

Revenue Assistance to Local Governments in Oil Development Areas

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Development of petroleum resources in North Dakota is providing added revenue but also creating economic and social impacts on communities and local governments in the development areas. An important issue is how the state can best provide financial assistance to help alleviate the problems of oil development impact. The 1981 Legislature provided for additional revenue to impacted local governments by returning more of the oil and gas production tax to oil-producing counties and by appropriating for an oil impact fund. Financial aid to impacted local governments will again be an issue for the 1983 Legislature as local interests groups express need for more financial assistance.

OIL REVENUE

Oil taxes have become a major source of revenue in the state due to expanded oil production, escalating oil prices and the addition of the 6½ percent oil extraction tax in 1981 by initiated measure. A 5 percent oil and gas production tax has been in effect since the 1950's.

Oil production in the state increased from 20 million barrels in 1973 to near 25 million barrels in 1978 and to an estimated 45 million barrels in 1982. North Dakota ranks ninth among states in oil production. The average annual price in North Dakota increased from \$4 per barrel in 1973 before the OPEC embargo, to \$18 in 1979, to approximately \$35 in 1981, but the price had declined to about \$30 per barrel by August 1982.

By 1982, oil taxes, at about \$169 million, were the second largest source of tax revenue in the state. Property taxes, levied by local governments, were near \$200 million in 1981. In fiscal 1982, sales tax collections, including the motor vehicle excise tax, were \$145 million. Income tax collections were \$67 million in fiscal 1982. Oil and gas tax collections are shown in Table 1. As shown, projections are for about a 10 percent decline in total oil revenue in fiscal 1983. Oil revenue estimates are difficult because of the unpredictability of both oil production and oil price.

Table 1. Oil and Gas Production Tax Collections, North Dakota, 1974-1981, Projections for 1982 and 1983^{a/}

Fiscal Year	5 Percent Oil and Gas Production Tax	6½ Percent Oil Extraction Tax	Total
	million dollars		
1974	\$ 4.4	--	\$ 4.4
1978	10.7		10.7
1979	13.4		13.4
1980	29.2		29.2
1981	63.6	\$23.7 ^{b/}	87.3
1982	79.4 ^{c/}	89.5 ^{c/}	168.9 ^{c/}
1983	72.1 ^{c/}	80.0 ^{c/}	152.1 ^{c/}

^{a/}Source: State Tax Department

^{b/}For 6 months, January 1 to June 30.

^{c/}State Tax Department Projections, March, 1982.

STATE AND LOCAL GOVERNMENT RELATIONSHIP

State responsibility for assisting local governments and communities impacted by oil development can be based on the relationship between state and local governments.

Under our federal system of government, the U.S. Constitution divides governmental powers between the federal government and the states. It includes no reference to local governments. The state government has the responsibility for providing needed public services and collecting needed revenue. State governments have, through constitutional and statutory measures, created local governments and permitted them to assist with carrying out state responsibilities for local public services.

With this state-local relationship, the state has legal authority for development of natural resources such as oil and for collection of tax revenue from this development. The state is also responsible for providing financial assistance to local governments impacted by oil development. The policy question is: What is the best method for the state to provide financial aid to local governments affected by oil development?

AID TO LOCAL GOVERNMENTS

In the past, oil producing counties received a portion of the 5 percent oil and gas production tax as compensation for oil development impact. The revenue returned to counties was divided among the county, school districts and cities in the county. The 1981 Legislature adjusted the formula to allow more funds to be returned to counties but placed limits based on population. In addition the Legislature appropriated \$10 million for the 1981-83 biennium from the state general fund for an oil impact fund. These funds are to be distributed by the Energy Development Impact Office to impacted local governments based on priority needs.

Oil Tax Distribution: Under 1981 Legislation, the formula for distribution of the 5 percent oil and gas production tax provides that an amount equal to 1 percent of the gross value of oil and gas production will go the state treasurer. For the 1981-83 biennium, part of this 1 percent revenue will be used to assist with the \$8 million appropriated to townships for the biennium. An amount up to a maximum of \$32 million for the biennium, including the township allocation, will be distributed to the state highway tax fund. All of this 1 percent oil revenue collected after June 30, 1983, will go to the state general fund.

Revenue equal to the remaining 4 percent oil tax is to be distributed between the state and oil-producing counties as shown in table 2. Also shown in table 2 is the distribution of this revenue within a county to the county general fund, school districts and incorporated cities.

Table 2. Distribution of Oil Tax Equal to Four Percent on Oil and Gas Production in Each Oil Producing County.

Oil Tax Collected from Production in County	County Share	State Share
First million dollars	75%	25%
Second million dollars	50%	50%
Over \$2 million	25%	75%

Distribution to Local Governments Within County

- 45 percent to county general fund.
- 35 percent to schools in county — based on average daily attendance
 - Limits — 75 percent of county average per pupil cost.
 - 120 percent of county average per pupil cost in school districts with less than 400 pupils^{a/}
- 20 percent to incorporated cities based on census data population. Limited to \$500 per capita.^{a/}

^{a/}Excess funds due to limits are allocated to county general fund.

Under this distribution formula for the 5 percent oil and gas production tax, approximately one-fourth of total collections will go to oil-producing counties and three-fourths to the state in fiscal 1982. As the level of oil taxes collected from counties increases, the state's share increases.

Oil Impact vs. Oil Production : Oil development impact in a county is not directly related to level of oil production in the county. Oil exploration, including testing and drilling, may occur in counties that have

little or no oil production revenue to compensate for the high costs of maintaining secondary roads and providing other public services for the added population. Also, the population growth and need for public services may be in counties adjacent to the counties with oil production. The 1981 Legislature placed limits on the revenue distributed to counties based on population as shown in table 3. For fiscal 1982, this limit affected only one county. (See table 4).

Table 3. Limits on Oil Tax Distributed to Counties Based on Population of County.

County Population ^{a/}	Fiscal Year Limit	
	1981-82	1982-83
Under 3,000	\$3,200,000	\$3,800,000
3,000-6,000	3,500,000	4,000,000
Over 6,000	4,000,000	4,500,000

^{a/}Based on decennial federal census data.

Oil Impact Fund: This appropriation from the state general fund provided that \$10 million for the 1981-83 biennium be available for distribution to impacted local governments based on need. In particular, these funds are to assist local governments in counties that need to provide increased services for a growing population and added road maintenance but that are not receiving comparable oil revenue from oil production.

In the first round of grants for 1982, \$5.5 million were distributed. The amount per county ranged from \$25,000 to over \$2 million as shown in table 4. County governments received 29.4 percent of the total distributed, schools received 24.3 percent, cities received 38.8 percent, park districts received 3.8 percent, fire districts received 1.8 percent, and townships received 1.9 percent.

WHAT'S HAPPENING IN IMPACT COUNTIES?

Are the present provisions for state revenue assistance to oil development counties adequate to help meet the extra demands on local governments? Economic impact from oil development includes increased employment and spending for oil exploration, drilling and production, as well as effects on the business sector from increased spending and employment. More people means more public services required from schools, cities and counties. Oil exploration and production place a heavy demand on county and township roads and bridges.

Data in table 4 on population changes, property tax levies, distribution of oil revenue, and oil impact fund grants may give some indication as to adequacy of present financial assistance to counties impacted by oil development. However, these data may not be a good indicator of added revenue needed to maintain rural roads. For comparative purposes, data on five counties with larger cities not in the impact area are included in table 4.

Population Changes: As shown in table 4, only four of the oil-producing counties had an increase in population from 1970 to 1980. These four counties each had a trade center with a population of 2,000 or larger and had active oil exploration in the county or

in adjacent areas. Bowman County has both coal and oil development. Other counties may have had population growth with oil development impact in the late 1970's which is not indicated by the decennial census data.

More people means increased need for local public services, such as schools, roads and streets, law enforcement, water and sewer systems and various other local services. Local revenue needs expand much faster than the increase in the property tax base.

Oil exploration, drilling and production creates heavy use of rural roads, but this added economic activity may not be reflected in local population growth. The county or township faces additional road construction and maintenance costs without additional local taxpayers or tax revenue. If drilling firms need new temporary roads to reach their well sites, these firms finance their own roads.

Local Tax Effort: Increased local government costs in impacted counties are financed by increasing property taxes if additional oil revenue or state aid are not adequate. Table 4 includes data for each oil impact county on total property taxes levied by all local units of government in 1981 and on percent increase since 1976, a year which preceded the rapid increase in oil development.

Total property taxes would be expected to increase with a growing population and related public services, expanded costs for road maintenance, and inflation. If inflation as measured by the Consumer Price Index reflects rising costs of providing local government services, then local government expenditures would have increased by 50 percent since 1976 just to maintain the same level of services. However, as shown in column 4, table 4, property taxes in most counties and as a state average went up less than 50 percent, largely due to increased federal and state aid to local governments.

Table 4. Population and Percent Change, Property Taxes Levied and Percent Change, Oil and Gas Production Tax Distribution and Oil Impact Fund Grants for Oil Development Impact Counties and Other Selected Counties.

County	(1) Population 1980	(2) Population Change 1970-1980 (percent)	(3) Property ^{a/} Taxes Levied 1981	(4) Change in Property Taxes Levied 1976-1981 (percent)	(5) Property ^{b/} Tax Levies in Mills 1981 (mills)	(6) Oil and Gas ^{c/} Tax Revenue Fiscal 1982	(7) Oil ^{d/} Impact Fund Grants 1982
Oil Producing							
Billings	1,138	-5.0	\$ 268,540	-1.4	55.8	\$ 3,200,000 ^{e/}	\$ 25,000
Bottineau	9,239	-1.7	3,286,000	+ 24.1	199.2	1,607,869	110,000
Bowman	4,229	+ 8.4	1,104,278	+ 16.5	157.5	1,190,428	189,000
Burke	3,822	-19.4	1,148,910	+ 7.0	168.4	857,726	32,000
Divide	3,494	-23.4	1,562,731	+ 12.0	184.1	464,740	25,500
Dunn	4,627	-5.5	1,332,549	+ 32.0	167.1	1,831,934	708,000
Golden Valley	2,391	-8.4	817,917	+ 16.9	157.0	570,460	114,059
Hettinger	4,275	-15.8	1,445,950	+ 19.6	181.2	37,810	70,000
McHenry	7,858	-12.5	2,221,340	+ 22.5	172.5	14,523	--
McKenzie	7,132	+ 16.4	1,626,333	+ 21.7	137.8	3,872,904	631,000
Mountrail	7,679	-9.0	2,145,640	+ 30.0	190.7	403,076	226,000
Renville	3,608	-5.7	1,149,064	+ 11.5	174.5	1,200,027	110,000
Slope	1,157	-22.0	545,886	+ 12.7	128.8	39,246	35,000
Stark	23,697	+ 20.8	6,924,393	+ 92.8	241.0	1,084,256	2,019,560
Ward	58,392	-0.3	13,448,105	+ 34.2	243.2	105,281	17,396
Williams	22,237	+ 15.2	7,125,949	+ 67.9	234.1	2,347,414	1,119,900
Total Oil Counties	164,975	+ 1.4	\$46,153,675	+ 38.1	204.5	\$18,827,694	\$5,432,415 ^{f/}
Others With Impact Funds ^{g/}							
Adams	3,584	-6.5	1,463,596	+ 38.4	214.4	--	90,000
Morton	25,177	+ 24.0	7,464,192	+ 79.0	240.3	--	33,500
Other Selected ^{h/}							
Burleigh	54,811	+ 34.6	17,706,479	+ 63.4	271.4	--	--
Cass	88,247	+ 19.8	28,152,870	+ 36.9	252.8	--	--
Grand Forks	66,100	+ 8.2	16,326,199	+ 30.3	252.5	--	--
Ramsey	13,048	+ 1.0	4,418,596	+ 30.1	241.8	--	--
Stutsman	24,154	+ 2.6	7,118,518	+ 34.2	182.4	--	--
State	652,717	+ 5.6	195,354,111	+ 37.5	212.5	--	\$5,555,915

^{a/}Includes all property tax levies for county, school districts, townships, cities and special districts, but does not include special taxes and special assessments.

^{b/}Average mill levy in county — total property taxes levied divided by total property taxable value in county in 1981.

^{c/}Includes actual distribution for first three quarters of fiscal 1982 plus State Tax Department projections made in April, 1982, for the fourth quarter.

^{d/}These are grants from the Energy development Impact Offices as of January, 1982, for the first year of the biennium to all political subdivisions in each county. Includes some forward commitments for 1983.

^{e/}\$3,200,000 was the statutory limit for 1982 based on population (see table 3).

^{f/}Adams and Morton Counties have been impacted by both coal and oil development, have little or no coal or oil production, but have received coal and oil impact funds.

^{g/}These counties were selected for comparative purposes because they have larger cities: Burleigh, Bismarck; Cass, Fargo; Grand Forks, Grand Forks; Ramsey, Devils Lake; Stutsman, Jamestown.

The average consolidated property tax levies in mills are shown in column 5, table 4. These were calculated by dividing total property taxes levied in the county in 1981 by total property taxable value in the county in 1981. Rural counties cannot be compared directly with counties with larger cities because cities provide additional services not available in rural areas. If assessed values were adjusted according to guidelines based on 1981 legislation, the mills levied should provide a comparative measure of local tax effort.

As shown, there is a difference among counties. For example, Stark County has the highest mill levy among counties in the primary impact area, the greatest increase in population and the most increase in property taxes. Although Stark County appears to have experienced the greatest impact, the oil revenue was relatively low. To compensate for the impact, Stark County received more grant funds from the Oil Impact Fund than any other county.

The data seem to indicate that the oil-impacted counties with larger cities, namely Stark, Williams and Morton, have experienced relatively more increase in property taxes than the five counties listed as not in the oil impact area. Burleigh and Morton counties have been affected by coal development in nearby counties.

Oil Tax Revenue and Oil Impact Grants: Local governments in oil impact counties receive revenue from the oil and gas production tax and from Oil Impact Fund grants as shown in columns 6 and 7 in table 4. In several counties, these revenues are greater than total property taxes levied by all local government units.

The oil and gas revenue distributed to counties may or may not coincide with the level of oil development impact. Current impact may be more related to oil exploration than to oil production.

Grants from the Oil Impact Fund provided financial assistance to counties in which rising local government costs due to oil development would have caused an undue burden on local property taxpayers. As shown in column 7, table 4, these grants were concentrated in four counties in the major impact areas. County governments, cities and school districts with less impact or those receiving adequate oil revenue to cover impact costs received smaller grants or did not qualify for grants.

Data in table 4 provide some indication of oil impact and sources of funds used to finance increases in local government services. The measures are imprecise but afford opportunity to make some judgment as to adequacy of present methods of distributing oil revenue and state funds to assist local governments in oil impact areas.

LOCAL GROUPS SUGGEST CHANGES

Local interest groups in oil impact counties are concerned that present legislation may not be pro-

viding equitable financial assistance to oil development impact areas. Some of their recommendations for changes in legislation include:

- An increase in the limits on the amount of oil revenue that can be distributed to oil producing counties.
- Doubling of the oil impact fund appropriation from \$10 million to \$20 million for the biennium.
- Creating a separate grant fund from the state's share of oil revenue to be used for assisting with roads and bridges in oil producing counties.
- Creating an impact loan fund available to local government units.

IMPLICATIONS

The state government has responsibility to provide financial assistance to local governments impacted by oil development. Currently, the state provides assistance through formula sharing of oil tax revenue with oil-producing counties and through grants from the Oil Impact Fund. Economic and political considerations will influence possible legislative changes.

Policy questions include:

- Is the present level of financial assistance to local governments adequate?
- Is the assistance going to local governments when and where most needed?
- If adjustments are made, should more revenue assistance be provided by the formula method or by grant funds?
- Are there alternative mechanisms for better assisting local governments with impacts?
- Should the private firms in oil development provide "front-end" financial assistance to impacted counties?

Each of the present assistance methods, formula funding and grant funding, has its advantages and disadvantages. Formula sharing of oil revenue to oil-producing counties provides annual revenue, but the amount may be unpredictable. Local officials have freedom in deciding how to use funds. However, the formula approach may not allocate funds when and where most needed.

The grant fund approach permits allocation of funds based on priority needs. It can provide assistance to impacted areas which may be receiving little, if any, oil revenue from the formula method. Grant funding is dependent on local government officials projecting needs and making application to the Energy Impact Office. This approach is dependent on administrative decisions and thus more subject to political pressures.

The present methods or possible new approaches to providing financial assistance to local governments impacted by oil development can be adjusted to changing conditions and based on experience. Legislative changes can be made with the support of an informed public.