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## LEGACY AND BUDGET STABILIZATION FUND ADVISORY BOARD

Wednesday, June 17, 2020

Representative Keith Kempenich, Chairman, called the meeting to order at 9:00 a.m.

**Members present:** Representatives Keith Kempenich, Gary Kreidt; Senators Jim Dotzenrod, Jerry Klein; Citizen Members Eric Hardmeyer, Joe Morrissette, Ryan Rauschenberger

**Members absent:** None

**Others present:** Senator Rich Wardner, Dickinson, member of the Legislative Management  
See [Appendix A](#) for additional persons present.

**It was moved by Representative Kreidt, seconded by Mr. Hardmeyer, and carried on a voice vote that the minutes of the December 3, 2019, meeting be approved as distributed.**

### 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 fund balance, investment performance, and fund allocation. Mr. Hunter said the budget stabilization fund had a net loss of 0.37 percent compared to a policy benchmark gain of 3.62 percent fiscal year to date through April 30, 2020. He said the fund had a net gain of 1.85 percent compared to a policy benchmark gain of 1.41 percent for the 5-year period ended June 30, 2019. He said as of April 30, 2020, the balance of the fund was \$708 million and the asset allocation of the budget stabilization fund was 98.9 percent short-term fixed income and 1.1 percent cash and equivalents. He said a market downturn related to the Coronavirus (COVID-19) pandemic resulted in a net loss of 3.59 percent, compared to a policy benchmark gain of 1.68 percent, for the quarter ended March 31, 2020. However, he said, the market value of the fund has rebounded and the fund has excellent liquidity. He said the market value is anticipated to be \$714 million as of May 31, 2020.

In response to a question from Chairman Kempenich, Mr. Hunter said due to the COVID-19 pandemic, there was a need for liquidity and investors were unable to sell other assets for a reasonable price. He said the sale of high quality short-term fixed income investments at a discount to raise cash decreased the value. He said because the fund is invested in short-term fixed income, the fund will trend toward par as asset maturity dates approach. He said the market value of the fund should fully recover by June 30, 2021.

In response to a question from Mr. Hardmeyer, Mr. Morrissette said North Dakota Century Code Section 54-27.2-01 provides any deposits or earnings of the fund which would bring the balance in the fund at the end of any fiscal year to an amount greater than 15 percent of the general fund budget may not be deposited in or credited to the fund, but must be deposited instead in the general fund. He said the statutory limit of the budget stabilization fund is \$726 million. He said in March 2020, the final oil tax revenue deposits were calculated and made to bring the fund to the maximum balance. He said the Office of Management and Budget does not anticipate making additional deposits to the fund based on changes in market value. He said the statute could be clarified regarding the effects of market value on fund deposits.

### 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 allocation, fund balance, investment performance, and investment management fees. Mr. Hunter said the market value of the legacy fund was \$6.15 billion as of March 31, 2020. He said asset allocations of the legacy fund were within 4 percent of target allocations reflecting the investment policy benchmark of 50 percent equity investments, 35 percent fixed income, and 15 percent real assets. He said given strong capital market and economic conditions, the legacy fund balance peaked in February 2020 at over \$7 billion. However, he said, due to the effect of the COVID-19 pandemic, returns declined 12.65 percent during the 1<sup>st</sup> quarter

of 2020. He said the fund gained 6.35 percent in April for a net loss of 1.30 percent fiscal year to date through April 30, 2020. He said based on preliminary estimates through June 12, 2020, the fund is anticipated to earn 2 percent during fiscal year 2020. He said legacy fund earnings have totaled \$1.321 billion since inception. He said earnings, as defined in Section 21-10-12 have totaled \$1.09 billion since inception, of which \$436.8 million was added to the principal of the fund. He said from June 2019 through April 2020, earnings, as defined in Section 21-10-12 totaled \$198.3 million. He said these earnings peaked on January 31, 2020, at \$262 million and declined to \$143 million by March 31, 2020.

In response to a question from Senator Klein, Chairman Kempenich said the 2019 Legislative Assembly recognized \$100 million of 2019-21 biennium legacy fund earnings as part of the 2019-21 biennium budget.

Mr. Morrisette said the 2019-21 biennium budget also includes a contingent transfer of \$64 million of legacy fund earnings to the common schools trust fund.

Chairman Kempenich said the volatility of earnings in the last 3 months is reason to avoid appropriating legacy fund earnings before the earnings are deposited into the general fund and to support a more stable distribution policy, such as percent of market value.

In response to a question from Mr. Hardmeyer, Chairman Kempenich said changing the distribution of earnings to a percent of market value would require legislation.

In response to a question from Senator Klein, Chairman Kempenich said the State Investment Board (SIB) supports a percent of market value distribution policy for the legacy fund.

Mr. Hunter said SIB supports the percent of market value method of distribution because it will eliminate risk in the state budget process.

In response to a question from Mr. Rauschenberger, Mr. Hunter said no one attending the SIB meeting voted against the percent of market value distribution. He said SIB did not recommend a percentage for distribution.

In response to a question from Senator Klein, Mr. Hunter said investment fees, as a percent of average assets under management, increased from .33 percent in fiscal year 2018 to .39 percent in fiscal year 2019. He said, even with activity necessary to rebalance the fund, investment fees should not exceed .50 percent in fiscal year 2020 because challenging market conditions likely will eliminate performance fees.

Mr. Hunter provided information ([Appendix D](#)) regarding market benchmarks and performance and SIB assets under management. He said the market value of assets under the management of SIB as of April 30, 2020, totaled \$15.5 billion.

No further business appearing, Chairman Kempenich adjourned the meeting at 10:02 a.m.

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Senior Fiscal Analyst

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