NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

# ELECTRIC INDUSTRY COMPETITION COMMITTEE

Tuesday, July 6, 2004
Roughrider Room, State Capitol
Bismarck, North Dakota

Representative Matthew M. Klein, Chairman, called the meeting to order at 9:00 a.m.

**Members present:** Representatives Matthew M. Klein, Arden C. Anderson, Wesley R. Belter, Jim Kasper, George Keiser, James Kerzman; Senators Duane Mutch, David P. O'Connell, Larry Robinson, Ben Tollefson, Thomas L. Trenbeath, Herb Urlacher

**Others present:** See Appendix A

**It was moved by Senator Robinson, seconded by Senator O'Connell, and carried on a voice vote that the minutes of the January 16, 2004, meeting be approved as distributed.**

## ELECTRIC INDUSTRY TAXATION

Chairman Klein called on Ms. Marcy D. Dickerson, State Supervisor of Assessments, Tax Commissioner's office, who presented an analysis of converting Verendrye Electric Cooperative to a centrally assessed property taxation system. A copy of her written presentation is attached as Appendix B.

In response to a question from Representative Kasper, Mr. Bruce R. Carlson, Manager, Verendrye Electric Cooperative, Velva, said the cooperative has approximately 10,200 meters and 8,100 members.

In response to a question from Representative Keiser, Ms. Ollie Glasoe, Office and Business Manager, Verendrye Electric Cooperative, Velva, said new construction costs are capitalized and maintenance expenses are not capitalized.

In response to a question from Senator Trenbeath, Mr. Carlson said Verendrye Electric Cooperative maintains approximately 4,300 miles of electricity lines.

Chairman Klein called on Mr. Harlan Fuglesten, Communications and Government Relations Director, North Dakota Association of Rural Electric Cooperatives, who discussed the analysis of converting Verendrye Electric Cooperative to a centrally assessed property taxation system, the amount of taxes paid by rural electric cooperatives and investor-owned utilities per consumer, and electric industry taxation. A copy of his written comments is attached as Appendix C. He said rural electric cooperatives do not support moving to a centrally assessed property taxation system because it would be subjective, unpredictable, and difficult to administer.

In response to a question from Representative Keiser, Mr. Fuglesten said it may be more advantageous for a certain political subdivision to be served by an investor-owned utility and it may be more advantageous for another political subdivision to be served by an electric cooperative. Overall, he said, electric cooperatives pay at least as much and perhaps more in property taxes as do investor-owned utilities. However, he said, depending on the amount of new construction, original investment, and the particular distribution formula involved, it may be more advantageous for a political subdivision to be served by one type of entity versus the other type of entity. That is why, he said, the rural electric cooperative's taxation proposal calls for two different methods of distributing property taxes back to political subdivisions. One method, he said, is based on line miles and the other is based on revenue. The reason for using the two methodologies, he said, is that the different methodologies have a disparate effect on political subdivisions. He said distributing revenue based on line miles benefits rural political subdivisions with low population densities while distributing revenue based on retail sales benefits urban political subdivisions with high population densities.

Chairman Klein called on Mr. Dennis Boyd, Senior Governmental Affairs Representative, Public Affairs Department, MDU Resources Group, Inc., who addressed the committee. Mr. Boyd discussed the amount of taxes paid by rural electric cooperatives and investor-owned utilities per consumer, converting rural electric cooperatives to a centrally assessed property taxation system, and cessation of efforts by Montana-Dakota Utilities Company and its partners to acquire NorthWestern Corporation. He then introduced Mr. Duane Steen who discussed the proposal by Montana-Dakota Utilities Company and Westmoreland Coal Company to construct a new lignite-fired electricity plant near Gascoyne. A copy of Mr. Boyd's written comments is attached as Appendix D and a copy of the slides used by Mr. Steen in his presentation is attached as Appendix E. Mr. Steen said Montana-Dakota Utilities Company and Westmoreland Coal Company have submitted a joint application for an air permit for the project. He said this is the first time a generator and mine operator have submitted a joint air quality permit to the State Health Department. He said construction is slated to begin in 2006 with the plant beginning commercial operations in May 2010. He said the plant and mine will employ approximately 100 full-time employees. He said the plant will consume 1.2 million tons of lignite per year or 3,500 tons per day. He said the plant will also consume 200 tons of limestone per day and use 130 gallons of water per minute.

In response to a question from Representative Klein, Mr. Steen said the water will come from dewatering the lignite mine.

In response to a question from Representative Keiser, Mr. Steen said at 175 megawatts, the plant will be network service or integrated into the current transmission system. However, he said, if a larger plant is constructed, new transmission assets will have to be developed.

In response to a question from Senator Urlacher, Mr. Steen said the limestone must be shipped from South Dakota or Montana because North Dakota does not produce commercial quantities of limestone.

Mr. Boyd said the tax burden per megawatt-hour of electric sales for property and income taxes only in North Dakota for the Montana-Dakota Utilities Company is $7.32.

In response to a question from Representative Kerzman, Mr. Boyd said Montana-Dakota Utilities Company did not include conversion taxes in its calculation because those taxes are paid by all generators at an equal rate. He said Montana-Dakota Utilities Company objects to the taxation proposal prepared by the Association of Rural Electric Cooperatives and presented at the January 16, 2004, meeting of the committee. He said property taxes should be taxes on the value of property, not an "in lieu of" system that is confusing and contains opportunity for mischief by shifting taxes from one property owner to another. He said the proposal violates the concept of simplicity and easy understandability and a tax on transmission lines, but not including substations, appears to be an effort to achieve a predetermined effect, i.e., a minimalization of tax increases for the large-voltage transmission lines. He said the proposal also would impose an administrative burden on investor-owned combination utility companies such as Montana-Dakota Utilities Company because it would subject their property to two different tax systems--one for electric operations and one for natural gas operations.

Mr. Boyd reviewed a bill draft [50064.0200] relating to elimination of gross receipts taxes for rural electric cooperatives and substitution of centrally assessed property taxes. He said the bill draft would eliminate the current gross receipts and per mile transmission line taxes paid by rural electric cooperatives and would subject their property to centrally assessed ad valorem property taxes. Thus, he said, the proposal would tax rural electric cooperative property in exactly the same manner in which investor-owned property is taxed. He said one of the vexing problems for the Legislative Assembly is education funding and while the Legislative Assembly has increased funding for education in each of the recent legislative sessions, a large portion of education funding still falls on local property tax owners. He said the proposal put forward by Montana-Dakota Utilities Company would broaden the state's tax base and reduce pressure on other property owners. He said the proposal advocated by the Association of Rural Electric Cooperatives would have the opposite effect by removing millions of dollars of tax valuations from the property tax rolls.

Mr. Boyd said the central assessment method is a well-developed system for determining value for investor-owned property and an appropriate methodology could be developed to extend this method to rural electric cooperative property, even if some of its original records are lost or unavailable. He said the committee should reject the proposal advanced by the Association of Rural Electric Cooperatives and take a hard look at the proposal submitted by Montana-Dakota Utilities Company.

In response to a question from Senator O'Connell, Representative Keiser said he had requested the Legislative Council staff to prepare the bill draft reviewed by Mr. Boyd.

Chairman Klein called on Mr. Steve Schultz, Otter Tail Power Company, Jamestown, who addressed the committee. A copy of his written comments is attached as Appendix F. Mr. Schultz said Otter Tail Power Company and its ratepayers pay property taxes in North Dakota, which are approximately equal to $1.47 per megawatt-hour. When state and federal income taxes paid by North Dakota customers of Otter Tail Power Company are included, he said, the total is $5.84 per megawatt-hour. He said these totals do not include coal severance or coal conversion taxes.

In response to a question from Senator Trenbeath, Mr. Schultz said Otter Tail Power Company does not anticipate the type of competition that was envisioned when the committee was formed. However, he said, to the extent that competition does develop, Otter Tail Power Company will be a vigorous participant in that competition.

In response to a question from Representative Keiser, Mr. Schultz said Otter Tail Power Company taxes would stay the same under the Montana-Dakota Utilities Company proposal but would be reduced by $148,000 per year under the Association of Rural Electric Cooperatives taxation proposal.

Chairman Klein called on Ms. Kathy Aas, Xcel Energy, Inc., Minot, who addressed the committee. She discussed taxes paid per customer and the two tax methods being considered by the committee. A copy of her written comments is attached as Appendix G. She said the total tax per megawatt-hour paid by Xcel Energy, Inc., including property and state and federal income taxes is $3.99.

In response to a question from Representative Kasper, Ms. Aas said adopting the proposal submitted by the Association of Rural Electric Cooperatives would not increase or decrease the amount of taxes paid by Xcel Energy, Inc.

Chairman Klein called on Mr. Bob Graveline, President, Utility Shareholders of North Dakota, who addressed the committee. A copy of Mr. Graveline's written comments is attached as Appendix H. He said the Utility Shareholders of North Dakota believes that a switch in policy that would tax electric cooperatives on an ad valorem basis, the same as shareholder-owned utility companies are taxed, would be a good move for all consumers, taxpayers, and competitors.

In response to a question from Senator Tollefson, Mr. Graveline said it should be possible to determine a base value for cooperative property based upon information filed by the cooperatives with the federal government.

In response to Mr. Boyd's comments concerning the line-mile tax, Mr. Fuglesten said the state's transmission lines are the method by which the state exports its electricity and increasing the tax too high too fast would have a detrimental effect on the export of electricity out of state and discourage the development of energy generation facilities in the state. Also, he said, taxing electricity lines on the basis of carrying capacity may not be the most appropriate method. He said if the committee is attempting to mirror a property tax, then it should be looking at the value of the property. Although a direct current line may carry more energy than an alternating current line, he said, it does not have more value because it has more limited uses than an alternating current line. He said the committee should base its taxation formula on the value and use of the line and other factors that relate to property taxation. He said increasing the highest category for the line-mile tax to $900 represents a 400 percent increase to Great River Energy. Finally, he said, the concept of revenue neutrality is measured by the total revenue raised by the different taxes on the electricity industry, not by whether each participant in the industry pays the same amount of taxes under a new system as it currently does.

Representative Klein presented Proposed Amendments to Bill Draft No. 30619.0100 proposed by the Association of Rural Electric Cooperatives. He said the amendments would do two things. First, he said, two new categories are added to the line-mile tax--a tax of $800 for transmission lines that operate at a nominal operating direct current voltage of less than 300 kilovolts and a tax of $1,200 for transmission lines that operate at a nominal operating direct current voltage of 300 kilovolts or more. Secondly, he said, the method of distribution of the line-mile tax is changed to provide that the revenue from the line-mile tax would be distributed to the political subdivisions where the energy is used as opposed to strictly where the lines are located as provided under current law.

## WIND ENERGY DEVELOPMENT STUDY

Chairman Klein called on Representative Jon O. Nelson, Wolford, who addressed the committee. Representative Nelson said he is a member of the Legislators Forum renewable energy working group. He said the Legislators Forum is composed of members from North Dakota, South Dakota, Minnesota, and Manitoba. Currently, he said, renewable energy efforts are focused on energy credit trading and tracking and development of hydrogen fuel cells as the nation's economy moves toward a hydrogen economy. He said the Legislators Forum is studying how North Dakota fits into these emerging renewable energy areas. He said states surrounding North Dakota have enacted renewable portfolio standards, which provide an opportunity for renewable energy development in North Dakota for export to these states as well as opportunities for North Dakota's institutions of higher education to develop renewable energy technologies.

Chairman Klein called on Mr. Brad Crabtree, Director, Powering the Plains Project, Ashley, and Mr. Bill Grant, Midwest Director, Izaak Walton League of America, St. Paul, Minnesota. Mr. Crabtree distributed a packet of material concerning renewable energy and the Upper Midwest hydrogen initiative, a copy of which is on file in the Legislative Council office, and the slides used by Mr. Crabtree and Mr. Grant in their PowerPoint presentation are attached as Appendix I.

Mr. Grant said the Northern Plains has a large economic potential in renewable and carbon-neutral energy production for a growing market. He said all states in the Northern Plains are in the top 10 for wind resource and Manitoba would be included in the top 10 as well. He said these states also have significant ag-based biomass and hydropower resources. Also, he said, North Dakota has cutting-edge experience with emerging climate-friendly coal technologies. However, he said, harnessing this potential requires regional collaboration. He said the Powering the Plains Project region includes North and South Dakota, Iowa, Manitoba, Minnesota, and Wisconsin, which was recently added. Participants in the Powering the Plains Project, he said, include elected and government officials, energy industry executives, farm organization and agricultural producer representatives, and environmental advocates. He said the Powering the Plains Project is funded by the Bush and Joyce Foundations; Basin Electric Power Cooperative, Great River Energy, Xcel Energy, Inc., and Manitoba Hydro; Iowa Farm Bureau and an individual producer in Iowa; Izaak Walton League and Minnesotans for an Energy Efficient Economy; and the United States Departments of Agriculture and Energy. At the Powering the Plains Project partnership with the 2003

Legislators Forum, he said, delegates passed two resolutions. He said one requested the Powering the Plains Project form a regional policy working group and the other endorsed the Upper Midwest hydrogen initiative, a Powering the Plains Project-launched regional public-private consortium. In the broader context, he said, the Powering the Plains Project seeks to challenge assumptions about what is possible on the Northern Plains; learn from leading country experiences with renewable energy development, climate change policy, and transition to hydrogen fuel; and apply these lessons to the Northern Plains region.

Mr. Grant said Powering the Plains Project representatives visited the Netherlands, Denmark, Germany, and Iceland to study what these countries have done with renewable energy initiatives. He said the group learned that large increases in renewable energy are achievable; encouraging renewable energy and reducing greenhouse gas emissions can drive innovation, job creation, and growth; ownership and scale of renewable energy projects is important; a 30- to 50-year vision, with bold and measurable targets and clear policy incentives, is critical; comprehensive strategies yield maximum results; and leadership and public support matter more than resources or population base.

Mr. Crabtree reviewed energy transition efforts in the Upper Great Plains region. He said the Northern Plains has advantages to transitioning to renewable energies because the area has world-class renewable resources, including wind, biomass, and hydropower. He said there is an opportunity for North American leadership in hydrogen production from renewable and carbon-neutral sources. Also, he said, significant ag-based carbon sequestration potential drawing on the region's vast soil and wetland resources exists in this area. Concerning the future, he said, zero to very low emission coal gasification potential utilizing the region's unique experience, coal reserves, and appropriate geologic reservoirs for carbon dioxide storage also exists. Finally, he said, the prospect of large-scale environmental credit marketing to other regions also exists.

Mr. Crabtree said the first proposed action step is that governments in the region become early adopters of hydrogen and fuel cell technologies. The second proposed action step, he said, is that governments support strategically important demonstration projects. The third proposed action step, he said, is that each state and province adopt specific and measurable goals to support the near- and long-term visions. The fourth proposed action step, he said, is that governments adopt financial incentives to support the region's energy vision and goals. The fifth proposed action step, he said, is that governments endorse and support public-private partnerships to advance the region's hydrogen goals and the sixth proposed action step is that an Upper Midwest hydrogen education and research consortium be established.

Mr. Grant said the third annual Legislators Forum developed recommendations for fostering renewable energy development in the region. He said the renewable energy recommendation was that the region pursue a regional renewable energy credit tracking system.

In response to a question from Representative Kerzman, Mr. Grant said wind energy with the federal production tax credit is more economically feasible than natural gas and, in some cases, new coal generation.

In response to a question from Representative Kasper, Mr. Grant said Congress is considering extending the federal production tax credit of 1.7 cents for wind energy for two to three years. He said wind energy may be the one renewable energy source that is ready to stand on its own. However, he said, that is not to say that without the federal production tax credit, many new projects may not be developed. He said many sources of energy were subsidized in their development stages in order to make them feasible.

In response to a question from Representative Klein, Mr. Grant said the Minnesota wind energy incentive is for wind energy projects of two megawatts or less. He said the demand has been so great that the available funds for small wind energy projects in Minnesota has been exhausted. He said Minnesota does not have a separate state incentive for projects larger than two megawatts.

In response to a question from Senator O'Connell, Mr. Boyd said MDU Resources Group, Inc., would provide information on the percentage of shareholders who pay income taxes in North Dakota.

No further business appearing, Chairman Klein adjourned the meeting at 2:00 p.m.

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Jeffrey N. Nelson
Committee Counsel

ATTACH:9