

## STUDY OF THE FOUNDATION AID STABILIZATION FUND - BACKGROUND MEMORANDUM

### STUDY OVERVIEW

Section 40 of 2013 House Bill No. 1015 ([Appendix A](#)) provides for a study of the foundation aid stabilization fund including:

- Anticipated growth in the fund;
- Appropriate funding levels;
- Options for the disposition of excess funding if appropriate funding levels are exceeded;
- The reallocation of oil extraction taxes currently being deposited in the fund; and
- The feasibility and desirability of proposing changes to the constitution relating to the fund.

The responsibility for this study was assigned to the Government Finance Committee.

### FUND HISTORY

The foundation aid stabilization fund was created in 1994 when the voters of North Dakota approved a constitutional amendment, now Article X, Section 24, of the Constitution of North Dakota ([Appendix B](#)), to provide that 20 percent of oil extraction tax revenue be allocated as follows:

- 50 percent (of the 20 percent) to the common schools trust fund.
- 50 percent (of the 20 percent) to the foundation aid stabilization fund.

The principal of the foundation aid stabilization fund may only be spent upon order of the Governor to offset foundation aid reductions made by executive action due to a revenue shortfall. North Dakota Century Code Section 54-44.1-12 ([Appendix C](#)) provides the Director of the Budget may order an allotment to control the rate of expenditures of state agencies. This section provides an allotment must be made by specific fund and all departments and agencies that receive money from a fund must be allotted on a uniform percentage basis, except that appropriations for foundation aid, transportation aid, and special education aid may only be allotted to the extent the allotment can be offset by transfers from the foundation aid stabilization fund. One budget allotment has occurred since the foundation aid stabilization fund was created in 1994. During the 2001-03 biennium, funding of \$5,500,639 was transferred to the Department of Public Instruction to offset a reduction in state school aid and special education payments resulting from a 1.05 percent budget allotment ordered by Governor John Hoeven in July 2002.

Article X, Section 24, of the Constitution of North Dakota, provides the interest income of the foundation aid stabilization fund must be transferred to the general fund on July 1 of each year. However, the State Treasurer's office allocates the interest income to the general fund on a monthly basis. During the 2009-11 biennium, \$511,593 of interest from the foundation aid stabilization fund was allocated to the general fund. For the period July 1, 2011, through May 31, 2013, \$368,799 of interest from the foundation aid stabilization fund has been allocated to the general fund.

### FUND ANALYSIS FOR THE 2011-13 AND 2013-15 BIENNIUMS

The schedule below provides an analysis of estimated revenues and expenditures of the foundation aid stabilization fund for the 2011-13 and 2013-15 bienniums.

	2011-13 Biennium		2013-15 Biennium	
Beginning balance		\$140,193,764		\$333,300,116
Add estimated revenues				
Oil extraction tax allocations	\$193,106,352 <sup>1</sup>		\$282,136,675 <sup>1</sup>	
Total available		333,300,116		615,436,791
Less estimated expenditures and transfers				
Transfer to foundation aid program	\$0 <sup>2</sup>		\$0 <sup>2</sup>	
Estimated ending balance		\$333,300,116		\$615,436,791

<sup>1</sup>Estimated revenues - Based on actual oil extraction tax collections transferred to the fund through April 2013 and estimated allocations for the remainder of the 2011-13 and 2013-15 bienniums per the February 2013 revised revenue forecast. The 2013-15 biennium amount includes an increase of \$8,660,000 of oil extraction tax allocations due to the estimated effect of 2013 House Bill No. 1198 which changes the eligibility for stripper well tax incentives.

<sup>2</sup>Estimated expenditures - As provided in Article X, Section 24, of the Constitution of North Dakota, the principal of the foundation aid stabilization fund can only be used to offset foundation aid reductions made by executive action due to a revenue shortfall. No foundation aid reductions as a result of a revenue shortfall are currently anticipated in the 2011-13 or 2013-15 biennium.

### HISTORICAL FUND BALANCES COMPARED TO TOTAL FOUNDATION AID OR STATE AID TO SCHOOLS

The schedule below compares the foundation aid stabilization fund balance at the end of each biennium since 1999 to the total funding for foundation aid or state aid to schools appropriated each biennium.

	Foundation Aid Stabilization Fund Balance at the End of the Biennium	Total Foundation Aid or State Aid to Schools Appropriated for the Biennium <sup>1</sup>	Foundation Aid Stabilization Fund Balance at the End of the Biennium as a Percentage of the Total Foundation or State Aid Appropriated for the Biennium
1999-2001	\$10,517,143	\$585,734,476	1.80%
2001-03	\$8,991,303	\$628,345,368	1.43%
2003-05	\$16,098,385	\$665,628,056	2.42%
2005-07	\$29,009,838	\$698,565,879	4.15%
2007-09	\$65,750,547	\$780,765,879	8.42%
2009-11	\$140,193,764	\$1,274,254,480 <sup>2</sup>	11.00%
2011-13 estimated	\$333,300,116	\$1,350,992,316 <sup>3</sup>	24.67%
2013-15 estimated	\$615,436,791	\$1,835,700,000 <sup>4</sup>	33.53%

<sup>1</sup>Total foundation aid appropriated from the general fund and state tuition fund.

<sup>2</sup>The Legislative Assembly provided, as part of state school aid, \$295 million from the general fund for mill levy reduction grants to school districts. In addition to funding from the general fund and the state tuition fund, the 2009 Legislative Assembly provided, as state school aid, \$85.6 million from federal funds available through the American Recovery and Reinvestment Act of 2009.

<sup>3</sup>The Legislative Assembly provided, as part of state school aid, \$341.8 million from the general fund for mill levy reduction grants to school districts and \$5 million from the oil and gas impact grant fund for rapid enrollment growth grants.

<sup>4</sup>The Legislative Assembly provided integrated formula payments totaling \$1.75 billion that includes \$656.5 million for the property tax relief component. The Legislative Assembly also provided \$13.6 million for rapid enrollment growth grants.

### BUDGET STABILIZATION FUND

The budget stabilization fund was established in 1987 and contains funds that may be used to offset a revenue shortfall. Any amount in the state general fund in excess of \$65 million at the end of the biennium must be transferred to the budget stabilization fund. However, the maximum balance of the fund is limited to 9.5 percent of the general fund budget as approved by the most recently adjourned Legislative Assembly. Based on general fund appropriations made during the 2013 regular legislative session, the maximum fund balance is currently \$583.5 million.

The Governor may order a transfer from the budget stabilization fund to the general fund if the Director of the Office of Management and Budget (OMB) projects general fund revenues for the biennium will be at least 2.5 percent less than estimated by the most recently adjourned Legislative Assembly. The amount transferred is limited to the difference between an amount 2.5 percent less than the original legislative general fund revenue forecast and the revised forecast prepared by OMB.

### Use of Budget Stabilization Fund for Foundation Aid Payments

In the event the Governor orders a budget allotment, funding from the foundation aid stabilization fund is to be used to offset the budget allotment for foundation aid, transportation aid, and special education aid payments to schools. If the projected revenue shortfall is 2.5 percent or less, the foundation aid stabilization fund is to be used to offset the entire allotment. If the projected revenue shortfall is 2.5 percent or greater, it appears that any allotment of school aid payments in excess of 2.5 percent may be offset by either a transfer from the foundation aid stabilization fund or the budget stabilization fund. The determination of which funding source to use for allotments in excess of 2.5 percent would be made by the Governor, who has the authority to order transfers from either fund subject to constitutional and statutory provisions. Attached as [Appendix D](#) is a copy of a letter from the Legislative Council regarding the use of funds from the foundation aid stabilization fund and the budget stabilization fund.

## RELATED LEGISLATION DURING THE 2013 LEGISLATIVE SESSION

### House Concurrent Resolution No. 3003

House Concurrent Resolution No. 3003, as introduced ([Appendix E](#)), would have submitted a constitutional amendment to the voters to limit the balance of the foundation aid stabilization fund to \$150 million. Any excess funds would have been transferred to a public employees retirement stabilization fund, and no additional funds would be allowed to be deposited in the foundation aid stabilization fund until the fund balance fell below \$100 million. Once the balance was below \$100 million, the foundation aid stabilization fund would again receive deposits and retain interest income until the fund balance reached \$150 million. If the balance of the public employees retirement stabilization fund exceeded \$450 million, any excess revenue would have been transferred to the state general fund to provide state aid to elementary and secondary education.

The resolution was amended by the House Judiciary Committee to reduce the amount of oil extraction taxes deposited in the foundation aid stabilization fund from 50 percent (of 20 percent of total tax collections) to 20 percent (of 20 percent of total tax collections). The remaining 30 percent (of 20 percent of total tax collections) would have been allocated to a state retirement stabilization fund for the purpose of addressing unfunded retirement benefit obligations of state retirement plans. The amendments also removed the language regarding the maximum fund balance of the foundation aid stabilization fund and the public employees retirement stabilization fund. The resolution, as amended ([Appendix F](#)), passed in the House but failed in the Senate.

### House Concurrent Resolution No. 3040

House Concurrent Resolution No. 3040, as introduced ([Appendix G](#)), would have submitted a constitutional amendment to the voters to limit the maximum balance of the foundation aid stabilization fund. Once the fund reached \$100 million, the maximum fund balance would not have been allowed to increase by more than 2 percent per year. Any excess revenues would have been deposited in the common schools trust fund. The resolution also allowed fund income to be expended for school aid in the event of a revenue shortfall, and any income not expended would have been transferred to the general fund.

The resolution was amended by the House Judiciary Committee to limit the balance of the foundation aid stabilization fund to an amount equal to 20 percent of the "grants - state school aid" line item in the prior biennium's appropriation bill for the Department of Public Instruction. Once the maximum fund level was reached, any excess revenue would have been deposited in the common schools trust fund. The resolution also would have allowed fund income to be used to meet benefit obligations of the state retirement plan. The resolution failed to pass the House. A copy of the engrossed resolution is attached as [Appendix H](#).

### Senate Concurrent Resolution No. 4010

Senate Concurrent Resolution No. 4010, as introduced ([Appendix I](#)), would have submitted a constitutional amendment to the voters regarding the foundation aid stabilization fund. The resolution would have limited the balance of the fund to \$300 million, except beginning July 1, 2017, the maximum fund balance would be adjusted biennially based on the rate of inflation. Any excess revenue would have been required to be transferred to another constitutional fund or appropriated for the support of elementary and secondary education in the state.

The resolution was amended by the Senate Education Committee to limit the balance of the fund to an amount equal to 20 percent of the "grants - state school aid" line item in the prior biennium's appropriation bill for the Department of Public Instruction. Once the maximum fund balance was reached, any excess revenue would have been required to be transferred to another constitutional fund or appropriated for the support of elementary and secondary education in the state. A copy of the Senate version of the resolution is attached as [Appendix J](#).

The resolution was amended by the House Judiciary Committee to limit the amount of oil extraction taxes deposited in the fund from 50 percent (of 20 percent of total tax collections) to 20 percent (of 20 percent of total tax collections). The remaining 30 percent (of 20 percent of total tax collections) would have been allocated to a state retirement stabilization fund for the purpose of addressing unfunded retirement benefit obligations of state retirement plans. The House version also would have limited the maximum balance of the foundation aid stabilization fund to an amount equal to 150 percent of the principal amount in the fund on July 1, 2014. Once the maximum fund balance was reached, any excess revenues would have been used as determined by the Legislative Assembly through the enactment of laws. A copy of the House version of the resolution is attached as [Appendix K](#).

The resolution passed the House and Senate in different forms and a conference committee was appointed for the resolution. However, the conference committee version of the resolution was defeated in the Senate.

## STUDY PLAN

The following is a proposed study plan for the committee's consideration in its study of the foundation aid stabilization fund:

1. Receive and review information from the Legislative Council regarding the history and purpose of the fund.
2. Review constitutional and statutory provisions relating to the fund.
3. Receive information from the Legislative Council regarding the sources of revenue deposited in the fund, estimated future fund deposits and earnings, and estimated fund balances.
4. Review previous expenditures from the fund due to budget allotments.
5. Review the feasibility and desirability of establishing a maximum fund balance, including what an appropriate maximum fund balance would be.
6. Review options for the reallocation of revenues deposited in the fund if a maximum fund balance is reached.
7. Receive testimony from interested persons regarding the study.
8. Develop recommendations and any bill drafts necessary to implement the recommendations.
9. Prepare a final report for submission to the Legislative Management.

ATTACH:11