

NORTH DAKOTA LEGISLATIVE MANAGEMENT

Minutes of the

LEGACY AND BUDGET STABILIZATION FUND ADVISORY BOARD

Tuesday, November 28, 2017
Harvest Room, State Capitol
Bismarck, North Dakota

Representative Keith Kempenich, Chairman, called the meeting to order at 1:10 p.m.

Members present: Representatives Keith Kempenich, Gary Kreidt; Senators Jim Dotzenrod, Jerry Klein; Citizen Members Eric Hardmeyer, Joe Morrisette, Pam Sharp

Others present: Representative Jeff Delzer, Underwood
See [Appendix A](#) for additional persons present.

It was moved by Senator Klein, seconded by Representative Kreidt, and carried on a voice vote that the minutes of the June 19, 2017, meeting be approved as distributed.

OIL AND GAS TAX REVENUE UPDATE

At the request of Chairman Kempenich, the Legislative Council staff presented a memorandum entitled [Oil and Gas Tax Revenues Monthly Update](#) regarding an update on oil production and prices, oil and gas tax revenue collections, and oil and gas tax revenue allocations for October 2017 and for the biennium to date.

STATUS OF THE BUDGET STABILIZATION FUND

At the request of Chairman Kempenich, Mr. David J. Hunter, Executive Director and Chief Investment Officer, Retirement and Investment Office, presented information ([Appendix B](#)) regarding the status of the budget stabilization fund, including investment performance, the fund balance, and the investment policy statement. He said the budget stabilization fund had a net return of 0.76 percent compared to a policy benchmark return of 0.69 percent for the 1-year period ended September 30, 2017. He said the fund had a net return of 1.56 percent compared to a policy benchmark return of 0.73 percent for the 5-year period ended September 30, 2017. He said the market value of the fund was \$38.5 million on September 30, 2017, which reflects investment earnings retained in the fund after the transfer of \$572.5 million to the general fund in fiscal year 2017 and a transfer of funds from the general fund in excess of \$65 million at the end of the 2015-17 biennium. He said the asset allocation of the budget stabilization fund is 100 percent short-term fixed income and cash. He suggested the committee amend the budget stabilization fund investment policy statement to acknowledge the transfer from the budget stabilization fund to the general fund.

In response to a question from Senator Dotzenrod, Ms. Sharp said any revenue in excess of \$65 million in the general fund at the end of a biennium is transferred to the budget stabilization fund. In addition, she said, the 2017 Legislative Assembly provided that up to \$75 million of oil and gas tax revenue, if available, will be transferred to the budget stabilization fund.

It was moved by Representative Kreidt, seconded by Mr. Hardmeyer, and carried on a roll call vote that the advisory board recommends the investment policy statement for the budget stabilization fund be amended to reference the transfer from the budget stabilization fund to the general fund and the statutory fund balance maximum for the fund for the 2017-19 biennium. Representatives Kempenich and Kreidt, Senators Dotzenrod and Klein and Citizen Members Hardmeyer, Morrisette, and Sharp voted "aye." No negative votes were cast.

STATUS OF THE LEGACY FUND

At the request of Chairman Kempenich, Mr. Hunter presented information ([Appendix C](#)) regarding the status of the legacy fund, including investment performance, the fund balance, and investment management fees. He said the legacy fund had an overall net return of 3.64 percent compared to a policy benchmark return of 3.14 percent for the fiscal year to date through September 30, 2017. He said net earnings for the fiscal year to date through September 30, 2017, totaled \$172.2 million, including \$52.4 million of realized earnings pursuant to the definition of earnings in North Dakota Century Code Section 21-10-12, and \$119.8 million of unrealized gains. He said the market value of the fund was \$4.96 billion on September 30, 2017. He said the actual asset allocations of the

legacy fund are within 1 to 2 percent of the target allocations reflecting the investment policy benchmark of 50 percent equity investments, 35 percent fixed income, and 15 percent real assets. He said investment management fees for the legacy fund totaled \$14 million in fiscal year 2017, or 0.32 percent of the average market value of the fund's assets. He said the Legislative Assembly, in Section 11 of 2017 House Bill No. 1015, estimates \$200 million of earnings will be transferred from the legacy fund to the general fund at the end of the 2017-19 biennium. He said the Retirement and Investment Office suggests contracting with Callan Associates to conduct an asset allocation and spending study for the legacy fund in fiscal year 2018. He said the estimated study cost is \$65,000 and the expected completion date is June 2018. He said the study will include the impact of increasing fixed asset investments at the Bank of North Dakota allowing the Bank to provide infrastructure loans to political subdivisions in the state.

In response to a question from Senator Dotzenrod, Ms. Sharp said because the Retirement and Investment Office will not know the actual amount until after the biennium closes, the Office of Management and Budget will use information available to estimate the investment earnings and provide for the transfer of an estimated earnings amount before the 2017-19 biennium closes at the end of July 2019. Mr. Hunter said as of September 30, 2017, earnings of the legacy fund eligible for transfer to the general fund at the end of the 2017-19 biennium is \$52.4 million.

In response to a question from Senator Klein, Mr. Hunter said external investment managers are used for the legacy and budget stabilization fund investments. He said the managers fees can be paid a fixed rate or a performance-based fee.

It was moved by Mr. Hardmeyer, seconded by Senator Dotzenrod, and carried on a roll call vote that the advisory board recommends the Retirement and Investment Office contract with Callan Associates to conduct an asset allocation study of the legacy fund. Representatives Kempenich and Kreidt, Senators Dotzenrod and Klein and Citizen Members Hardmeyer, Morrissette, and Ms. Sharp voted "aye." No negative votes were cast.

BANK OF NORTH DAKOTA MATCHING AND INFRASTRUCTURE LOAN PROGRAMS

At the request of Chairman Kempenich, Mr. Hardmeyer presented information ([Appendix D](#)) regarding the Bank of North Dakota's matching loan program and the possibility of increasing legacy fund investments in Bank certificates of deposits (CDs) in order for the Bank to increase funding available for the matching loan program and an infrastructure loan program. He said there is no risk to the legacy fund as the risk of loss lies with the Bank and the Bank has never had a loss on a loan in its match program.

In response to a question from Representative Kreidt, Mr. Hardmeyer said the CD rate would be the United States Treasury rate plus an agreed upon markup. He said the match program currently includes a fixed interest rate for a 5-year period with terms of 15 to 20 years. He said the political subdivisions would prefer to have a longer period in which the interest rate is fixed.

No further business appearing, Chairman Kempenich adjourned the meeting at 2:50 p.m.

Chris Kadrmas
Fiscal Analyst

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