

NORTH DAKOTA LEGISLATIVE MANAGEMENT

Minutes of the

LEGISLATIVE REVENUE ADVISORY COMMITTEE

Thursday, September 13, 2018
Roughrider Room, State Capitol
Bismarck, North Dakota

Senator Ray Holmberg, Chairman, called the meeting to order at 8:30 a.m.

Members present: Senators Ray Holmberg, Dwight Cook, Joan Heckaman, Rich Wardner; Representatives Larry Bellew, Al Carlson, Jeff Delzer, Corey Mock

Others present: Senator Jerry Klein, Fessenden, and Senator Donald Schaible, Mott, members of the Legislative Management

Senator Gary A. Lee, Casselton

Senator Ronald Sorvaag, Fargo

Representative Mark Sanford, Grand Forks

See [Appendix A](#) for additional persons present.

It was moved by Representative Mock, seconded by Senator Wardner, and carried on voice vote that the minutes of the August 15, 2018, meeting be approved as distributed.

Chairman Holmberg called on the Legislative Budget Analyst and Auditor to provide comments regarding the state revenue forecasting process. The Legislative Budget Analyst and Auditor said the committee entered a contract with IHS Markit to provide economic forecasting data. He said the Legislative Council staff provided information to IHS Markit regarding historical tax collections and tax policies. He said representatives from IHS Markit developed forecasting models based on the information provided by the Legislative Council staff to provide an independent projection of North Dakota state tax revenues. He said the economic forecasting data from IHS Markit will provide additional information, along with the executive branch revenue forecasts, for the Legislative Assembly to consider as it develops the state budget.

STATE REVENUE FORECASTING INFORMATION

Mr. James Diffley, Executive Director, Industry Services Consulting Group, Economics and Country Risk, IHS Markit, presented information ([Appendix B](#)) regarding forecasting results for general fund revenues. He said revenue forecasting is a challenging process, particularly for a commodity-based state like North Dakota. He said the volatility of global markets influences commodity prices, which can significantly impact North Dakota's tax revenue collections. He said the preliminary forecast for general fund sales and use tax collections totals \$1,805 million for the 2019-21 biennium compared to a revised forecast of \$1,704 million for the 2017-19 biennium and the original forecast of \$1,702 million for the 2017-19 biennium. He said individual income tax collections in fiscal year 2018 totaled \$364 million, or 16.5 percent more than the collections in fiscal year 2017, primarily because of strong capital gains. He said sales and use tax collections and individual income tax collections are anticipated to increase at 2 to 3 percent per fiscal year in the 2019-21 biennium, which reflects the historical rate of growth.

Mr. Diffley said the IHS Markit forecasting models produce quarterly estimates for the state revenue forecasts, which are aggregated into fiscal year and biennial totals. He said forecasting models use data from a variety of economic sectors, but the results from the models are primarily based on two economic drivers for each tax type. He said the economic drivers have the strongest correlation between the economic activity and the tax collections. He said the primary economic drivers to forecast the sales and use tax collections are oil well completions and personal consumption expenditures. He said the personal consumption expenditures reflect overall consumer spending on goods and services in the North Dakota economy and are estimated to grow at a modest rate. He said IHS considered the potential effect of collections from online sales in the development of the forecast for sales and use tax collections. He said other states have been estimating an increase of 2 percent in sales tax collections from online sales.

In response to a question from Representative Delzer, Mr. Diffley said the component of the forecast for sales and use tax collections based on oil well completions reflects 80 oil well completions per month for the remainder of the 2017-19 biennium and the entire 2019-21 biennium.

Senator Wardner said capacity constraints in the natural gas pipelines and regulations by the Department of Mineral Resources may limit the growth of oil well completions for the next few years as the oil and gas industry works to develop more infrastructure.

Mr. Diffley said motor vehicle excise tax collections are driven primarily by new car registrations and employment in the oil and gas industry. He said new car registrations in North Dakota are anticipated to decrease similar to national trends. He said car prices are increasing, which results in an increase in motor vehicle excise tax collections in the forecast.

Mr. Diffley said the primary economic drivers to forecast individual income tax collections are wage withholdings and property income. He said individual income tax collections related to wages increase by 1.1 percent for each 1 percent increase in wages due to the progressive structure of the income tax. He said property income contributes to estimated payments for individual income tax collections and consists of dividend and interest income as well as royalties.

Mr. Diffley said the primary economic drivers to forecast the corporate income tax collections are national corporate profits and oil prices. He said national corporate profits have increased significantly in the past year due to a strong national economy and the federal income tax reforms. He said oil prices were identified as a primary economic driver because higher oil prices lead to an increase in oil development activity and higher corporate profits. He said the single sales factor apportionment method is being phased in, and a portion of the estimated effect has been included in the forecast. He said IHS will continue to monitor the effect of the single sales factor apportionment method, and can adjust the forecasts as needed.

Mr. Diffley said IHS Markit's forecast for West Texas Intermediate (WTI) oil prices estimates the prices will remain at about \$70 per barrel through the 2019-21 biennium. He said oil production in the Bakken is estimated to increase and then stabilize at approximately 1.35 million barrels per day by 2021. He said the oil production forecast is based on estimates developed by oil industry specialists at IHS Markit, which reflect corporate leaders' expectations. He said constraints in the Bakken may limit oil development creating a discrepancy between corporate leaders' expectations and feedback from local industry representatives.

Mr. Diffley said the forecasts also include optimistic and pessimistic scenarios for each of the four primary general fund revenue tax types. He said the optimistic scenario reflects WTI prices \$10 more than the baseline forecast of about \$70 per barrel. He said the pessimistic scenario reflects WTI prices \$10 less than the baseline forecast. He said IHS Markit could provide additional optimistic and pessimistic scenarios for consideration by the Legislative Assembly based on higher or lower oil prices.

In response to a question from Representative Cook, Mr. Diffley said the oil price changes for the optimistic and pessimistic scenarios do not include any changes to the number of oil well completions. He said the optimistic and pessimistic scenarios were intended to show the effect of changing only the oil price without considering the impact from changing other variables such as oil well completions.

Mr. Diffley said IHS Markit will provide a comprehensive report detailing the economic outlook and forecasting data by September 30 pursuant to the contract. Subsequent to the meeting, the report ([Appendix C](#)) was submitted to the Legislative Council office.

BUDGET UPDATE

The Legislative Council staff distributed a memorandum entitled [General Fund Revenues Monthly Update](#), which provides information on actual general fund revenue collections for July 2018 and for the biennium to date.

The Legislative Council staff presented a memorandum entitled [Oil and Gas Tax Revenues Monthly Update](#), which provides information on oil and gas tax revenue allocations for August 2018 and for the biennium to date.

The Legislative Budget Analyst and Auditor presented a memorandum entitled [Budget Outlook - 2017-19 and 2019-21 Bienniums](#). He said the memorandum was revised after the committee's last meeting to reflect updates based on the September 2018 executive branch revenue forecast, higher education formula cost increases, estimated health insurance costs, and estimated unspent appropriation authority.

In response to a question from Representative Carlson, the Legislative Budget Analyst and Auditor said the budget outlook does not reflect any agency budget reductions, resulting from the Governor's budget guidelines in which agencies must reduce their 2019-21 budget requests by 5 percent or 10 percent.

The Legislative Council staff distributed a memorandum entitled [General Fund Revenue Forecast Comparison](#), which compares general fund revenue forecast estimates prepared by the Office of Management and Budget and by IHS Markit.

It was moved by Representative Carlson, seconded by Representative Mock, and carried on a voice vote that the Chairman and the Legislative Council staff be requested to prepare a report and to present the report to the Legislative Management.

It was moved by Representative Mock, seconded by Representative Carlson, and carried on a voice vote that the committee be adjourned sine die.

No further business appearing, Chairman Holmberg adjourned the committee sine die at 9:40 a.m.

Adam Mathiak
Senior Fiscal Analyst

Allen H. Knudson
Legislative Budget Analyst and Auditor

ATTACH:3