUTHORITY FINANCING

Chairman Cook called on committee counsel for presentation of a memorandum entitled *Building Authority Financing of Public Buildings for Political Subdivision Use*.

Representative Kasper said use of building authorities has not been abused in all cases but he believes in some cities it has been a problem. He said many taxpayers believe building authority use is to avoid the requirement of voter approval of new buildings.

PROPERTY TAX STATISTICAL INFORMATION

Chairman Cook called on Ms. Marcy Dickerson, State Supervisor of Assessments, Tax Department, for presentation of information on levy limitations that apply to political subdivisions. Ms. Dickerson said the Tax Department prepares a schedule of levy limitations after each legislative session to update the limitations. She distributed copies of the July 2009 schedule of levy limitations (Appendix Q).

Ms. Dickerson said she was also requested to provide the committee information on 10 years' historical data for city and city park property taxes and special assessments. She distributed a report showing that information for each county for the years 1999 to 2008 (Appendix R).

BOARD OF EQUALIZATION ASSESSMENT APPROVAL

Chairman Cook called on committee counsel for presentation of a bill draft [10025.0100]. Committee counsel said at the previous meeting Ms. Dickerson voiced concern with the range for assessment approvals by the State Board of Equalization. He said 2009 legislation limited the State Board of Equalization approval so that assessments could not be approved for a taxing district in which true and full value for residential and commercial property exceeds 100 percent of the true and full value under the sales ratio study. He said Ms. Dickerson said the State Board of Equalization retained the previous 95 percent floor on valuation, which means only a 5 percent range exists for approval. He said Ms. Dickerson said she believes a 5 percent range is inadequate to allow flexibility and that a range of 90 percent to 100 percent would be more appropriate. He said the bill draft incorporates that range in statute.

Ms. Dickerson said the existing statutory provision has a 100 percent cap, but the 95 percent floor is policy determined by the State Board of Equalization. She said she would prefer to keep it that way and that the floor is not needed in the statutory provision because the board could establish a different floor by policy. She said she would recommend to the State Board of Equalization that the approval range should be 90 percent to 100 percent of valuation for approval.

In response to a question from Senator Nodland, Ms. Dickerson explained how the sales ratio study is completed for each county and the information is provided to each county prior to completion of assessments.

STRIPPER WELL PROPERTIES

Chairman Cook called on Mr. Rauschenberger, who distributed copies of information requested earlier in the meeting, provided in a stripper well analysis (Appendix S) prepared by the Tax Department. He said the analysis compares the number of stripper wells to the total number of producing wells and the number of stripper wells currently producing at a higher daily production rate than the statutory limit for stripper well classification.

NEXT GENERATION 911

Chairman Cook called on Mr. Terry Traynor, Assistant Director, North Dakota Association of Counties, for testimony (Appendix T) relating to the study of Next Generation 911.

Senator Cook said the study being conducted by the Emergency Services Communications Coordinating Committee will be a significant study. He said the objective of the Taxation Committee is to examine fees or funding for 911 services and the kinds of communication not currently subject to fees which should be subject to fees.

In response to a question from Senator Miller, Mr. Traynor said there are 380,000 landlines and 460,000 wireless telephones in North Dakota which are subject to 911 fees.

Committee counsel said federal law was enacted to prohibit states from taxing access to the Internet. He asked whether that law prohibits states from imposing 911 fees on Internet-based services. Mr. Traynor said the Federal Communications Commission has ruled that 911 fees can apply to Internet communications.

Chairman Cook called on Mr. Mike Lynk, Director, Division of State Radio, to provide information (Appendix U) relating to the 911 funding study.

Mr. Lynk said North Dakota currently has 22 public safety answering points and 6 of those serve multiple counties. He said 2009 legislation allowed political subdivisions with a multicounty public safety answering point to increase the 911 fee from $1 to $1.50. He said two counties served by State Radio have increased the fee to $1.50.

Mr. Lynk said the revenues, expenditures, and reserves chart attached to his testimony identifies fee revenues and local general fund dollars required to support 911 services.

In response to a question from Senator Cook, Mr. Lynk said prepaid calling cards are subject to sales taxes. Senator Cook asked where the sales tax on prepaid calling cards is sourced. Mr. Lynk said he will have to research the question to find the correct answer. Senator Cook asked where the 911 fees on wireless service are allocated and whether the sourcing is based on the point of purchase or where the user resides. Mr. Lynk said he will research that question. Mr. Traynor said he believes that where the telephone is activated should be where the fees go under the Mobile Communications Sourcing Act.

Chairman Cook said he would be willing to initiate committee consideration of a bill draft to eliminate 911 fees and replace the revenue from state sources. Representative Belter said he would agree with that approach if a way could also be found to reduce the number of public safety answering points. Representative Pinkerton said he agrees with Representative Belter that the state would have an interest in controlling the costs of the system if state funding sources are used.

Senator Miller said paying the cost of 911 services from state sources would relieve the problems in collecting fees and be more fair to users. Representative Weiler said he agrees with Senator Miller and that paying the cost of 911 services from the state general fund is a better approach than creating new taxes. He said he also agrees that reducing the number of public safety answering points would make the system more efficient. Senator Potter said he agrees that the state general fund would be a proper funding source for 911 services.

No further business appearing, Chairman Cook adjourned the meeting at 4:00 p.m.

John Walstad
Code Revisor

ATTACH:21