NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

BUDGET AND FINANCE COMMITTEE

Thursday, June 19, 2008
Roughrider Room, State Capitol
Bismarck, North Dakota

Representative Al Carlson, Chairman, called the meeting to order at 9:00 a.m.

Members present: Representatives Al Carlson, Ole Aarsvold, Rick Berg, Merle Boucher, Jeff Delzer, Bob Skarphol, Ken Svedjan, Clark Williams; Senators Randel Christmann, Elroy N. Lindaas, Larry J. Robinson

Members absent: Representative Bob Martinson; Senators Tony Grindberg, Ray Holmberg, David O'Connell, Bob Stenehjem

Others present: Jim W. Smith, Legislative Council, Bismarck

See attached appendix for additional persons present.

It was moved by Senator Robinson, seconded by Representative Aarsvold, and carried on a voice vote that the minutes of the previous meeting be approved as distributed.

STATUS OF THE GENERAL FUND

Mr. Joe Morrissette, Executive Budget Analyst, Office of Management and Budget (OMB), presented a report on the status of the general fund, including oil and gas tax distributions to local governments, the history of the use of the money deposited in the permanent oil tax trust fund, and a history of annual oil and gas tax and mineral royalty distributions to individual cities and counties. Mr. Morrissette presented the following schedule showing the status of the general fund for the 2007-09 biennium as of May 31, 2008:

July 1, 2007, balance	$295,541,176
Estimated revenues	2,437,493,115
Estimated available funds	$2,733,034,291
Appropriations	(2,461,973,956)
Estimated June 30, 2009, balance	$271,060,335

Mr. Morrissette presented the following schedule showing the status of the permanent oil tax trust fund for the 2007-09 biennium as of May 31, 2008:

July 1, 2007, balance	$143,270,662
Estimated revenues	271,338,702
Estimated available funds	$414,609,364
Appropriations and transfers	(145,716,541)
Estimated June 30, 2009, balance	$268,892,823

Mr. Morrissette presented the following schedule showing the history of revenues and expenditures of the permanent oil tax trust fund since the 1999-2001 biennium as follows:

Beginning July 1, 1999, balance	$0
Estimated revenues	511,359,825
Appropriations and transfers	(242,467,002)
Estimated June 30, 2009, balance	$268,892,823

In response to a question from Representative Carlson, Mr. Jim W. Smith, Director, Legislative Council, said if the proposed constitutional measure creating a new permanent oil tax trust fund is approved in the November 2008 general election, resulting in the repeal of the current permanent oil tax trust fund, the 2009 Legislative Assembly would need to address the use of the balance in the current permanent oil tax trust fund currently estimated to be $269 million.

Mr. Morrissette presented a schedule showing oil and gas tax and mineral royalty allocations to cities and counties for fiscal years 2004 through 2007 and for fiscal year 2008 through May 2008. The information indicates that allocations to cities and counties from these sources have increased from a total of $18.8 million for fiscal year 2004 to $43.6 million for fiscal year 2008 through May 2008. A copy of the OMB reports are on file in the Legislative Council office.

Representative Skarphol expressed concern with the inconsistency of the current oil and gas tax allocation formula to cities within counties. He said allocations to cities of similar size and similar oil impact activity vary greatly under the current system. He suggested the 2009 Legislative Assembly consider increasing funding for the oil and gas impact fund that could be used to correct inconsistencies that result from the allocations made under the current formula. He suggested the Legislative Assembly establish a priority listing for the use of the funding in the oil and gas impact fund.

Ms. Kathryn L. Strombeck, Tax Department, provided information on the status of corporate income tax collections, financial institutions tax collections, and individual income tax collections to date for the 2007-09 biennium and on the amount of homestead income tax credits being claimed on 2007 tax returns.

Ms. Strombeck said corporate income tax collections through May 2008 compared to collections

through May of the previous fiscal year have increased by $23.2 million or 24.6 percent.

Regarding financial institutions tax collections, Ms. Strombeck said collections for fiscal year 2008 through May 2008, compared to collections through May of the previous fiscal year, have increased by $2 million or 12.5 percent.

Regarding individual income tax collections, Ms. Strombeck said for fiscal year 2008 through May 2008 individual income tax collections are $18.8 million or 6.2 percent less than the same period in the previous year. However, she said, adjusting for property tax relief, which has reduced collections, collections have increased by approximately 7 percent compared to the previous fiscal year to date.

Regarding property tax relief income tax credits, Ms. Strombeck said through June 18, 2008, the Tax Department has processed 151,432 tax returns claiming a property tax income tax credit which has totaled $36.8 million. She said approximately 20,000 individual income tax returns are still outstanding due to extensions being granted. A copy of the report is on file in the Legislative Council office.

In response to a question from Representative Carlson, Ms. Strombeck said the fiscal note on 2007 Senate Bill No. 2032 anticipated a total general fund revenue reduction of $112 million relating to the individual income tax and commercial income tax property tax credits. Based on the claims processed to date, she said, she anticipates the actual general fund revenue reduction resulting from the credits to be less than the $112 million anticipated in the fiscal note.

In response to a question from Representative Delzer, Ms. Strombeck said most corporations will not file and claim their commercial property tax income tax credit until September or October of this year.

Representative Boucher said some taxpayers are confused by the process involved in claiming the property tax income tax credit.

Senator Robinson suggested the committee receive information on the types of jobs that are increasing in the state compared to those that are decreasing. Chairman Carlson asked that Job Service North Dakota be scheduled to present information on this at the committee's next meeting.

OIL-RELATED TAX REVENUES

Ms. Becky Keller, Fiscal Analyst, Legislative Council, presented a memorandum entitled *Oil Production, Oil Market Price, and Oil Tax Revenue Information for the 2007-09 Biennium*. She reviewed information included in the memorandum regarding oil production, oil market prices, and oil tax revenues, including information on the statutory provisions relating to the oil and gas gross production tax, the oil extraction tax, the permanent oil tax trust fund, the oil and gas research fund, oil production and revenues for the 2007-09 biennium, and the history of oil activity in North Dakota.

Ms. Keller said based on actual oil and gas tax revenues through May 2008, assuming a high volume of oil production for the remainder of the biennium based on projections made by the Industrial Commission's Department of Mineral Resources, and assuming an oil price of $109 per barrel for the remainder of the biennium, a total of $947 million of oil and gas tax revenues would generated resulting in a total of $614.8 million being deposited in the permanent oil tax trust fund for the 2007-09 biennium.

Senator Christmann suggested the committee receive information on the taxation of oil produced on tribal land. Chairman Carlson asked that the Tax Department provide this information to the committee at its next meeting.

Ms. Strombeck presented information on the actual fiscal effect of provisions of 2007 Senate Bill No. 2178 and 2007 House Bill No. 1044 relating to oil tax distributions. She said 2007 Senate Bill No. 2178, which increased maximum county oil and gas tax allocations by $1 million, is currently anticipated to increase the counties' share and reduce state revenues by $10.8 million for the 2007-09 biennium. She said 2007 House Bill No. 1044, which increases the counties' share of oil and gas tax collections beginning July 1, 2009, is currently anticipated to increase the counties' share and reduce state revenues by $5 million for the second year of the 2007-09 biennium. A copy of the report is on file in the Legislative Council office.

In response to a question from Representative Delzer, Ms. Strombeck said the fiscal note for 2007 Senate Bill No. 2178 indicated a $2 million increase in the counties' share and a $2 million decrease in the state share of oil and gas tax revenues. She said 2007 House Bill No. 1044 was anticipated to increase the counties' share and reduce the state share by $5.9 million.

In response to a question from Representative Skarphol, Ms. Strombeck said the effect of these bills on the 2009-11 biennium is anticipated to total $22 million, $12 million of which relates to provisions of 2007 Senate Bill No. 2178 and $10 million relates to provisions of 2007 House Bill No. 1044.

NORTH DAKOTA LOTTERY

Ms. Julie K. Thompson, Interim Lottery Director, Attorney General's office, presented information on the North Dakota lottery.

Ms. Thompson said the estimated gross proceeds of the lottery for fiscal year 2008 is $22.1 million. Based on this estimate, she said, the lottery should meet its general fund revenue projection for the 2007-09 biennium of $11,155,000.

Ms. Thompson said the lottery is unable to determine the amount of lottery sales that are made to in-state compared to out-of-state residents. She said the lottery has issued prizes to out-of-state players in 37 states and three Canadian provinces. Since the lottery began in March 2004, she said, it has paid over $10 million in high-tier prizes. She said high-tier

prizes are those of $5,000 or more. She said of the $10 million in high-tier prizes, $443,000 was paid to eight out-of-state players--four were from Minnesota, one from Wisconsin, two from Canada, and one from South Dakota. A copy of the report is on file in the Legislative Council office.

In response to a question from Representative Berg, Ms. Thompson said approximately 28 percent of gross lottery sales is deposited as general fund revenue.

Representative Skarphol asked for information on the timing of the use of lottery proceeds by the state.

In response to a question from Representative Berg, Mr. Don Wright, Mental Health and Substance Abuse Services Division, Department of Human Services, said the division administers the compulsive gambling treatment program. He said of the $400,000 of lottery proceeds provided for compulsive gambling treatment services each biennium, $334,000 is used for direct treatment services and approximately $50,000 is used for compulsive gambling awareness programs.

Representative Berg asked for information on the number of compulsive gamblers in North Dakota and whether the treatment services are effective. Mr. Wright said he would provide information on the treatment services to the Legislative Council staff for distribution to committee members.

Representative Delzer asked for information on funding for compulsive gambling treatment that is being provided by the casinos or the Indian tribes in the state.

Representative Berg asked for information on the funding the state provides for compulsive gambling treatment services as a percentage of all gaming revenue collected by the state.

Representative Aarsvold asked for information on recidivism rates for individuals completing compulsive gambling treatment. Mr. Wright said the department would attempt to gather that information and provide it to committee members.

In response to a question from Senator Lindaas, Ms. Thompson said the lottery spends approximately 2 percent of its gross proceeds on advertising and marketing.

NORTH DAKOTA HOME FORECLOSURES

Mr. Robert J. Entringer, Assistant Commissioner, Department of Financial Institutions, presented information on the number of home foreclosures in North Dakota. He said in April 2008 North Dakota had one home foreclosure filing for every 14,657 North Dakota households. He said North Dakota ranks 49th in the number of home foreclosures nationwide. He said rankings for surrounding states are as follows: Minnesota 32nd, South Dakota 47th, and Montana 44th. A copy of the report is on file in the Legislative Council office.

In response to a question from Representative Carlson, Mr. Entringer said approximately .4 percent of all loans in North Dakota are considered subprime.

AGENCY BUDGET INFORMATION

Mr. Dale Frink, State Engineer, State Water Commission, provided information regarding the status of the State Water Commission's 2007-09 biennium budget, federal funds and programmatic changes, status of any one-time expenditures, and anticipated costs to continue and other budget needs for the 2009-11 biennium.

Mr. Frink said through April 2008, the commission has spent $28.7 million for state projects or grants for water projects. He anticipates total project expenditures for the 2007-09 biennium to be approximately $85 million. He said oil tax revenues deposited in the resources trust fund are anticipated to be at least 50 percent more than originally projected for the 2007-09 biennium. As a result, he said, the commission has accelerated several projects, including the Southwest Pipeline Project and the Northwest Area Water Supply Project.

Regarding federal funding, Mr. Frink said the commission received an increase in federal funds in federal fiscal year 2008 for the Municipal, Rural, and Industrial Water Supply Program. He said the increase included $10 million for the Northwest Area Water Supply Project and $4 million for the Southwest Pipeline Project. He said the level of federal funding that may be available for the next biennium is not yet known.

Mr. Frink said the commission anticipates requesting two or three new full-time equivalent (FTE) positions for the next biennium. He said operating expenses will also increase as a result of increases in Fleet Services and information technology rates. A copy of the report is on file in the Legislative Council office.

In response to a question from Representative Carlson, Mr. Frink said State Water Commission bond payments total approximately $14 million per biennium.

Representative Berg asked for information on available State Water Commission funding, amounts committed, and potential future projects. Representative Skarphol asked for information on projects included on the State Water Commission's priority list. Chairman Carlson asked that the State Water Commission provide information to the committee on its anticipated available funds for the next two bienniums, amounts that are committed, and anticipated future water projects and related estimated costs in priority order.

The committee recessed for lunch at 12:10 p.m. and reconvened at 1:00 p.m.

Ms. Roxanne Woeste, Assistant Legislative Budget Analyst and Auditor, presented a memorandum entitled *Status of 2007-09 One-Time Funding Items*. She said the 2007 Legislative Assembly identified a total of $169.3 million, of which $139.5 million is from

the general fund and $29.8 million is from the permanent oil tax trust fund, as one-time funding items for the 2007-09 biennium. She reviewed a schedule summarizing the current status of each one-time funding item identified by the Legislative Assembly.

The Legislative Council staff presented a report entitled *Agency Compliance With Legislative Intent*. The Legislative Council staff said the report includes information on agency compliance with sections of legislative intent included in the agencies' 2007-09 appropriations and information on major agency activities and programs. The report also includes information on the status of selected special funds.

Representative Skarphol suggested the committee receive additional information on activities and state funding provided to regional education associations. Representative Boucher suggested the committee also receive information on other funding received by these associations.

Representative Carlson expressed concern with actions of the Department of Transportation to comply with provisions of the federal REAL ID Act. He suggested the department provide information to the committee at its next meeting regarding its activities associated with the REAL ID and possible alternatives, including the development of an enhanced driver's license.

EXTRAORDINARY REPAIRS

Ms. Woeste presented a memorandum entitled *Status of Extraordinary Repairs Funding - 2007-09 Biennium*. She said the report compares extraordinary repair expenditures by project for all agencies to budgeted amounts for the 2007-09 biennium. She said the 2007 Legislative Assembly identified extraordinary repair projects totaling $40.4 million, of which $28.8 million is from the general fund, for the 2007-09 biennium. She said agencies currently anticipate spending a total of $37.4 million, of which $28.3 million is from the general fund, on extraordinary repair projects. She said a number of agency project priorities have changed from the proposed projects presented to the 2007 Legislative Assembly.

The Legislative Council staff presented a memorandum entitled *Options for Legislative Monitoring of State Agency Extraordinary Repairs Expenditures*. The Legislative Council staff said the memorandum provides information on the current process of budgeting and accounting for extraordinary repair projects and options to allow for comparisons of actual expenditures to budgeted amounts for extraordinary repair projects. The Legislative Council staff said the current process for providing funding for extraordinary repair projects begins with state agencies requesting funding for extraordinary repairs as part of the state agency budget request process. Agencies identify and prioritize each extraordinary repair project for which funding is being requested.

The Legislative Council staff said OMB considers the agency extraordinary repairs request as it develops the executive budget recommendation for each agency. Any change to the extraordinary repairs included as part of the agency's base budget request and any approved extraordinary repairs optional adjustment requests are documented and explained as part of the executive budget recommendation. The executive budget summary report includes a schedule identifying the extraordinary repairs funding approved for each agency in the executive budget recommendation.

The Legislative Council staff said the funding recommended as part of the executive budget for extraordinary repairs for each agency is included in the capital assets line item of the appropriation bill for the agency along with funding being recommended for capital projects, other capital payments, information technology equipment over $5,000, and other equipment over $5,000. Any legislative changes to extraordinary repairs funding are explained in the statement of purpose of amendment to the appropriation bill and included in the Legislative Council's *Analysis of Legislative Changes to the Executive Budget* report at the end of the legislative session. This report also includes a schedule of legislatively approved funding for extraordinary repairs by project for each agency.

The Legislative Council staff said as agencies spend funds from the capital assets line item for extraordinary repair projects, the agency charges the costs to an extraordinary repairs account code under the capital assets line item. Although agencies may internally monitor actual expenditures to budgeted amounts for specific extraordinary repair projects, there is no statewide report generated comparing actual expenditures to budgeted amounts for extraordinary repair projects.

The Legislative Council staff presented options to provide more information on actual expenditures compared to the legislatively approved amounts for extraordinary repair projects, including:

1. An interim legislative committee or the Appropriations Committees during a legislative session may request selected agencies to report on the status of these expenditures periodically.
2. An interim legislative committee or the Appropriations Committees during a legislative session may request the Legislative Council staff to prepare a report on the status of these expenditures for all agencies.
3. A statutory change to North Dakota Century Code Section 54-44.1-06 could be made to require a report on the status of these expenditures for all agencies be included as part of the budget data prepared as part of the executive budget.
4. The Office of Management and Budget could implement a policy that agencies account for these budgeted amounts and expenditures

using project reporting or separate account codes for each project within PeopleSoft. The Office of Management and Budget could generate a periodic report comparing budgeted to actual expenditures by project for all agencies that may be provided to interim legislative committees or the Appropriations Committees upon request.

5. The Legislative Assembly could choose to appropriate extraordinary repairs funding in a separate line item. The Office of Management and Budget could implement a policy that agencies account for these budgeted amounts and expenditures using project reporting or separate account codes for each project within PeopleSoft. The Office of Management and Budget could generate a periodic report comparing budgeted to actual expenditures by project for all agencies that may be provided to interim legislative committees or the Appropriations Committees upon request.

Ms. Lori Laschkewitsch, Executive Budget Analyst, OMB, commented on options for comparing extraordinary repair expenditures to budgeted amounts, including the estimated costs of implementing the various options. She said the best source of information for comparing budgeted amounts to actual expenditures for extraordinary repairs is the state agency to which the funding is appropriated. She said any information that would be provided during the budgeting process would not be complete information for the biennium and would still involve budget estimates for projects that had not yet been completed.

Ms. Laschkewitsch said using the project reporting system within PeopleSoft may not be an adequate solution to provide all of the information needed for providing adequate extraordinary repair project comparisons.

Representative Delzer said state agencies need to be aware of the Legislative Assembly's concern that the funding provided is used for the intended purpose.

Representative Carlson said it is important for agencies to be accountable to the Legislative Assembly on the use of funding provided for extraordinary repairs.

Senator Christmann said agencies have reported that a substantial amount of funding is needed for deferred maintenance projects. He said the Legislative Assembly should have a method of comparing and prioritizing these projects statewide. He suggested adding an additional FTE position to OMB or the Legislative Council to conduct an unbiased evaluation of all of these requests and report to the Legislative Assembly. He said this position could also monitor the subsequent agency expenditure of the funding provided to determine that it is being spent in accordance with legislative intent.

HISTORICAL ECONOMIC INDICATORS

Ms. Keller presented a memorandum entitled *State Revenues and Selected Economic Indicators - Historical Comparison*. She reviewed a number of charts providing a historical comparison of selected economic indicators for North Dakota, including crop production values, real estate values, oil prices, oil production, personal income, and gross state product, to ongoing general fund taxes and fee collections, including collections from sales tax, motor vehicle excise tax, individual and corporate income taxes, and other ongoing revenues.

Representative Delzer suggested additional information be included on the charts regarding general fund appropriations.

Representative Aarsvold suggested a similar chart be prepared showing information on federal revenues received in the state.

Representative Boucher suggested preparing a chart including information on North Dakota's population.

Senator Christmann suggested preparing a chart including information on livestock values.

PRELIMINARY 2009-11 BUDGET INFORMATION

The Legislative Council staff presented a memorandum entitled *Preliminary Outlook - North Dakota 2009-11 Biennium General Fund Budget*. The Legislative Council staff said the memorandum provides preliminary information on general fund ongoing and one-time revenues and expenditures anticipated for the 2009-11 biennium. The Legislative Council staff said the revenue items are subject to updated revenue estimates expected in July 2008 for the remainder of this biennium and the 2009-11 biennium.

Mr. Morrissette presented 2009-11 biennium cost to continue amounts being identified in the budget development process. He said to determine each agency's 2009-11 biennium general fund base budget limit, OMB staff adjusts each agency's 2007-09 biennium appropriation by removing capital projects and other one-time funding items and any authorized carryover funding from previous bienniums and adding the cost to continue the second-year salary increase, phased-in programs, and any ongoing costs to continue current services. He said the base budget limit amounts have not yet been identified for all agencies. A copy of the report is on file in the Legislative Council office.

In response to a question from Representative Carlson, Mr. Morrissette said because agencies are limited in their base budget request to the current biennium's adjusted funding level, agencies must consider more efficient ways to provide their services.

Representative Delzer suggested OMB consider limiting the amounts agencies may request as part of their optional adjustment requests.

AGENCY BUDGET INFORMATION

Mr. Mike Ressler, Deputy Chief Information Officer, Information Technology Department, provided information on the status of the department's 2007-09 biennium budget, federal funds and programmatic changes, status of any one-time expenditures, anticipated costs to continue and other budget needs for the 2009-11 biennium, and a history of the correlation of Information Technology Department service rate increases and employee salary increases. He said the department's 2007-09 biennium budget totals $126.4 million, of which $11.7 million is from the general fund. He said of this appropriation, $1.6 million from the general fund is for one-time funding items.

Of the department's 85 unique service types, Mr. Ressler said the department is requesting service rate increases for 32 service types. He said the department estimates these increases will cost state agencies $4.5 million for the 2009-11 biennium, which is a 4.8 percent increase. He said the majority of the increases relate to software development and project manager services, device connection/technology fees, and computer hosting services. He said the department's rates will allow the agency to provide a 15 percent salary increase for the next biennium for its software developers and project managers.

Mr. Ressler said agencies that will be most affected by the rate increases include the Department of Human Services, Department of Transportation, and OMB.

Mr. Ressler said the department is experiencing a 7 percent employee turnover rate during the current year compared to a 4.6 percent turnover rate for the previous year. He said the department is having difficulty recruiting and retaining employees. A copy of the report is on file in the Legislative Council office.

Mr. Mark Molesworth, Enterprise Project Manager, Information Technology Department, presented information on changes being proposed to state agency information technology project budgeting. He said the supporting documentation submitted by state agencies when requesting funding for information technology projects as part of their information technology plan will include information on additional costs that are considered "reallocated" from other areas of the agency's budget that relate to the information technology project. He said this information will provide a more accurate cost of each information technology project for which funding is being requested.

COMMITTEE DISCUSSION AND STAFF DIRECTIVES

Representative Aarsvold suggested that because the state is such a large consumer of energy, the committee may wish to receive information on the possibility of the state purchasing its energy based on a fixed price contract for a certain period of time.

Representative Skarphol asked the Legislative Council staff to continue to update the committee on anticipated deficiency appropriations that may be requested of the 2009 Legislative Assembly.

The committee adjourned subject to the call of the chair at 4:25 p.m.

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Allen H. Knudson
Legislative Budget Analyst and Auditor

ATTACH:1