

**2015 HOUSE APPROPRIATIONS**

**HB 1033**

# 2015 HOUSE STANDING COMMITTEE MINUTES

## Appropriations Committee Roughrider Room, State Capitol

HB 1033  
1/20/2015  
22474

☐ Subcommittee  
☐ Conference Committee



### Explanation or reason for introduction of bill/resolution:

Relating to definitions for the legacy fund, principal balance and transfer of legacy fund earnings

### Minutes:

Attachments: **2**

### Chairman Jeff Delzer

Opened the hearing on HB 1033 and mentioned that he may have some comments about the bill, but would have Legislative Council explain the bill first and then the committee could talk about whether we need to have some changes made to it.

**Allen Knudson Legislative Council** staff made a presentation to offer information about the bill, neither for nor against it.

### Representative Bellew

Has earnings been defined?

**Knudson:** The next definition. The second one does define earnings. That was approved in 2013; HB1167 actually did define "earnings". Only realized gains and losses are recognized as earnings for the purpose of making the transfer and for purposes of the amount of money that can be spent out of the Legacy Fund from the earnings.

### Chairman Jeff Delzer

The way its set up in the Constitution, there would not be a transfer to the general fund until the end of the 2017-2-19 biennium, is that right?

**Knudson:** that is correct

### Representative Glassheim

Earnings mean any appreciated value of investments. And you can't sell them because it's principle, so you can tie up stuff for a long...Am I correct now, it doesn't include appreciated value of your investment and most things will be invested, there would be some dividend money, but most of it would be tied up?

**Knudson:** Until those are actually sold or traded it would be, but the State Investment Board would better be able to answer that than I am.

**Vice Chairman Keith Kempenich**

We allocated the funds to certain investments. They are moving in and out between these investment managers, there is income generated, but for most intents and purposes, you're right. If asset values go up, they would have to be sold to have some type of earnings on them.

**Chairman Jeff Delzer**

But if they sell and switch, to another, then there should be a realized earning for that portion, but if they hadn't sold it yet, they couldn't take it as part of the earnings.

**Knudson:** presentation continued

**Chairman Jeff Delzer**

As far as government finance, this discussion was had when things were going really well in oil industry, it would have been equal to having \$40B in the fund. The 25% would be if something happened, like we're going through, that you may want to have the earnings available for the next biennium and when we get done with all the testimony, I do have some amendments to change that from intent language to actual language. One of the issues we have is whether or not we would the earnings for the next biennium to be available and if we did, then we have to change the date on number 1 as well.

**Knudson:** presentation continued

**Chairman Jeff Delzer**

Questions on the bill as it stand before us?

**Representative Glassheim**

Why do you transfer to the general fund and immediately transfer back to the legacy fund? What does the Constitution say is supposed to happen with the money?

**Knudson:** at the end of the biennium, the State Treasurer transfers the earnings to the General Fund

**Chairman Jeff Delzer**

But the constitution also says the Legislative Assembly can do what they want with those earnings and if they desire to put them back into the Fund, they can become part of the principle.

Instead of just spending, we would want to save it if we could. Oil is finite, it's a question on how long that takes, but that is what the discussion was in the committee.

**Representative Glassheim**

We can transfer it back, but the intention of the constitutional measure was that we spend some of the earnings.

**Chairman Jeff Delzer**

Allen do you have the actual language?

**15:47**

**Knudson:** it's in a couple different spots, and then in subsection 1, it says "the State Treasurer shall transfer earnings of the North Dakota Legacy Fund to the state general fund at the end of the biennium and beyond..." In subsection one, "the Legislative Assembly may transfer funds from any source into the Legacy Fund and such transfers become part of the principle of the fund".

**Chairman Jeff Delzer**

It's kind of a case they are conflicting whatever...both sides can make the argument. And it's in the constitution.

**Vice Chairman Keith Kempenich**

It becomes a question of the Legacy Fund; truthfully it's not a very big fund, when you start looking at sovereign wealth funds. When you're dealing with a natural resource; there's got to be some definitions. We had a hard time on the advisory board because the investment folks that came in always wanted to know what your goal is. There's lots of problem with sovereign wealth funds. In Norway which has about \$1 trillion, they got things they're doing with it, but they really don't have any, they're just collecting. Granted Alaska did some stuff, they've got money and they're going to run into trouble this year. They've got \$52+ billion in their permanent trust fund its going back out to the people, but they can't build a road with it. Most states that have mineral resources have sovereign wealth funds and they are all over the board of what they do with them.

**Chairman Jeff Delzer**

Any further questions for Allen?

I won't get up to testify, but will say I do support the bill. I do have some amendments that I'll offer after a while.

Is there further testimony, opposition or neutral to HB 1033?

**Chairman Jeff Delzer**

Closed the open hearing on HB1033 and began the discussion on HB 1033.

**Chairman Jeff Delzer**

I have two different sets of amendments that change the intent language to actual language. I thought there might be a situation where we would like to have, if its 25% less next time, it would be kind of nice to have the interest. Then the year after, if it wasn't 25% it would roll over back into the General Fund. And one thing about this it's all statutory; any legislature can always change it at a 50% vote.

And what it does is it takes the intent language out and crosses out the intent language on 14, 15 and 16; and just inserts the word "unless". In other words, I would make it that its actually part of the bill. I was thinking it would make the interest available for the next biennium.

And the second amendment that is here, on page one of the bill would change the July 1 on line 16 to July 1 of 2015. What it would mean is that all earnings up to 2015 would be

transferred back into the fund and become part of principle but the interest line from 2015-2017 during this biennium would if it fell under this 25% less ...money, be in the fund where the legislature could go in and appropriate it. Brady, is that correct?

**Brady Larson, Legislative Council:** There is not supposed to be an interest transferred until 2017.

**Vice Chairman Keith Kempenich**

The measure could have been written better. You could appropriate it, but not access it.

**Chairman Jeff Delzer**

Brady, you want to try and answer that, because I think the 2017 session could appropriate out of that fund, could it not?

**Larson:** yes, there's a difference between appropriating and expending; so you can appropriate prior to July 1 of 2017 but you actually can't expend until after that date.

**Chairman Jeff Delzer**

Until that biennium actually starts. And if I understood Allen to be right, the earnings portion would be a majority vote.

**Larson:** Yes, it would be a simple majority for the earnings

**Chairman Jeff Delzer**

But the principle part would be 2/3 of each House. This puts in place how this current Legislature feels about what we should do about these things. And these would be the two items that would trigger it one way or the other. The first section of amendments we certainly need to do. Section 2 we need to do too, then it comes down to whether or not we want to do Section 3. If we don't do anything with it, at the end of 2017, the next Legislative session would have to decide what it's going to do because that money would roll out at the end of the 2017-2019 biennium. The committee worked hard, granted it was a while back and things are different now, but that's why I offered the amendments.

**Representative Glassheim**

My preference would be to not have Section 3 in there. When you don't have money, why would you bind yourself to say we must put it immediately back into savings? That becomes part of the principle that you can't touch. For the next two years, why would we put in law to transfer?

**Chairman Jeff Delzer**

That's part of the amendment; so that if it was actually 25% less of oil money, compared to the current biennium, it would not do that. That's part of the intent of the amendments. The other thing to remember is that this would simply put a statute out there that could be changed at every legislative session. Every legislature can change it vs. fighting that battle and either let it go or decide they want to put it back or whatever.

**Representative Glassheim**

What are the dollar amounts of the 25%?



**Chairman Jeff Delzer**

I believe the 25% for the next biennium off of the Governor's proposal would be \$134M, if that Governor's proposal is considerably less. It's probably not going to be a whole lot less. Brady isn't that the numbers you've given us; \$134M?

**Larson:** Yes, that is the estimated investment income for 2015-2017 biennium.

**Chairman Jeff Delzer**

That would allow if there was 25% less than the previous biennium.

**Representative Glassheim**

And that would be 100 and some million less?

**Chairman Jeff Delzer**

No it would be about \$1 ½ billion.

**Larson:** Yes, it would be about \$6 billion

**Chairman Jeff Delzer**

About \$1billion and one half less of expected income and if we stay \$40 per barrel oil, that will happen

**Representative Glassheim**

Nothing would happen

**Chairman Jeff Delzer**

If we adopt the amendments that it would mean that the \$134 million would be sitting there so the Legislature could decide if they wanted to. It would be transferred to the General Fund unless the next Legislature said not to transfer it; if we adopt both sets of amendments. Brady is that correct?

**Larson:** there will not be a transfer made at the end of the 15 -17 bienniums, so if both were adopted.

**Chairman Jeff Delzer**

But the legislature in 17 could appropriate that money.

**Larson:** yes it could be appropriated

**Representative Dosch**

Personally, I couldn't support the amendments, we are coming up to our first bump in the road and it seems to me we start clamoring to spend the legacy money. We have time to adjust the budgets now. I think it's giving out the whole wrong message out there. This Legacy Fund was for the future and if we can't get through one budget cycle without right away running to the fund, I think it sends the wrong message.

**Chairman Jeff Delzer**

What about the bill, if it's not amended?

**Representative Dosch**

I could support that.

**Representative Bellew**

Even if the amendments passed,...(unintelligible).....until the 2017 biennium, right?

**Chairman Jeff Delzer**

That's correct; the 2017 legislature will have the opportunity to appropriate the earnings out of it. And the 17 Legislature will have the opportunity to do the 15% on the principle. But they can't expend it till end of the next biennium.

**Vice Chairman Keith Kempenich**

Three options; Do nothing; which will be a transfer in June of 2019, or do this way, this amendment it would be available for 2017-2019 and have to wait till after June 30<sup>th</sup> to spend it .....

**Chairman Jeff Delzer**

The way the bills before us would move it all back in unless the next Legislature changed it. Committee members, I think we'll hold this until Tuesday morning, and give people time to think about it, whatever we want to do, but next time we meet in full committee, we'll try to kick 1094 and this bill out; also 1067.

**Chairman Jeff Delzer**

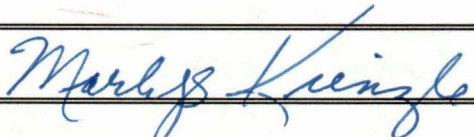
Adjourned the bill hearing.

# 2015 HOUSE STANDING COMMITTEE MINUTES

## Appropriations Committee Roughrider Room, State Capitol

HB 1033  
1/29/2015  
22832

- ☐ Subcommittee  
☐ Conference Committee



### Explanation or reason for introduction of bill/resolution:

Relating to definitions for the legacy fund, the legacy fund principal balance, and a transfer of legacy fund earnings

### Minutes:

**Chairman Jeff Delzer** opened the hearing on HB 1033 and summarized the bill. Referred to a possible amendment to the bill (.03002) that was handed out from bill hearing on 01/20/15.

### Representative Dosch

Resist any change of the date on amendment .03002.

### Chairman Jeff Delzer

It's not part of the one just handed out.

### Chairman Jeff Delzer

This would change it from intent to being part of the language. The interest would be set to go into the general fund right after the end of the 17...Brady is it 17-19?

### Brady Larson, Legislative Council Staff:

The first transfer would occur at end of 17-19 biennium.

### Chairman Jeff Delzer

So this would not affect that anyway, and then would it?

**Larson:** No, it would not.

### Chairman Jeff Delzer

Then there's probably no reason to amend it.

What about the bill itself, what are your wishes? Its good language; intent language.

**Representative Hogan** motioned for a Do Pass on HB 1033 as originally introduced .03000.



**Representative Boehning**

Motion seconded

**Representative Kreidt**

If we had significant earnings; would we have to sell part of the stocks?

**Chairman Jeff Delzer**

Bill itself; it will have to be dealt with, but if future legislators decide they want it to go back to the fund and stay there, then that has to be available as cash to go to the general fund; they'd have to have that much cash.

**Representative Kreidt**

How much cash would be earning interest?

**Chairman Jeff Delzer**

Before the prices went down, there was quite a bit of cash coming in every month

**Representative Kreidt**

Divided into percent's; stock; real estate, different entities.

**Chairman Jeff Delzer**

Maybe the investment committee needs to look at; at the end of the 17-19 biennium, it will have to be transferred, because that's what the constitution says.

**Vice Chairman Keith Kempenich**

They are tracking what the valuations are going up on it. You didn't want to use unrealized earnings. You might have to go into some of the shares. Not the corpus of the funds.

13:03

**Representative Kreidt**

We would have to liquidate some of the assets in order to cover?

**Chairman Jeff Delzer**

The Invest Committee might need to look at that during the interim.

**Representative Monson**

Are these earnings always earnings, are they now part of the corpus, or are they earnings forever?

**Chairman Jeff Delzer**

Anything the legislature puts in over and above becomes part of the principle

**Vice Chairman Keith Kempenich**

Anything they put in, even though it's statutory becomes part of the corpus of the investment.

House Appropriations Committee

HB 1033

01/29/15

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**Chairman Jeff Delzer**

Called for a vote

Motion carries 21 Yes; 0 No; 2 Absent

**Representative Vigesaa** will carry the bill.

Date: 1/29/15  
Roll Call Vote #: 1

2015 HOUSE STANDING COMMITTEE  
ROLL CALL VOTES  
BILL/RESOLUTION NO. 1033

House Appropriations Committee

☐ Subcommittee

Amendment LC# or Description: \_\_\_\_\_

Recommendation:	<input type="checkbox"/> Adopt Amendment	<input type="checkbox"/> Without Committee Recommendation
	<input checked="" type="checkbox"/> Do Pass	<input type="checkbox"/> Do Not Pass
	<input type="checkbox"/> As Amended	<input type="checkbox"/> Rerefer to Appropriations
	<input type="checkbox"/> Place on Consent Calendar	
Other Actions:	<input type="checkbox"/> Reconsider	<input type="checkbox"/>

Motion Made By: Hogan Seconded By: Boehning

Representatives	Yes	No	Representatives	Yes	No	Representatives	Yes	No
Chairman Jeff Delzer	✓		Representative Nelson	✓		Representative Boe	✓	
Vice Chairman Keith Kempenich	✓		Representative Pollert	✓		Representative Glassheim	✓	AB
Representative Bellew	✓		Representative Sanford	✓		Representative Guggisberg	✓	
Representative Brandenburg	✓		Representative Schmidt	✓		Representative Hogan	✓	
Representative Boehning	✓		Representative Silbernagel	✓		Representative Holman		AB
Representative Dosch	✓		Representative Skarphol	✓				
Representative Kreidt	✓		Representative Streyle	✓				
Representative Martinson	✓		Representative Thoreson	✓				
Representative Monson	✓		Representative Vigessaa	✓				
	<u>9</u>	<u>0</u>		<u>9</u>	<u>0</u>		<u>3</u>	<u>2 Absent</u>

Totals

(Yes)	<u>21</u>
No	<u>0</u>
Absent	<u>2</u>

Grand Total

Floor Assignment: Vigessa

If the vote is on an amendment, briefly indicate intent: \_\_\_\_\_

**REPORT OF STANDING COMMITTEE**

**HB 1033: Appropriations Committee (Rep. Delzer, Chairman)** recommends **DO PASS**  
(21 YEAS, 0 NAYS, 2 ABSENT AND NOT VOTING). HB 1033 was placed on the  
Eleventh order on the calendar.

**2015 SENATE APPROPRIATIONS**

**HB 1033**

# 2015 SENATE STANDING COMMITTEE MINUTES

## Appropriations Committee Harvest Room, State Capitol

HB 1033  
3/13/2015  
Job # 24786

- ☐ Subcommittee  
☐ Conference Committee

Committee Clerk Signature

*Doris E. Perry for Rose Lanning*

### Explanation or reason for introduction of bill/resolution:

Relating to the legacy fund, legacy fund principal balance, and transfer of legacy fund earnings; relating to a definition of legacy fund earnings.

### Minutes:

Attachment 1 - 2

Legislative Council - Brady Larson  
OMB - Tammy Dolan

**Co-Chairman Bowman** called the committee to order on HB 1033. Roll Call was taken.

### Jeff Delzer, State Representative, District 8:

Testified in favor of HB 1033. Testimony - Attachment 1.

This bill came out of the Government and Finance committee which he chaired. One of the studies done was to look at the Legacy Fund. We finished this study early in the year before the oil numbers changed. I handed out a sheet with some definitions that are being worked on and also the forecast for the Legacy Fund based on our January forecast.

He went over the handout.

Section 1 - definitions.

Section 2 - clarifies the process of determining how much principal funding is available to be expended by the Legislative Assembly during each biennium.

Section 3 - intent that the committee had. Any fund earnings should be returned to the Legacy Fund until \$40B. That's where the interest would be equal to 33% of the oil and gas tax collections for the previous biennium.

We don't have the authority to spend the earnings and the earnings won't go into the general fund and have to have something done with them until the end of 2017-19 biennium.

There were amendments offered on the House side that would have changed section three from intent to actual language. Intent language doesn't tie the next legislative assembly. Anything we do statutorily, the next legislative assembly can always change. The intent of



the House was that the earnings would go back in unless the next assembly changed the intent.

**Senator Carlisle:** Did you have any opposition, any questions or formal opposition?

**Rep. Delzer:** No, there was nothing formal. There was discussion in House Appropriations about it, but there was no opposition. It was moved Do Pass 21-0.

**Senator Bowman:** With this passing, all the money will stay in legacy fund until 2019 and then the interest...

**Rep. Delzer:** The timing will be by the constitution. There will not be a transfer of earnings until end of 2017-2019 biennium. The 2017 biennium could spend up to 15% of the principal and I think they could appropriate the earnings as well.

**Senator Carlisle:** Is that taking 2/3 vote?

**Brady Larson, Legislative Council:** Yes, for the principal it would require a 2/3 vote. For the earnings, that would be just a majority vote.

**Rep. Delzer:** If you look on the chart (page 2) of the January forecast, the discussion was somewhere in the neighborhood of \$1.1 to \$1.13 to production so these numbers are probably going to drop. It looks at the earnings as being possibly \$124M. Brady is that at the end of 2017 or 19?

**Brady Larson:** That would be for the 2015-17 biennium that \$124M is the estimate.

**Senator Mathern:** Section three really has no impact. It doesn't really change our present law?

**Rep. Delzer:** I would say it does not but it says the intent of this legislative assembly that the next assembly should look at that. The intent will still be there when the next session rolls around.

**Senator Mathern:** In section 2 - It essentially is kind of a work order for the Legislative Council.

**Rep. Delzer:** No, for OMB to actually come up with the number for the principal and I guess they'd work with the treasurer's office.

**Senator Mathern:** Would section 2 have the same level of meaning - wouldn't OMB be doing this anyway?

**Rep. Delzer:** There is nothing in the code or anything that says they should do it, so it would simply be a case where the legislature would have to ask for that information. This simply puts the information out there before the Legislative Assembly.

**Senator Sorvaag:** A lot of this was to deal with the earnings that are happening now. It would be the choice of each legislative body?

**Rep. Delzer:** Correct - #3 on the principal on section 1 that goes to prior of July 1, 2017. On section 2, it says that the governor should not include any of the 15% in his budget proposal to the legislative assembly. That last line says the governor should not include that as part of his budget proposal.

**Senator Krebsbach:** Last week you brought us a bill to take money from the state bank to put into a revolving loan fund for political subdivisions. I'm wondering if you would see that as a good program for the Legacy Fund.

**Rep. Delzer:** I haven't thought about that, I don't know if I would. The legislative assembly can do what they want with that but we also have the legacy investment committee that is supposed to be set up for that.

**Senator Krebsbach:** Sometime down the road, would you see that type of a program as fitting into the Legacy Fund?

**Rep. Delzer:** something like that could happen because the legacy fund does not have the same restrictions that the common schools trust fund has (it has to receive interest the same as it would anywhere else, the state can't use part of the money for low interest loans or anything). 1433 was a low interest loan.

**Senator Bowman** when the legislators figure out a use for this there will be a lot of bills.

**Rep. Delzer:** This is a good way to look at it for this legislative assembly; we really don't have any authority anyway. The idea of saying that the earnings earned to that point is part of the principal, it's a pretty good move. Not being able to use it in the governor's budget is a good move, it should be a legislative decision and it takes a 2/3 vote. When it's in the budget, it's hard to get out.

**Rep. George Keiser,** District 47, testified in favor of HB 1033. Amendment - Attachment 2. Provided background on the amendment: the House subcommittee had completed the work on the Legacy fund and Rep. Delzer said he didn't want to adopt an amendment without a hearing. I support that, so we brought the amendment here. It clearly states that we will utilize local financial institutions for placement of 10% of the amount in the legacy fund for management. They would apply the same standards in selecting the local management firms to manage these dollars. These are our funds, in our state. There was frustration with the placement of the funds in one source and not getting an opportunity for a slice of the pie. They pay taxes, they employ people in our state, it is not fair, nor right, they should have an opportunity. I think this provides a very good opportunity. What if local firms don't produce the same results in their investment of this 10% compared to the 90%, what if they do? What basis are we using to compare the 100% investment currently in terms of how well it is performing; it may be better than the average or below the average. I suspect our local firms will be very competitive in the placement of their investments. It gives us an opportunity for a 2yr period to test it. We can always come back and change it. We worked very hard with attorneys and Legislative Council. The language is very general

because that leaves the decision making where it should be within the investment board and we don't want to get too specific on details.

**Senator G. Lee:** when the board that over oversees these investments seeks investment managers, are local banks excluded now?

**Rep. Keiser:** I don't know, it has historically been placed in one fund, in one large bid. Do you want it to happen from policy perspective?

**Senator Mathern:** aren't some of our financial institutions that can invest this money, part of national firms that do this? Wouldn't Wells Fargo and other banks already be able to do this?

**Rep. Keiser:** Yes, most firms that would qualify given the standards of the investment board won't be solely ND company. They are making an investment in our state and we should help them be successful as they operate in our state.

**Senator Sorvaag:** the intent is to give them dollars to invest, there are no strings attached.

**Rep. Keiser:** We want them to maximize the investment so that is true.

**Senator Wanzek:** Are you suggesting we replace section 1 with your amendment?

**Rep Keiser:** I don't think so, it's an amendment to section 2110-11 Legislative Council drafted; they will answer questions which are way beyond my scope. Intent was to make a correction.

**Senator Bowman** who decides which banks will participate?

**Rep. Keiser:** The investment board establishes the criteria for selecting firms that will manage the investment dollars.

**Rick Clayburgh**, President, CEO, ND Bankers Association, in support of Rep Keiser's amendment. Some of the language is broader; it gives the state investment board the authority to work with local companies. We have a number of trust banks in the state that invest billions of dollars on behalf of ND, dollars that are invested with fund managers that look at specific industries. They are based in NY, NJ and elsewhere. All of the income that comes back to the state is based on the prudent institutional investor rule under the direction of the state investment board. Our local financial institutions that have a considerable amount of experience aren't given that opportunity because they operate in a different funding arrangement. They try to break them out into individual investments, other types of products. The board looks at a return based on 3-5 years. Our trust companies in ND are having their portfolio returns on their trust equal to the state. They might not be at the same level but they're comparable. This is based on the legacy fund, but could be any fund; lets' keep that fee in ND. We are just talking about a little sliver, app \$200M.

This bill will be heard again on Tuesday because our Trust Expert will be here.



**Senator Heckaman:** You said the investment would not be quite at the same level but comparable? Total amount in fund right now will be about what? Can't they already invest that in ND if they want to?

**Mr. CLayburgh:** When you deal with different investment houses, their investments are slightly different; they have their own fund managers so I can't say they're identical. Our trust companies have investment managers who are same ones used in NY and NJ. The fair value would be \$2.2B (6/30/14). The state investment board deals with a consultant who manages these dollars and finds the firms that deal with investment dollars. They have not been allowed the opportunity to bid in.

**Senator Heckaman:** if I go back to the advisory board minutes, I'd find this in the minutes?

**Clayburgh:** My request no. We have institutions they've been working with for some time; I don't know how they have been doing that.

**Senator Robinson** how many trust companies in ND right now?

**Clayburgh:** We have specific trust companies and banks with trust powers.

**Senator Robinson:** During time of downturn in marketplace locals did as well or better.

**Clayburgh:** I won't say that we'll perform better, less or as good as - things can always change with time. The state investment board would set the rules. It wouldn't be every bank in the state; we are talking about institutions that have considerable investment knowledge.

**Senator G. Lee:** Maybe we should be looking at advisory board in terms of how they determine who can invest. I've been in these situations; boards determine how much money to allocate into growth, value, bonds, etc... they put out an rfp and get proposals. Just saying that we're going to give 10% to local institutions, they should propose what they could do in a certain sector of those available funds. Putting this to into state law could not be the place. I am trying to think thru this. Why 10%, not 20-25%. We should have advisory board do that as opposed to us saying it.

**Clayburgh:** Our witness coming in on Tuesday will provide more details. It's not the state investment board, probably has more to do with the consultants who put the big packages in. RFPs could be written in such a way that we can be involved. 10% is trying to be realistic. This is over a 2 year period, and then let's see 3-5 years.

**Senator G. Lee:** did Rep. Delzer say we'd like to get it to \$40B? Then 10% is a big number.

**Clayburgh -** We want something to start with, to get something done now for a short period. Put a sunset in, let's see and at that point take the constraints off

**Chairman Holmberg** let the sponsor of the bill know that we have more on Tuesday.

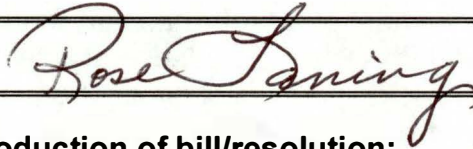
# 2015 SENATE STANDING COMMITTEE MINUTES

## Appropriations Committee Harvest Room, State Capitol

HB 1033  
3/17/2015  
Job # 24962

- ☐ Subcommittee  
☐ Conference Committee

Committee Clerk Signature



### Explanation or reason for introduction of bill/resolution:

Relating to the legacy fund, legacy fund principal balance, and transfer of legacy fund earnings; relating to a definition of legacy fund earnings.

### Minutes:

Attachment 1 - 2

Legislative Council - Brady Larson  
OMB - Tammy Dolan

**Co-Chairman Bowman** called the committee to order on HB 1033.

**Marilyn Foss, North Dakota Bankers Association:** We're coming to follow up on the discussion we had last week about an idea for the expanding the investment managers who take care of the funds in the legacy fund. I would like to start out by introducing Bob Willer.

**Bob Willer, American Trust Center in Bismarck:**  
Testified in favor of HB 1033. No written testimony.

I'm here in support of the amendment for HB 1033 as an idea to explore some opportunities that we feel that might be great for the state of North Dakota. I am in the Trust Department at American Trust Center in Bismarck.

Over the years, what we do in managing assets for different institutions that there are a number of opportunities that might be available with the State of North Dakota. Ten or twelve years ago, we started the process of trying to familiarize ourselves to come to the State Investment Board meetings on a monthly basis in trying to meet with people to see why we couldn't be one of the managers that was selected to manage (today) over \$9B in funds that the state is responsible for.

We tried on several occasions and visited with board members. We visited with the State Investment office with varying degrees of success. Sometimes it was that you're not qualified in the way we manage the money and we would look for ways that we might be qualified and really believe that we are; that we do things no different than many of the money managers that you currently have. We have the same fiduciary responsibility by which any trust department is bound.

In September of last year in the Pension and Investment magazine, it often highlights what is happening in the different states. In the article, referencing North Dakota, said "the North Dakota State Investment Board in Bismarck, hired JPMorgan asset management to run it's \$118M in mortgage backed securities said David Hunter, executive director and Chief Investment Officer. The Board which oversees \$9.2B in assets, including \$4.6B in pension assets conducted the invitation only search earlier this year because existing manager, Western Asset Management Company was on watch for personnel changes. Talon Associates assisted." It was another reminder that we were not included in that search. When I left Bell, we were currently managing over \$3B in assets from insurance companies, from college foundations, from hospital foundations, from YMCA foundations and wondered why we would not be included. It seems to come back to the way the guidelines are written almost to preclude anyone from ND to be able to manage those assets. You'll hear today from some of those that are here that have used North Dakota institutions to manage those funds that were every bit as qualified. Our performance is every bit as good. Long term/short term the averages will show you that we would do the kind of job that anyone else would do that's in this business.

When I think of taking a sliver of \$9B and reinvesting it in North Dakota institutions who live and die here; who's money it comes from, that if we had just a sliver and instead of paying in excess of \$31M dollars in fees that leaves the state. We hear over and over again how great ND is. We hear about the well run state government. We're one of two states in the black. We hear about the great talent in workforce that we have. You can take a North Dakota person, put him anywhere in the United States, and if they apply for a job, they're going to get the job because they know how good people from ND are; that they show up for work. Even if it's blizzarding, they'll find a way to get there. But when it comes to managing the state dollars, we're not good enough and that money leaves the state managed by other institutions and money managers. If we took a sliver of those dollars and invested it with institutions in ND, that would be a big deal for any of us. The bankers, in any of the communities who have the ability to do this, are the first ones that anyone comes to for any capital fund raising drive. Anything that's going on to improve the community, the bank is generally the lead donor. Why wouldn't we try to make our communities better by giving them an opportunity to do what they do in a professional way with the fiduciary responsibilities - and allow them to give back to the community even more? For all of us in the state of North Dakota, it's a win-win scenario.

(8:10)**Senator G. Lee:** You said you talked to the investment board and the people on it. What are the specifics they give you that don't allow you to participate?

**Bob Willer:** I can go back over the years and at one time we were told, "What kind of manager are you?" "Are you a large cap growth manager or are you a small cap value manager? We search and find the best managers in each of those spaces, and that's who we hire." Any institution in North Dakota is going to specialize in that one area. We have equity portfolios. We have fixed income portfolios. We do fund to fund management which are things that are done. But "You've got to specialize and then you can apply and we can consider you." But to not be invited; to not be a part of; I've not seen an RFP that has ever gone out that would include us that would give us the opportunity. We got close to exploring when Mr. Solberg and Bruce Furness came out and visited with then Lt. Gov. Dalrymple. He told Steve Cochrane, at the time, to see if there wasn't a way that they



could do business. It was shortly after that that Steve took his life and was not there anymore.

**Senator G. Lee:** The question is what do you need to specifically be a part of this. Is the slice too big that they're offering? Do you need an annuity section or a bond section. The treasurer asks for money to be put into state institutions and now they're not really interested in it in the way she wants to put it in, so what are you looking for? Be more specific in terms of the answers.

**Bob Willer:** This is not a savings account. If we're thinking of offering up CDs, that not what we're talking about. We're talking about managing the investments from the funds that are part of the \$9.2M. If the guidelines that have been established over the years for their selection process, was such that we could manage money like they do for it. We are not specialized in the large cap growths. We do a composite; or let us do fixed income and try it on for a three year period. In any way, you may be the best; you may be the worst, but if you average it over time, you'll find that anyone of these institutions is going to be competitive.

**Senator G. Lee:** So if it was a composite of a variety of fund sources and a small enough slice that your group could participate in, that would satisfy an area that you could participate in?

**Bob Willer:** I believe so. There would be more detail to be worked out. I think that there's probably not any one of us that can take on \$9M dollars and be a good manager for you. We're not asking that. All we're asking is to consider what a small sliver might do for the institutions in the state set up in a way that we could manage, we could benchmark, where you could monitor, where we could keep track of and see how we do. Just like any other money manager that currently is on board, if we're not performing, get rid of us.

(12:40) **Senator Carlisle:** What would be wrong with putting a sunset clause on the bill? It would give you a shot for a couple of years, you report back and is that too short a window?

**Bob Willer:** When you look at averages of money managers, you're looking at 3,5 and 10 year increments. I'm thinking we'd want to at least look at three years.

**Senator Bowman:** What we're really looking for on the money is return on investment. If your opportunity to meet and take part of that portfolio and show the state that you're return back to the state is going to be as good, if not better. What I looked at from a business standpoint is that by doing that, part of that money that you generate from operating this stays in the state of North Dakota and gets reinvested in the state and it's a win-win deal for the whole state.

**Bob Willer:** That's exactly how we look at it. North Dakota derives its income from doing this kind of work. The reinvestment that we can make in the communities that we work, live and play in is a win-win. From a government standpoint, wouldn't the public love to know that as a state, we're looking for ways to improve our communities by simply managing?

**Kevin Dvorak, President, North Dakota Community Foundation:**  
Testified in favor of HB 1033. No written testimony.

We are a statewide non-profit organization that has the fiduciary responsibility to the investment board and we fulfill that obligation by investing in North Dakota institutions for nearly all of our investment portfolio. We currently have six investment advisors. They are bank trust department's wealth management divisions in ND. I'm a certified financial planner certificant so I have an education in financial matters. I also have twenty five years' experience at the North Dakota Community Foundation. Most foundations use a similar system to what ND does. We're a little bit different in that respect, in that we thought that if we're a ND institution, we ought to invest in ND institutions and use that expertise that's here in North Dakota. We are members of the National Council on Foundations. We participate in a quarterly survey of our peers for investment returns. We benchmark ourselves against those other institutions across the country. Our returns over the last 25 years that I've been at the North Dakota Community Foundation are generally at or above the mean for our peers across the country and many of them employ Kalon and SEI and all those large firms, but they actually long term, do no better than the ND Community Foundation does by investing in First International Bank, Bell State Bank, US Bank, Bremer, Wells Fargo and Bank of the West, currently. We have those relationships ongoing. We give them a full portfolio so each of those advisors gets an investment policy that's passed by the Board of the Community Foundation. They all have the same investment policy in which to invest its diversified portfolio. We benchmark them against each other on their total net return of net of fees and then those that are doing better get more money; those that are not doing so well, don't get any new money; and if they're poor enough, they get put on probation. If they continue to do poorly, then the money is moved somewhere else. This gives us the ability to compare apples to apples. When they have the same investment policy to follow, you can benchmark them against each other whenever you want to.

(18:40) **Senator Robinson:** Have you noticed any significant difference on fee structures?

**Kevin Dvorak:** There is a variation, but it's generally a stepped fee depending upon how much money we have. We generally try to get them to at least \$6M per advisor. Some of them are approaching \$20M in assets and so the fee structure is stepped. We pay between 30-60 basis points for investment advice.

**Senator Heckaman:** When you invest in those 6 banks, do they invest that money only in ND?

**Kevin Dvorak:** No, that's a fallacy. There is really no way for you to invest only in ND companies and meet your fiduciary responsibility. You have to be diversified. We are making those institutions stronger by investing with them. They have a presence here. They live here. They give here and do things in ND. They are the relationships that we think are important. We're making those institutions stronger by using them, but there is no way we could say you can only invest in North Dakota institutions. That's not a practical way to go.

**Senator Heckaman:** Do you know what percent stays in ND of your investments and what goes out and is invested out of state?

**Kevin Dvorak:** If you were to look at Fortune 500 companies, we have one in ND - MDU Resources. I don't know if there are still some S&P 500 or not. I would say that a very small percentage is invested in ND companies if you look at the stocks and bonds because there isn't a market of sufficient size to do that. When you support those institutions that have a presence here, you make those institutions stronger and that is good for the community.

**Senator Heckaman:** My thought is that they'd be investing in their local community by lending that money in their local community, but that's not so?

**Kevin Dvorak:** We're not in the banking business. We're in the investment business and there is a difference between running a bank and loaning the money to ND organizations. That's another way of investing money. We are investing money in the full economy of the world. That's the way you have to if you're going to maintain your fiduciary responsibility. You could say a certain portion of it has to go to ND banks and it has to be lent out to North Dakota institutions, but that is micro managing to some degree and we don't generally do that.

**John Stibbe, Wealth Manager and Senior Vice President, First International Bank and Trust:** Testified in favor of HB 1033. No written testimony.

The First International Bank and Trust was established in 1910 so we've been in the State of North Dakota for over 100 years and we continue to grow and see our commitment to the state and communities grow. Today, we're about a \$2B bank and employ over 500 employees. In 1992, we established our trust department and currently manage about \$700M in assets and we also work with the ND Community Foundation.

(Told of two situations where North Dakotans had moved out of state and are currently back home working for their bank.)

As a North Dakota institution, we're familiar with the "prudent investment standards" under the NDCC and we have a well-defined strategy for managing our client portfolios. As a North Dakota bank, we have a vested interest in the prudent investment of the Legacy Fund. The trust industry in this state has a rich history of managing funds in a fiduciary manner. The duties of a trustee under the Century Code guide our industry and help define the strategies we employ to build prudent strategically diversified strategies for our clients. If we were working for the State Investment Board, we would work with them in a very close manner to make sure that we are in compliance with their investment policy statements. The amendment proposed in HB 1033 would support the objectives of the legacy fund by having ND institutions governed by the Century Code's prudent investment standards while managing a portion of the legacy fund. The local financial institutions in our state are well qualified to effectively and efficiently manage funds for the legacy fund. Keeping a portion of these funds to be managed in the state, the fees for managing those funds will stay in ND and will benefit North Dakota institutions.

(24:50) **Senator G. Lee:** We're told that the investment board isn't really cooperative in terms of allowing your size of investor. What size of dollars would meet your ability to participate in the investment opportunity that's here?



**John Stibbe:** From our perspective, we would not have an issue with the size of the investment dollars. The reality is that we have foundation clients where we're managing \$50M dollars. We'd have no problem with a \$50M - \$100M investment in our shop. It's a scalable strategy and because we have a staff that is able to handle that.

**Senator G. Lee:** \$50M-100M - your trust company could manage that size of a portfolio? (Answer - Correct.)

**Senator Sorvaag** asked what the fees would be on \$100 M. The fees that you'd earn on the \$900M is what would stay in the state?

**John Stibbe:** It would depend on the size of the portfolio. As you get to the larger commitment, you see your fees reduced. His estimate of 30-60 basis points is a fair estimate.

**Senator Sorvaag:** \$20-30M would stay in the state, then? That's the earnings? I'm trying to put together a number of why we are doing this. You'd invest \$900M.

**John Stibbe:** One percent of \$900M, you'd be at \$9M and with 50 basis points would make it \$4.5M.

**Senator Robinson:** What are the total fees we are paying now under the current structure?

**Dave Hunter, Executive Director & CIO, ND Retirement and Investment Office (RIO):** The Legacy Fund spent approx. \$4.8M in fees for the fiscal year ending June 30, 2014. That approximated 27 basis points on the assets at that time.

**Senator Robinson:** What are we paying on the full \$9M?

**Dave Hunter:** For the fiscal year ending June 30, 2014, we spent \$44M on fees - that was on an average asset base of about \$8.5B

**Kevin Strege, Banker and also representing the Bismarck-Mandan Chamber of Commerce:** Testified in favor of HB 1033. No written testimony.

The Chamber's support for this is a basic support of competition; that there has not been the allowance of. There has not been the use of North Dakota institutions. We fully expect them to all be held to the same standards, both in terms of fiduciary and in terms of fees as the current level. The way to find that out is to allow them a chance. There is economic development and there is a multiplier effect. Money that is created with new jobs in a state spends thru the economy multiple times as this competitive process is allowed to progress.

**Senator O'Connell:** Of the \$44M in fees, what did we make or what was our return?

**David Hunter:** For the overall \$9B, (talking in percentage terms): For the pension trust itself, for the fiscal year ending June 30, 2014, we earned about a 16% return; for the insurance trust, it varied because of the assets, but included the Legacy Fund, it ranged

from as little as 2% for the budget stabilization fund up to 17% for the Cultural Endowment Fund. The Legacy Fund itself, ending December 31, 2014 generated a return of 4.2%.

**Laney Herauf, Greater ND Chamber, Lobbyist # 145:**

Testified in favor of HB 1033. No written testimony.

Wants to inform the committee that the Chamber supports the legislation and feels that investing in North Dakota institutions is a good way to create economic development and bring people back to ND and create jobs.

**David Hunter, Executive Director/CIO, ND Retirement and Investment Office (RIO):**

Testimony - Attachment 1.

State Investment Board and Legacy Fund Investment Overview - Attachment 2.

(40:16) **Senator Bowman:** Do you charge a fee? You show a net return of 1%. What fee do you take out of the total amount to cover the cost of administrating this?

**David Hunter:** The net investment return takes into account the administrative expenses of the Retirement and Investment Office. It's less than 1 ½ basis points; that's one and a half one hundredths of one percent. It's a very small number. When I said in excess return of one percent, that's over a benchmark, We're delivering not only passive benchmark returns, but excess returns on top of that. If you step back and look at the amount of money we spend in the Legacy Fund for investment manager fees versus our excess return just for the recent year. For the one year period ending 12/31/14, we generated about 60 basis points or .6% of excess return. For the one year period ending 6/30/14, we spent 27 basis points or .27%, so we actually got a better than a two for one return on our investment dollars. Many times people say "Gee, we're sending dollars out of the state". If I could send one dollar out and get a multiple of that back at the end of every year, that's a great investment decision. That's what is happening with our State Investment Board asset allocations investment manager decisions. We're getting better than a two for one return on an annual basis, at least for the past year, two and three year period overall.

**Senator Carlisle:** Who did the research? There are some bankers in here and I hope they'll comment. Have they seen a copy of your testimony?

**David Hunter:** I have not made my testimony available before hand, but I'd be happy to provide them a copy. NDCC 21-10-07 relating to the "prudent investor rule", and it is pretty black and white. The goal of the NDCC when it comes to investing is to always make sure we are being prudent. We're not going to try to focus on what I'd call economic re-targeted investing. It's not to say we wouldn't participate in it if the overall return in that economic re-targeted investing was as good or better from liquidity risk return overall profile.

**Senator Robinson:** Aren't we talking about a pilot, and if it's equal or greater, fine. If not, we discontinue it. I'm a little troubled that we're going to send a message to the state and if you want a good investment, you have to go outside ND. If you look at the 2008 downturn, it wasn't ND banks. It was the big banks we're talking about.

**David Hunter:** There is no prohibition whatsoever against ND institutions. What this amendment proposes is saying that we're putting a minimum requirement. It says "the

investment board shall place at least 10% of the legacy fund assets with one or more financial institutions. From a practical matter, we're not sitting down and asking how we can get ND institutions involved so much as what's the best thing to do for the fund overall and if we can align a match, it's what we look to do.

**Senator Robinson:** I'd like to see that happen, but history has told us that hasn't happened and that's why this is before us. If this would've happened, we wouldn't be dealing with this today. Shouldn't our ND companies not have at least an equal opportunity and if they fall short, they fall short? If need be, we can re-structure the language.

**David Hunter:** The issue that you have is when you start putting minimum thresholds and saying you have to do something. If there's an opportunity where our interests are aligned, it can meet and we can find a great scenario, but there's been no impetus to do that.

**Rick Clayburgh, President and CEO, North Dakota Banker's Association:**

Thank you for hearing us a second time as witnesses were not available last Friday. Saying ten percent of the funds need to be invested through investment managers is not imprudent. It does not violate the prudent investor rule. Our financial institutions have to follow the prudent investor rule themselves. Specific to the NDCC, this is the legislature, the policy making branch of government, amending another section of code. The last to pass is what controls so if there is even a perceived conflict, it's the legislature saying that we're going to do this now and it controls so 10% of funds would be under management of prudent investors of ND. We don't see what the concern is. If there are issues with other funds, if there are legal issues there, if there's a way that we can sit down with this committee and come up with amendments to fix issues, if there are issues. We're open to that and we'd like to make this a workable bill.

**Senator Bowman:** Different things that we've done with different groups, we always ask for accountability before the next legislative session which would ease a lot of the pressure just to show that if we do this, that it's working. That takes pressure off of us because we're accountable to people. When we make that decision and come back in a year and you can show that you've done very well with the fund, it's a win/win deal for us, but if you don't... I'd like to see it, if we're going to do the 10%, that there is some accountability and there would be some reporting in every biennium to the legislative body before the next session.

**Rick Clayburgh:** We would agree. We would certainly be a part if you wanted to put a study or reporting back, we'd be part of it. This would still be under the State Investment Board. We would be line items in the report, and you'd see the same return that you see on all other investments that are shown under the State Investment Board report. We would be open to making a specific report to this legislature about the performance of our ND institutions.

**Chairman Holmberg:** The amendment that is the crux of the discussion is over a month and a half old. How much dialogue was there between your groups and the treasurer's office and the board regarding this language to try to work out any differences before the pickle is put on our plate?



**Rick Clayburgh:** This was Representative Keiser's amendment and at first we were deferring to Rep. Keiser. After the point that we had met with Legislative Council and Rep. Keiser, we reached out to you. We did not have discussions with the investment board. Again, we're talking about the Legacy Fund. At the time, we didn't anticipate concern with it. I was visiting with the Lt. Gov. and I understand there are some issues there. And if there are or there's a way we can address some of the concerns they have, we're open to it. Specifically, we're talking of the Legacy Fund, none of the other funds that may have other types of restrictions on it. To your question, we did not and I don't believe Rep. Keiser had any discussions with them.

**Kelly Schmidt, North Dakota State Treasurer:** I am currently the longest serving member on the State Investment Board and I'm disappointed to hear that there's a miscommunication in our process. From hearing some of the discussion today and last Friday, I think there really is a miscommunication on how we do things. Also, during my 10 year tenure on the board, I have not been approached by any ND bankers relating to an opportunity to do business with the State Investment Board and I would welcome that conversation. We do have a process and it has worked very well for us for a very long time not only in the sense that we honor our fiduciary responsibility, but it has brought responsible returns to what we do for the people of ND. That process added 1% of alpha (see footnote) to our overall funds of what we do. We don't go out and pick managers. We have a process in which we have a structure in which we need to hire someone. We go to our consultant and say we're looking for a manager that can do this. They go out into their system and they find us a group of however many there may be and we drill it down and drill it down and drill it down until we perhaps have four or five. Then our RIO staff drills it down and drills it down until we get the best of the best. That is how those managers come to us. We have gone thru the due-diligence of that process. We do business with the Bank of North Dakota. We have over \$100M invested with the Bank of ND. I would state that that too puts dollars into our state and brings opportunities for housing and different things as it relates turning our economic development.

Something else that I've heard that is not correct is that we don't RFP our process. Century Code 21-10, the prudent investor rule does not require us to RFP so if someone is expecting an invitation to come and bid and be part of that process, never in my 10 year term have I understood anyone to have an opportunity to be invited. You're invited to go thru the process to work with our consultants and be part of that portion and we would be more than happy to sit down with anyone that wants to learn and understand how that process is. Our fiduciary responsibility is number one and only number one - and that is to do the very best that we can for the legacy fund and pension funds for the state of ND. They are ND dollars and we have the prudent investor and fiduciary responsibility to all of them. It's very different for us to have someone point a finger and say now we have to cherry pick.

Our managers are consistent. It would not be fiscally responsible for us to hire someone with the intention that they were only going to stick around for a couple years. It costs us money to uninvest and reinvest. Every time we change a manager, it costs us and the people of ND dollars and so if we invest with a company and if we've done it well, I hope we never have to change them. We have manager reviews regularly where we are watching and we are paying attention to their management structure, to their team, to their returns and we have a criteria that our board and staff pay a lot of attention to. We have hired

managers and fired managers, but that being said, I am happy to answer any questions. I know myself and fellow board members and the Retirement and Investment Office would be happy to sit down with this group and have a conversation because until last Friday, we didn't know anything about this amendment.

**Chairman Holmberg:** I would suggest this committee is not a referee and I think your suggestion that you all get together and do some visitation before we take this bill up, we've got time. We are busy this week and next week so hopefully between that time.... We will discuss the bill in this committee over a week from now but you've got to have that dialogue, unless we have to pick a winner or loser and we don't always do a good job doing that.

**Drew Wrigley, Lt. Governor, State of North Dakota and Chairman of the State Investment Board:** I think there are a couple points that do need to be made. The entire investment board welcomes every opportunity and would certainly be glad to stand up here and say we have a strong preference for investing in the State of ND, or even a small preference, a 10% preference as a compromise position. But we have real legal mandates that we would be forced, by this amendment, to violate one of. We'd be able to choose tho, which legal mandate or who do we want to be sued by. Do we want to be sued by the people who hold pensions in the State of ND because we've violated the prudent investor rule which is not a negotiable matter, it's a maximization requirement. So do you want to be sued by all the teachers, and the firemen and the police officers, and the state employees for not maximizing? Or do we want to violate the new mandate from the State of ND? We'd love to find a way that we could have that preference. Treasurer Schmidt points out that no bankers have approached her. Several bankers have approached me, probably as chairman of the committee. A former governor has approached me on behalf of an interest. Every single time, I tell them the same thing. My requirement is that I be objective about it and that I then turn those people over to the process with our staff and they follow through. I would love it if they came back and said, "Following our objective process, meeting our legal obligation on behalf of, by the way, not just those pensioners, the State of ND has a strong financial interest. When those dollars are not maximized and we don't meet the mandate, you all have to come through with the money that you promised people under their pensions. You have to come up with that money when we don't meet our mandate to maximize if we're not going to. It's an untenable choice. I would say this on the compromise. This is a situation we can't compromise. There is a valley with a river a long ways down. You can take the road that we are required to legally or there is the other road. There's no compromising or you're falling into the abyss. We have to meet those legal obligations. This would put one on us that would make us choose. We could choose though. Who do you want to be sued by? Which law do you want to violate? Access to make the pitch - any and every entity who has approached me, including the entity which was known to the former ND governor got the same exact treatment and the same fingers crossed. I hope that it works out. It was mentioned that Bell State, as some time back, I think it was implied to this committee that had there not been the death of Mr. Cochran, and maybe if Lt. Gov. Dalrymple hadn't become the governor, it might have changed. I can tell you that it would have been the same result. Bell State approached us recently again and I did the same thing. We turned them over to the process. We crossed our fingers and hoped. I hope that it works out the very best way. Nothing in our process forecloses anyone from ND. I don't think anyone can

seriously wonder, if any member of that board wouldn't like to prefer, but we're not legally allowed to prefer anything other than attempting to maximize on behalf of the pensioners and on behalf of the State of North Dakota. We'd be anxious to meet and talk. Could there be some legal ground established, where you could stand on where we would be relieved of legal obligation that we now have - which is a serious one for which we could be sued when we violate? If that legal ground could be established, of course, we'd be willing to entertain that and have any and all discussions. I'll leave it at that. We're sympathetic, I get the impulse and we're all in politics so I get the impulse of wanting to do something that is favorable to your constituency. We understand it. It would be easy also, especially for Treasurer Schmidt and me, to not come into this room and have to testify, hide in the hallway and we not come in and testify, and just send our staff in. But it's a serious obligation that we've a sworn obligation, a legal obligation to meet. With that said, we look forward to the opportunity to talk with the members, but we have to include the AGs office because there's a legal foundation that has to be established. We're open to the discussion. Thank you to the committee and I could answer any questions.

**Chairman Holmberg** closed the hearing on HB 1033 and we will be in touch with the groups prior to when we take the bill up again.

#### DEFINITION of 'Alpha'

1. A measure of performance on a risk-adjusted basis. Alpha takes the volatility (price risk) of a mutual fund and compares its risk-adjusted performance to a benchmark index. The excess return of the fund relative to the return of the benchmark index is a fund's alpha.

#### INVESTOPEDIA EXPLAINS 'Alpha'

1. Alpha is one of five technical risk ratios; the others are beta, standard deviation, R-squared, and the Sharpe ratio. These are all statistical measurements used in modern portfolio theory (MPT). All of these indicators are intended to help investors determine the risk-reward profile of a mutual fund. Simply stated, alpha is often considered to represent the value that a portfolio manager adds to or subtracts from a fund's return.

A positive alpha of 1.0 means the fund has outperformed its benchmark index by 1%. Correspondingly, a similar negative alpha would indicate an underperformance of 1%.



# 2015 SENATE STANDING COMMITTEE MINUTES

## Appropriations Committee Harvest Room, State Capitol

HB 1033  
4/7/2015  
Job # 25854

- ☐ Subcommittee  
☐ Conference Committee

Committee Clerk Signature



### Explanation or reason for introduction of bill/resolution:

A BILL for an Act to create and enact three new sections to the NDCC, relating to definitions for the legacy fund, the legacy fund principal balance, and a transfer of legacy fund earnings; and to repeal a section of the NDCC, relating to a definition of legacy fund earnings. (Do Pass)

### Minutes:

No attachments

**Chairman Holmberg** called the committee to order on Tuesday, April 07, 2015 in regards to HB 1033. Roll Call was taken. All committee members were present. Adam Mathiak, Legislative Council and Becky Deichert, OMB, were also present. We have four bills that have come back. We'll talk about them before we go up to floor session today. We will start with 1033. HB 1033 has to do with the definitions for the legacy fund. The banks gave us some great information the other day. They've been working with the State Investment Board and others and are to be thanked for their input, as I understand they're planning to work together with the entities over the next while, after the session.

**Rick Clayburgh, President of ND Banker's Association** stated they wish to back away from their amendments.

**Chairman Holmberg:** if they backed away from their amendment is there a proposal from the committee on 1033? That was the only amendment we had.

**Adam Mathiak, Legislative Council:** The main purpose of the bill is to create some clarity, because the constitution for the legacy fund didn't give precise explanations on certain things. The intent of this bill was just to provide some additional clarity, things like what is at the end of the biennium mean; what exactly is composed of the earnings and principle, and to define the total revenue, as far as what is that excluded. It's not based on the total revenue with the allocations that go to the tribes. It's the 30% of the revenue after deducting out the portion that goes to the tribal allocation. It's mainly just to provide some clarity. There is also the additional language that OMB would be the one that's going to determine the limitation, there is a 15% of limitation of spending the principal and so this just identifies OMB as the office that will determine that amount. There was some intent language that was added related to the legacy fund transfers. Essentially it is that the

transfers will go back into the fund to accumulate so be transferred to the general fund but then transferred back from the general fund to legacy fund. So that was just section of intent in section 3. (4.32)

**Chairman Holmberg:** It came from the interim committee and it was a technical correction and then we had suggested amendments that had been offered and those amendments were withdrawn so what we have is an interim technical correction bill for defining the legacy fund. Do we have a motion?

**V. Chairman Krebsbach moved a Do Pass on HB 1033. 2<sup>nd</sup> by V.Chairman Bowman.**

**Senator Robinson:** This is an example of an exercise that works, the two sides come together. We opened up some communication. We'll see what happens in the next couple years. No one was suggesting that we bend or break the rules. Let's hope things will work out. In the past the communication wasn't there. I feel good about this.

**Chairman Holmberg:** Would you call the roll on a Do Pass on HB 1033.

A Roll Call vote was taken. Yea: 13; Nay: 0; Absent: 0. V. Chairman Krebsbach will carry the bill.

The hearing was closed on HB 1038.

Date: 4-7-15  
Roll Call Vote #: 1

**2015 SENATE STANDING COMMITTEE  
ROLL CALL VOTES**  
BILL/RESOLUTION NO. 1033

Senate Appropriations Committee

☐ Subcommittee

Amendment LC# or Description: \_\_\_\_\_

Recommendation: ☒ Adopt Amendment  
☒ Do Pass ☐ Do Not Pass ☐ Without Committee Recommendation  
☐ As Amended ☐ Rerefer to Appropriations  
☐ Place on Consent Calendar  
Other Actions: ☐ Reconsider ☐ \_\_\_\_\_

Motion Made By Krebsbach Seconded By Bowman

Senators	Yes	No	Senators	Yes	No
Chairman Holmberg	<input checked="" type="checkbox"/>		Senator Heckaman	<input checked="" type="checkbox"/>	
Senator Bowman	<input checked="" type="checkbox"/>		Senator Mathern	<input checked="" type="checkbox"/>	
Senator Krebsbach	<input checked="" type="checkbox"/>		Senator O'Connell	<input checked="" type="checkbox"/>	
Senator Carlisle	<input checked="" type="checkbox"/>		Senator Robinson	<input checked="" type="checkbox"/>	
Senator Sorvaag	<input checked="" type="checkbox"/>				
Senator G. Lee	<input checked="" type="checkbox"/>				
Senator Kilzer	<input checked="" type="checkbox"/>				
Senator Erbele	<input checked="" type="checkbox"/>				
Senator Wanzek	<input checked="" type="checkbox"/>				

Total (Yes) 13 No 0

Absent 0

Floor Assignment Krebsbach

If the vote is on an amendment, briefly indicate intent:



**REPORT OF STANDING COMMITTEE**

**HB 1033: Appropriations Committee (Sen. Holmberg, Chairman)** recommends **DO PASS** (13 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). HB 1033 was placed on the Fourteenth order on the calendar.

**2015 TESTIMONY**

**HB 1033**

Introduced by

Legislative Management

(Government Finance Committee)

1 A BILL for an Act to create and enact three new sections to chapter 54-27 of the North Dakota  
2 Century Code, relating to definitions for the legacy fund, the legacy fund principal balance, and  
3 a transfer of legacy fund earnings; and to repeal section 21-10-12 of the North Dakota Century  
4 Code, relating to a definition of legacy fund earnings.

5 **BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:**

6 **SECTION 1.** A new section to chapter 54-27 of the North Dakota Century Code is created  
7 and enacted as follows:

8 **Definitions for the legacy fund.**

9 For the purposes of section 26 of article X of the Constitution of North Dakota:

- 10 1. "At the end of each biennium" means after cancellation of unexpended appropriations  
11 pursuant to section 54-44.1-11.  
12 2. "Earnings" means net income in accordance with generally accepted accounting  
13 principles, excluding any unrealized gains or losses.  
14 3. "Principal" means thirty percent of total revenue derived from taxes on oil and gas  
15 production and extraction deposited in the legacy fund, earnings of the fund accruing  
16 prior to July 1, 2017, and any funds transferred by the legislative assembly into the  
17 fund from any source.  
18 4. "Total revenue derived from taxes on oil and gas production or extraction" means  
19 taxes collected from oil and gas production or extraction pursuant to chapters 57-51,  
20 57-51.1, and 57-51.2, excluding the amounts allocated to the Three Affiliated Tribes.

21 **SECTION 2.** A new section to chapter 54-27 of the North Dakota Century Code is created  
22 and enacted as follows:

1     **Legacy fund expenditure limit determination - Draft appropriation act restriction.**

2     The director of the office of management and budget shall determine, by December first of  
3 each even-numbered year and at other times as requested by the legislative management, the  
4 amount equal to fifteen percent of the principal balance of the legacy fund, which may be  
5 available for expenditure during a biennium in accordance with section 26 of article X of the  
6 Constitution of North Dakota. The determined limit on available funds must be included in the  
7 budget data presented to the legislative assembly as provided for in section 54-44.1-07. The  
8 available funds may not be included in draft appropriations acts under section 54-44.1-06.

9     **SECTION 3.** A new section to chapter 54-27 of the North Dakota Century Code is created  
10 and enacted as follows:

11     **Transfer of legacy fund earnings --Intent.**

12     Any legacy fund earnings that are transferred to the general fund in accordance with  
13 section 26 of article X of the Constitution of North Dakota must be transferred immediately by  
14 the state treasurer to the legacy fund to become part of the principal of the fund. ~~It is the intent~~  
15 ~~of the legislative assembly that the earnings of the legacy fund continue to accumulate as part~~  
16 ~~of the principal of the fund until unless~~ either oil and gas tax collections for a biennium decrease  
17 by at least twenty-five percent from the previous biennium or the earnings of the legacy fund for  
18 a biennium exceed thirty-three percent of the oil and gas tax collections for the same biennium.  
19 For purposes of this section, "oil and gas tax collections" means total revenue derived from  
20 taxes on oil and gas production or extraction pursuant to chapters 57-51, 57-51.1, and 57-51.2,  
21 excluding the amounts allocated to the Three Affiliated Tribes.

22     **SECTION 4. REPEAL.** Section 21-10-12 of the North Dakota Century Code is repealed.

15.0057.03002  
Title.

Prepared by the Legislative Council staff for Representative Delzer  
January 19, 2015

Attachment 2

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1033

Page 1, line 16, replace "2017" with "2015"

Page 2, line 11, remove "- Intent"

Page 2, line 14, remove ". It is the intent"

Page 2, remove line 15

Page 2, line 16, replace "of the principal of the fund until" with "unless"

Renumber accordingly

## HOUSE BILL NO. 1033 - DEFINITIONS FOR THE LEGACY FUND #1

This memorandum provides an overview of the definitions provided for the legacy fund in 2013 House Bill No. 1033. The following is a list of definitions included in Section 1 of the bill and the purpose of each definition.

Definition	Purpose
"At the end of each biennium" means after cancellation of unexpended appropriations pursuant to section 54-44.1-11.	Clarifies that the transfer of earnings from the legacy fund to the general fund at the end of a biennium is made after any appropriations of earnings made by the Legislative Assembly for that biennium are canceled.
"Earnings" means net income in accordance with generally accepted accounting principles, excluding any unrealized gains or losses.	Prevents unrealized gains from being considered earnings available to be appropriated as transferred. The definition was originally enacted by the 2013 Legislative Assembly and codified as Section 21-10-12. House Bill No. 1033 moves the definition to Chapter 54-27 to be located with the other proposed legacy fund definitions and repeals Section 21-10-12.
"Principal" means thirty percent of total revenue derived from taxes on oil and gas production and extraction deposited in the legacy fund, earnings of the fund accruing prior to July 1, 2017, and any funds transferred by the legislative assembly into the fund from any source.	Clarifies that any fund earnings accruing prior to July 1, 2017, are considered principal of the fund. For consistency, the definition also includes the constitutional provisions 30 percent of total revenue derived from oil and gas production and extraction and transfers made into the fund are considered to be fund principal.
"Total revenue derived from taxes on oil and gas production or extraction" means taxes collected from oil and gas production or extraction pursuant to chapters 57-51, 57-51.1, and 57-51.2, excluding the amounts allocated to the Three Affiliated Tribes.	Clarifies that oil and gas production and oil extraction taxes allocated to the Three Affiliated Tribes are not subject to legacy fund deposit requirements. This definition is consistent with current Tax Department allocations.

In addition to the definitions in Section 1 of the bill, Section 2 of the bill clarifies the process of determining how much principal funding is available to be expended by the Legislative Assembly during each biennium. The section provides for the Office of Management and Budget to determine by December 1<sup>st</sup> of each even-numbered year, and at other times as requested by the Legislative Management, the amount equal to 15 percent of fund principal which may be expended during a biennium.

# ANALYSIS OF THE LEGACY FUND FISCAL YEAR 2013-15 AND 2015-17 BIENNIUMS (INCLUDING PROPOSED CHANGES AS OF JANUARY 27, 2015)

	2013-15 Biennium		2015-17 Biennium	
Beginning balance		\$1,280,714,486		\$3,341,414,486
Add estimated revenues				
30 percent of oil and gas gross production and extraction tax collections <sup>1</sup>	\$1,665,930,000		\$1,186,250,000	
Transfer of oil and gas tax revenues from the strategic investment and improvements fund <sup>2</sup>	240,370,000		119,150,000	
Transfer of other revenue sources from the strategic investment and improvements fund <sup>3</sup>	30,400,000		13,000,000	
Investment earnings <sup>4</sup>	124,000,000		124,000,000	
Total estimated revenues		2,060,700,000		1,442,400,000
Total available		\$3,341,414,486		\$4,783,814,486
Total estimated expenditures and transfers <sup>5</sup>		0		0
Estimated ending balance		\$3,341,414,486		\$4,783,814,486

<sup>1</sup>Estimated revenues - These amounts reflect actual oil tax revenue collections deposited in the fund through December 2014 and estimated allocations for the remainder of the 2013-15 biennium and estimated oil tax revenue allocations for the 2015-17 biennium based on the January 2015 revised revenue forecast. These amounts do not reflect any transfers from the strategic investment and improvements fund. The transfer amounts are shown separately on the schedule.

<sup>2</sup>Pursuant to North Dakota Century Code Section 15-08.1-08, if the unobligated balance of the strategic investment and improvements fund exceeds \$300 million at the end of any month, 25 percent of any revenues received for deposit in the strategic investment and improvements fund in the subsequent month must be deposited instead into the legacy fund. These amounts do not reflect additional transfers from the strategic investment and improvements fund from revenue sources other than oil and gas tax revenue.

<sup>3</sup>These amounts reflect transfers to the legacy fund from the strategic investment and improvements fund from revenue sources other than oil and gas tax revenue, pursuant to Section 15-08.1-08.

<sup>4</sup>These amounts reflect investment earnings estimated by the Retirement and Investment Office.

<sup>5</sup>The principal and earnings of the legacy fund may not be spent until after June 30, 2017.

## NOTE

The following bill under consideration by the Legislative Assembly may have a significant effect on the legacy fund:

- House Bill No. 1377 amends Section 15-08.1-08 to eliminate the transfer of 25 percent of any revenues from the strategic investment and improvements fund to the legacy fund, if the unobligated balance of the strategic investment and improvements fund exceeds \$300 million at the end of any month.

## FUND HISTORY

The legacy fund was created in 2010 when the voters of North Dakota approved a constitutional amendment—now Article X, Section 26, of the Constitution of North Dakota—to provide 30 percent of oil and gas gross production and oil extraction taxes on oil and gas produced after June 30, 2011, be transferred to the legacy fund. The principal and earnings of the legacy fund may not be spent until after June 30, 2017, and any expenditure of principal after that date requires a vote of at least two-thirds of the members elected to each house of the Legislative Assembly. Not more than 15 percent of the principal of the legacy fund may be spent during a biennium. The Legislative Assembly may transfer funds from any source to the legacy fund, and such transfers become part of the principal of the fund. The State Investment Board is responsible for investment of the principal of the legacy fund. Interest earnings accruing after June 30, 2017, are transferred to the general fund at the end of each biennium.



HB 1033  
3-13-15  
#2

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1033

Page 1, line 3, replace "repeal section" with "amend and reenact sections 21-10-11 and"

Page 1, line 4, replace "a definition of" with "investment of the"

Page 1, line 4, remove "earnings"

Page 1, after line 5, insert:

**"SECTION 1. AMENDMENT.** Section 21-10-11 of the North Dakota Century Code is amended and reenacted as follows:

**21-10-11. Legacy and budget stabilization fund advisory board.**

The legacy and budget stabilization fund advisory board is created to develop recommendations for the investment of funds in the legacy fund and the budget stabilization fund to present to the state investment board. The goal of investment for the legacy fund is principal preservation while maximizing total return and utilizing local financial institutions. The board consists of two members of the senate appointed by the senate majority leader, two members of the house of representatives appointed by the house majority leader, the director of the office of management and budget or designee, the president of the Bank of North Dakota or designee, and the tax commissioner or designee. The board shall select a chairman and must meet at the call of the chairman. The board shall report at least semiannually to the budget section. Legislative members are entitled to receive compensation and expense reimbursement as provided under section 54-03-20 and reimbursement for mileage as provided by law for state officers. The legislative council shall pay the compensation and expense reimbursement for the legislative members. The legislative council shall provide staff services to the legacy and budget stabilization fund advisory board. The staff and consultants of the state retirement and investment office shall advise the board in developing asset allocation and investment policies.

**SECTION 2. AMENDMENT.** Section 21-10-12 of the North Dakota Century Code is amended and reenacted as follows:

**21-10-12. Legacy fund - ~~Earnings defined~~Investment.**

~~For the purposes of section 26 of article X of the Constitution of North Dakota, the term "earnings" means net income in accordance with generally accepted accounting principles, excluding any unrealized gains or losses. Notwithstanding section 21-10-07, the state investment board shall place at least ten percent of the legacy fund with one or more financial institutions chartered in and located in this state and which are experienced in and hold considerable knowledge of the field of investments.~~

Page 2, remove line 22

Renumber accordingly

HOUSE BILL 1033

North Dakota Retirement and Investment Office ("RIO")  
Testimony to the Senate Appropriations Committee  
David Hunter, Executive Director/CIO

March 17, 2015

I am here to provide clarifying testimony relating to a Proposed Amendment to House Bill No. 1033 which recommends that "the state investment board shall place at least 10% of the legacy fund with one or more financial institutions chartered in and located in this state and which are experienced in and hold considerable knowledge of the field of investments". **This proposed amendment is inconsistent with North Dakota Century Code ("NDCC") which states the SIB shall apply the prudent investor rule in investing for funds under its supervision.**

*The "prudent investor rule" means that in making investments the fiduciaries shall exercise the judgment and care, under the circumstances then prevailing, that an institutional investor of ordinary prudence, discretion, and intelligence exercises in the management of large investments entrusted to it, not in regard to speculation but in regard to the permanent disposition of funds, considering probable safety of capital as well as probable income.*

**It is important to note that the current governance structure which includes the "prudent investor rule" has combined with SIB's investment manager selection ability to generate approximately 1% of excess return since the inception of the Legacy Fund.**

**The attached presentation provides: 1) an overview of the SIB investment process; 2) a summary of client assets under management; and 3) the investment results experienced by the Legacy Fund over the past three years.**

I sincerely thank the Committee for allowing me the opportunity to provide clarifying testimony and would be happy to address any questions at this time.

HB 1033  
3-17-15  
#1

# State Investment Board and Legacy Fund Investment Overview

**Senate Appropriations Committee**

March 17, 2015

Dave Hunter, Executive Director / CIO  
ND Retirement & Investment Office (RIO)  
State Investment Board (SIB)

418 1033  
3-17-15  
#2

# Presentation Agenda

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## ▷ **State Investment Board**

- ▷ Client Assets Under Management
- ▷ Investment Process Overview
- ▷ Client, Board and RIO Responsibilities
- ▷ Manager, Custodian and Consultant Responsibilities

## ▷ **Legacy Fund**

- ▷ Asset Allocation
- ▷ Interim Investment Update
- ▷ Implementation of Strategic Allocation (Callan Associates)
- ▷ Investment Manager Allocations



# State Investment Board – Client Assets Under Management

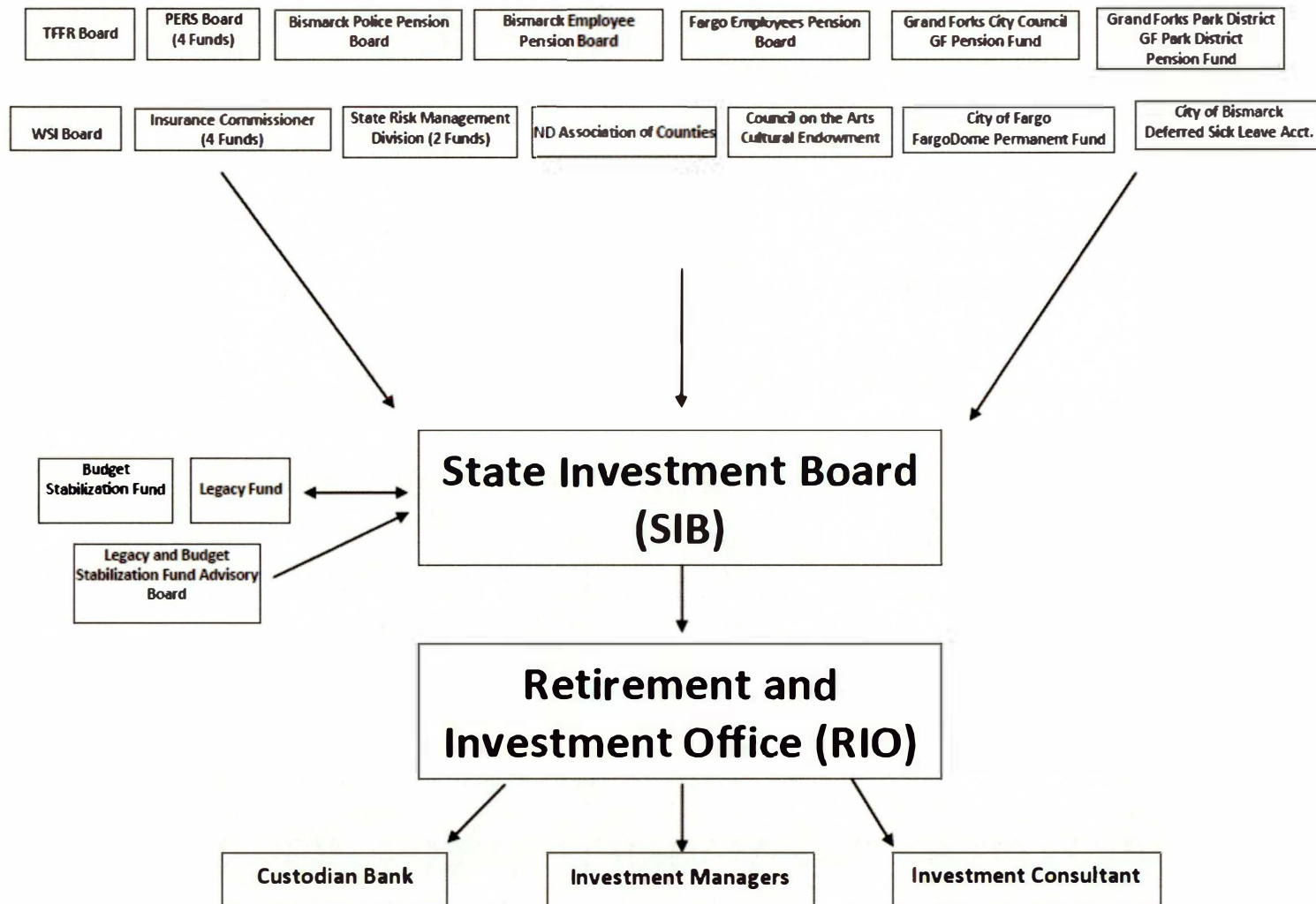
<b>Fund Name</b>	<b>Market Values as of 12/31/14 <sup>(1)</sup></b>	<b>Market Values as of 6/30/14 <sup>(2)</sup></b>	<b>Market Values as of 12/31/13 <sup>(1)</sup></b>
<b>Pension Trust Fund</b>			
Public Employees Retirement System (PERS)	2,345,979,927	2,332,744,037	2,204,819,633
Teachers' Fund for Retirement (TFFR)	2,046,439,456	2,061,684,912	1,970,377,031
Job Service of North Dakota Pension	96,920,165	97,825,769	95,276,201
City of Bismarck Employees Pension	79,421,743	78,804,326	74,832,971
City of Grand Forks Employees Pension	56,347,332	57,896,611	53,459,799
City of Bismarck Police Pension	34,834,996	34,643,204	32,887,889
Grand Forks Park District	5,893,072	5,938,993	5,653,023
City of Fargo Employees Pension	9,656	9,702	4,742,525
<b>Subtotal Pension Trust Fund</b>	<b>4,665,846,347</b>	<b>4,669,547,555</b>	<b>4,442,049,072</b>
<b>Insurance Trust Fund</b>			
Legacy Fund	2,900,880,837	2,215,941,142	1,695,950,111
Workforce Safety & Insurance (WSI)	1,710,647,794	1,703,987,980	1,627,545,930
Budget Stabilization Fund	589,598,047	586,199,881	588,744,084
PERS Group Insurance Account	42,705,101	37,425,567	39,626,348
City of Fargo FargoDome Permanent Fund	40,651,973	41,775,992	38,668,924
State Fire and Tornado Fund	25,065,765	29,223,707	28,625,262
Petroleum Tank Release Compensation Fund	7,152,822	7,092,998	6,899,622
State Risk Management Fund	6,771,080	6,948,162	6,593,046
State Risk Management Workers Comp Fund	6,141,008	5,965,322	5,654,121
ND Association of Counties (NDACO) Fund	3,481,321	3,445,373	2,894,408
State Bonding Fund	3,299,303	3,268,991	3,171,622
ND Board of Medical Examiners	2,131,999	1,889,897	
Bismarck Deferred Sick Leave Account	859,648	849,818	807,624
Insurance Regulatory Trust Fund	646,335	1,146,038	1,107,837
Cultural Endowment Fund	373,276	364,979	359,577
<b>Subtotal Insurance Trust Fund</b>	<b>5,340,406,309</b>	<b>4,645,525,847</b>	<b>4,046,648,516</b>
PERS Retiree Insurance Credit Fund	93,282,939	90,360,366	83,492,581
<b>Total Assets Under SIB Management</b>	<b>10,099,535,595</b>	<b>9,405,433,768</b>	<b>8,572,190,169</b>

<sup>(1)</sup> 12/31/14 and 12/31/13 market values are unaudited and subject to change.

<sup>(2)</sup> 6/30/14 market values as stated in the Comprehensive Annual Financial Report.

- ▶ SIB Client Assets Under Management grew by approximately 18.5% or \$1.53 billion in the last year.
- ▶ The Pension Trust posted a net return of approximately 6%, while the Insurance Trust generated a 5.1% net return in the last year. Investments were responsible for gains of \$265 million for the Pension Trust and \$204 million for the Insurance Trust.
- ▶ Legacy assets increased by 71% (or \$1.2 billion) primarily due to tax collections, while net returns were 4.2% for the year ended December 31, 2014.
- ▶ SIB client assets approximated \$10.1 billion based on preliminary valuations as of December 31, 2014.

# SIB Investment Process Overview



# SIB Client, Board and RIO Responsibilities

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**Client Responsibilities:** (Per NDCC 21-10-02.1) The governing body of each fund shall establish policies on investment goals, objectives and asset allocation that must include:

- Acceptable rates of return, liquidity and levels of risk
- Long-range asset allocation goals

**State Investment Board Responsibilities:** (Per NDCC 21-10):

- Implement client asset allocations
- Apply **Prudent Investor Rule** when investing for fund under its supervision
- Approve general types of securities for investment
- Set policies and procedures regulating securities transactions on behalf of clients
- Select custodian servicer
- Select investment director and/or investment consulting service
- **Approve investment manager recommendations** of investment director and consultant

**Retirement and Investment Office Staff Responsibilities (on behalf of SIB):**

- Administer overall investment strategy
- Advise SIB on ways to maximize risk/return opportunities within each asset class
- Act as liaison between SIB and managers, consultant and custodian
- Monitor individual clients' investment guidelines and asset allocations
- Maintain separate accounting for client accounts

# Manager, Custodian and Consultant Responsibilities

---

## **Investment Manager Responsibilities:**

- Implement specific mandates or “investment missions”
- Make buy/sell decisions based on investment guidelines
- Report to RIO Staff on regular basis
- Provide education to SIB

## **Custodian Bank Responsibilities:**

- Safe-keep assets
- Settle trades
- Record-keeper

## **Investment Consultant Responsibilities:**

- Performance measurement of investment managers
- Manager search assistance
- Provide education to SIB
- Special projects



# Legacy Fund Asset Allocation

	12/31/14 Market Value	Actual Weight	Interim Policy Weight
TOTAL LEGACY FUND	2,900,880,837	100.0%	100.0%
LARGE CAP DOMESTIC EQUITY	640,354,913	22.1%	22.1%
SMALL CAP DOMESTIC EQUITY	238,534,459	8.2%	8.2%
INTERNATIONAL EQUITY	566,879,673	19.5%	19.5%
FIXED INCOME	1,009,803,904	34.8%	34.8%
DIVERSIFIED REAL ASSETS	211,717,138	7.3%	7.3%
REAL ESTATE	145,500,467	5.0%	5.0%
CASH EQUIVALENTS	11,440,987	0.4%	0.0%
SHORT TERM FIXED INCOME	76,649,295	2.6%	3.0%

NOTE: Monthly market values are preliminary and subject to change.

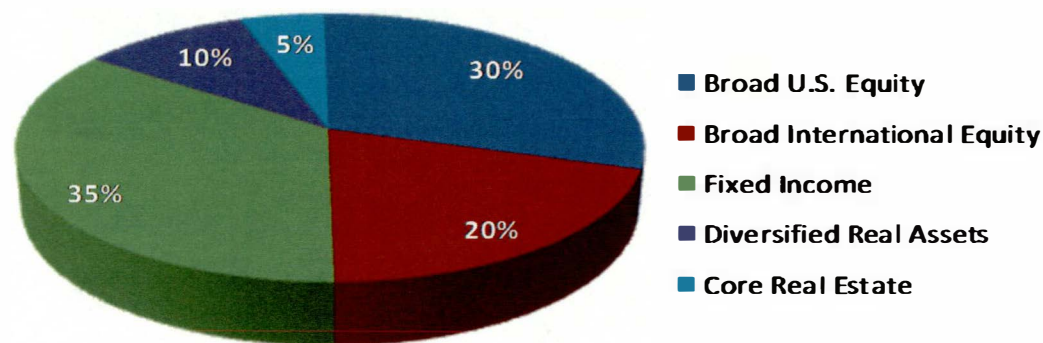
**Equity Target = 50%**  
(Large Cap of 22.1% +  
Small Cap of 8.2% +  
International of 19.5%)

**Fixed Income = 35%**  
(34.8% per left)

**Real Assets = 15%**  
(Diversified of 7.3% +  
Real Estate of 5.0% +  
Short Term Fixed of 2.6%)  
noting that Short-Term  
Fixed will be converted into  
Real Assets during 2015.

# Legacy Fund – Interim Investment Update

## Policy Allocation



Transition completion  
January 2015

	1 Yr Ended 12/31/2014	3 Yrs Ended 12/31/2014
<b>Total Fund Return - Net</b>	4.2%	3.0%
<b>Policy Benchmark Return</b>	3.6%	2.0%
<b>Excess Return</b>	0.6%	1.0%

## LEGACY FUND

Total Fund Return - Net	4.2%	3.0%
Policy Benchmark Return	3.6%	2.0%
<b>Excess Return</b>	<b>0.6%</b>	<b>1.0%</b>

Note: Amounts are preliminary, unaudited and subject to change.

## Key Overall Observations:

- Asset allocation is the primary driver of investment returns.
- The Legacy Fund transitioned from a 100% short-term fixed income allocation to a 50% equity, 35% fixed income and 15% diversified real asset allocation in the last 18 months.
- The Legacy Fund generated a net return of 4.2% and 3.0% for the 1- and 3-year periods ended 12/31/14, respectively.
- Active management was primarily responsible for generating **0.6%** of “**Excess Return**” (over passive benchmark indices) in 2014.

# Legacy Fund: The Implementation of Strategic Allocation

As of December 31, 2014

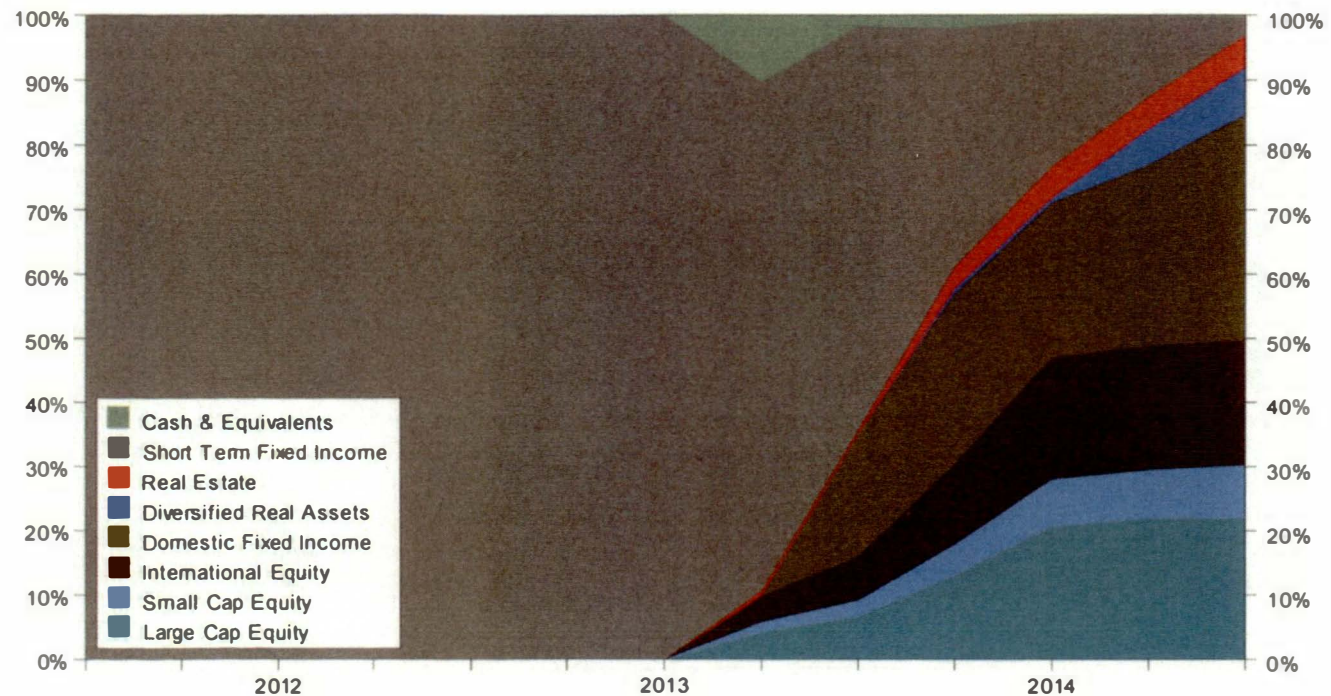
Actual Historical Asset Allocation

## Annualized Return

Three years as of  
December 31, 2014

Fund: 3.13%

Target: 2.16%



- The Legacy Fund's asset allocation policy has been implemented in a prudent, orderly manner.
- The three-year returns are better than benchmark, due chiefly to the short term bond results.



# Legacy Fund - Investment Manager Allocations

	Style	12/31/14		Style	12/31/14
<b>Large Cap Domestic Equity Pool</b>			<b>Fixed Income Pool</b>		
Los Angeles Capital Management	Lg Cap Growth	191,045,943	Western Asset Management	Core	327,529,166
LSV Asset Management	Lg Cap Value	193,231,379	Prudential	Core Plus	81,921,935
Los Angeles Capital Management	Enhanced Russell 1000	128,032,469	Declaration Management & Research	Mortgage Backed	77,893,283
The Clifton Group	Enhanced S&P 500	128,045,122	State Street	Government/Credit	143,035,239
<b>Total Large Cap Domestic Equity Pool</b>		640,354,913	Wells Capital Management	Baa Average Quality	327,940,491
<b>Small Cap Domestic Equity Pool</b>			PIMCO	Distressed Sr. Debt	51,483,790
Research Affiliates	Small Cap Value	70,004,841	<b>Total Fixed Income Pool</b>		1,009,803,904
The Clifton Group	Enhanced Russell 2000	168,529,618	<b>Short Term Fixed Income Pool</b>		
<b>Total Small Cap Domestic Equity Pool</b>		238,534,459	Babson Capital - Legacy	US Gov't & Credit (1-3 yrs.)	43,642,546
<b>International Equity Pool</b>			JP Morgan - Legacy	US Gov't & Credit (1-3 yrs.)	33,006,749
Capital Group	Intl Quality Growth	227,657,125	<b>Total Short Term Fixed Pool</b>		76,649,295
LSV Asset Management	Intl Value	225,288,693	<b>Real Assets Pool</b>		
Dimensional Fund Advisors (DFA)	Intl Small Cap Value	56,897,869	Western Asset Management	Global TIPS	211,717,138
Vanguard	Intl Small Cap Growth	57,035,986	JP Morgan	Real Estate	78,672,478
<b>Total International Equity Pool</b>		566,879,673	Invesco	Real Estate	66,827,989
			<b>Total Real Assets Pool</b>		357,217,605
			<b>Cash Equivalents Pool</b>		
			Northern Trust	Enhanced Money Marke	11,440,987
			<b>Total Cash Equivalents Pool</b>		11,440,987
			<b>Total Insurance Trust</b>		2,900,880,837

Note: All amounts are deemed to be materially accurate, but are unaudited and subject to change.