

NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

BUDGET AND FINANCE COMMITTEE

Wednesday, October 31, 2007
Harvest 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 Martinson, Bob Skarphol, Ken Svedjan; Senators Randel Christmann, Tony Grindberg, Ray Holmberg, Elroy N. Lindaas, David O'Connell, Larry J. Robinson

Members absent: Representative Clark Williams; Senator Bob Stenehjem

Others present: See attached [appendix](#)

Mr. Jim W. Smith, Legislative Budget Analyst and Auditor, reviewed the [Supplementary Rules of Operation and Procedure of the North Dakota Legislative Council](#).

Chairman Carlson commented on the committee's responsibilities. He said because the Legislative Council has not appointed interim budget committees during this interim to monitor and receive information on agency budgets, this committee will also be fulfilling that responsibility. He said the committee will also be gathering information on major budget items to assist the 2009 Legislative Assembly in its consideration of state budget issues.

COMMITTEE RESPONSIBILITIES

The Legislative Council staff presented a background memorandum entitled [Budget and Finance Committee - Background Memorandum](#). The Legislative Council staff reviewed the following potential duties and responsibilities of the committee:

- Monitor the status of state revenues and expenditures for the 2007-09 biennium.
- Receive input from major state agencies regarding the status of their budgets and changes in federal funds.
- Receive information from major state agencies regarding anticipated program changes, costs to continue, and other budget needs for the 2009-11 biennium, including elementary and secondary education, higher education, human services, corrections, and transportation.
- Receive information on any deferred maintenance issues relating to facilities and other infrastructure throughout state government.
- Review current budget forms and guidelines, consider any appropriate changes, and provide a recommendation to the Budget Section.

- Receive input from industry and academic representatives on the status of the state's economy, state revenue impact, and expectations for the 2009-11 biennium.
- Receive information from the economic forecasting consultant under contract with the state on the state's economy, including strengths and weaknesses, and provide input to the consultant on the development of the July 2008 general fund revenue forecast for the 2007-09 biennium and the preliminary forecast for the 2009-11 biennium.
- Receive the July 2008 revised general fund revenue forecast.
- Review projected revenues, expenditures, and fund balances of major state funds.
- Review preliminary information on 2009-11 estimated revenues and appropriation requirements, including cost to continue items.
- Discuss possible legislative initiatives that would affect the budget.
- Discuss possible methods of returning excess revenues to North Dakota taxpayers.
- Identify key budget issues for the 2009 legislative session.
- As appropriate, make recommendations to the Legislative Council.

PREVIOUS STUDIES

The Legislative Council staff reviewed previous studies relating to the budget process. The Legislative Council staff said that beginning with the 1975-76 interim, a Legislative Council interim committee has been assigned the responsibility of monitoring the status of major state agency and institution appropriations. In previous bienniums, the committee's review placed emphasis on expenditures of major state agencies.

A report on the status of agency compliance with legislative intent has been completed each interim since 1987-88. This report has included the status of state agency and institution budgets, the status of the implementation of budget/programmatic changes, legislative directives contained in appropriation bills and other legislation, and the identification of key agency budget issues.

The Legislative Council staff said the 1997-98 interim Budget Committee on Government Finance, Senator David E. Nething, Chairman, studied North

Dakota's budgeting process. As part of the study, the committee:

1. Considered the development of a legislative budget and recommended a bill which would have created a legislative budget committee and additional interim committees to provide assistance to the Legislative Assembly in the development of the legislative budget.
2. Reviewed the performance budgeting pilot project.
3. Considered other budgeting issues.

The Legislative Council staff said the 2003-04 interim Government Performance and Accountability Committee, Representative Al Carlson, Chairman, studied state government performance and accountability practices and recommended House Bill No. 1035 providing for the creation of a government performance and accountability system. The bill was amended by the 2005 Legislative Assembly to provide for a government performance and accountability system pilot project.

The 2005-06 interim Budget Committee on Government Services, Representative Al Carlson, Chairman, was assigned responsibility to establish the government performance and accountability pilot project involving up to three executive branch agencies. The committee approved designating the Department of Transportation, Parks and Recreation Department, and the Highway Patrol as participants in the government performance and accountability system pilot project. The committee did not make any recommendations regarding the government performance and accountability system pilot project.

NORTH DAKOTA'S BUDGETING PROCESS

The Legislative Council staff reviewed North Dakota's budgeting process and constitutional and statutory provisions relating to the state budget, including Article V, Section 7, of the Constitution of North Dakota relating to the powers of the Governor, Article X, Section 12, of the Constitution of North Dakota relating to legislative appropriations, North Dakota Century Code (NDCC) Sections 54-35-12 through 54-35-14 relating to the powers of the legislative budget analyst and auditor, and Chapter 54-44.1 relating to the office of the budget.

The Legislative Council staff reviewed North Dakota's revenue forecasting process and said the executive budget office has primary authority for revenue forecasting in North Dakota. Historically, during each biennium, the Office of Management and Budget (OMB) issues three revenue forecasts:

- **June preliminary revenue forecast** - Issued in the even-numbered year prior to the start of the legislative session.
- **December executive budget revenue forecast** - Presented along with the executive budget recommendations to the Budget Section

and to the organizational session of the Legislative Assembly.

- **February/March revised revenue forecast** - Presented in either February or March during the legislative session at which time the forecast is reviewed by legislative leadership, Appropriations Committee members, and Finance and Taxation Committee members of both houses. The Appropriations Committees by motion approve the revised revenue forecast which is then used as the "official" legislative revenue forecast. The Legislative Assembly has generally not changed the revised revenue forecast.

During the 2007 legislative session, this forecast was received in February. Previously, this forecast was received in March.

The Office of Management and Budget contracts with Moody's Economy.com to provide economic projections for the state of North Dakota. North Dakota's current contract with Moody's Economy.com is for the period beginning November 14, 2005, and ending November 13, 2007. The contract provides for the state of North Dakota to pay Moody's Economy.com two annual payments of \$26,185 or \$52,370 per biennium.

The state subscribes to the following Moody's Economy.com publications:

- *Regional Financial Review.*
- *Precis: State.*
- *Precis: Macro With U.S. Macro/Financial Database.*

Moody's Economy.com provides tax-based forecasts for each of the major taxable sectors. Reports prepared by Moody's Economy.com include analyses and forecasts of sweet crude oil prices and production. As needed, Moody's Economy.com will also include analyses and forecasts of North Dakota's major crops and livestock, including farm income and cash receipts for livestock and products.

The Tax Department is responsible for the basic methodology for forecasting the following general fund tax types--sales, motor vehicle excise, individual income, corporation income, financial institution, oil extraction, oil and gas production, cigarette and tobacco, coal conversion, and wholesale liquor taxes. The revenue forecasting process includes the following steps:

- At the start of each of the three forecasts, the Tax Department updates the historical tax base statistics and provides the results to Moody's Economy.com.
- Moody's Economy.com processes the historical data through forecasting models, adjusting and updating forecast equations or "drivers" as needed.
- The Tax Department and Office of Management and Budget participate in conference calls with Moody's Economy.com to discuss views on the United States and North Dakota economies.

- Moody's Economy.com creates North Dakota's tax-based forecasts for each of the next three fiscal years.
- The Office of Management and Budget schedules a meeting of the Revenue Advisory Committee to review the tax-based forecasts and make any modifications as determined by the committee.
- The Tax Department applies the appropriate tax rates and statutory distributions through the use of in-house tax revenue models to produce the tax revenue forecast, which is supplied to the Office of Management and Budget.

The Revenue Advisory Committee is a committee generally consisting of private sector members, at least two legislators, and other public officials. The Revenue Advisory Committee, which was created by the Office of Management and Budget, meets before each forecast is issued to review the economic projections and resulting tax-based forecasts.

FISCAL INFORMATION

The Legislative Council staff presented a schedule comparing general fund collections to revenue forecasts for the period 1981-83 through 2005-07. Actual revenues varied from being 15.6 percent **less than** forecast in the 1981-83 biennium to being 19.8 percent **more than** forecast in the 2005-07 biennium.

The Legislative Council staff distributed a copy of the June 2007 state economic report for North Dakota prepared by Economy.com.

The Legislative Council staff reviewed the memorandum entitled [Fiscal Information Summary](#) which included information on various tax revenue sources and major expenditure items.

The Legislative Council staff distributed an economic brief prepared by the North Dakota State Data Center on oil production in North Dakota. The information indicated that North Dakota ranked ninth in crude oil production out of 31 oil-producing states and two federal offshore areas in 2006. The Legislative Council staff said that of the major oil-producing states in the United States, only North Dakota and Montana have experienced increased oil production during the last 10 years.

Ms. Roxanne Woeste, Senior Fiscal Analyst, Legislative Council, presented a report entitled [Budget and Fiscal Trends](#) which provided information on state revenue and expenditure levels during the last 10 years.

COMMITTEE DISCUSSION

Representative Delzer asked the Legislative Council staff to review the factors included in the determination of the consumer price index.

Representative Skarphol expressed concern that while oil produced in North Dakota is currently not experiencing discounting, an increase in oil production in Canada has the potential to result in North Dakota

oil again being discounted due to limited pipeline capacity.

In response to a question from Representative Carlson, the legislative budget analyst and auditor said the proposed constitutional amendment affecting the amount of oil tax revenue deposited in the general fund and the amount deposited in the permanent oil tax trust fund would begin in July 2009. He said the proposal provides that the first \$100 million of oil tax revenues be deposited in the state general fund and the remainder in the permanent oil tax trust fund. He said the \$100 million deposited in the general fund would be allowed to increase each biennium by the consumer price index. He said money deposited in the permanent oil tax trust fund may be spent only upon approval by at least 75 percent of the Legislative Assembly.

Senator Christmann asked for information on the availability of a consumer price index specific to North Dakota and, if available, how the index is calculated for the state. He also asked for information comparing the percentage change in North Dakota personal income to the percentage change in North Dakota inflation and information on causes of the variances.

Representative Skarphol asked the Legislative Council staff to provide a graph showing the level of higher education general fund appropriations and tuition income in total and percentage changes for the last 10 years.

Representative Delzer asked for information on the level of assets included in the common schools trust fund since the 1997-99 biennium.

Representative Berg asked for additional information on the common schools trust fund, including constitutional and statutory provisions relating to investments and distributions from the fund and current investment strategies and distributions made by the Board of University and School Lands.

Representative Skarphol asked for information on the number of clients served by the Department of Human Services in long-term care facilities compared to those served in home and community-based care programs.

Regarding Department of Corrections and Rehabilitation information, Representative Berg asked for projected inmate populations for the next 10 years. Senator Christmann asked for additional information on the current biennium's appropriation increase, including amounts related to medical costs. Representative Boucher asked the Legislative Council staff to project for the next 10 years Department of Corrections and Rehabilitation spending based on historical spending trends which reflect a biennial increase of 30.6 percent. Senator Grindberg asked for the number of male inmates in the corrections system who have been incarcerated for the first time as a result of a drug offense.

Senator Holmberg asked that the state employee information identify programs transferred from political subdivisions or other entities to the state that have resulted in additional state employees.

Representative Aarsvold asked for the level of local funding support for programs for which the state also provides support, such as schools.

Representative Berg asked for the impact on property taxes of state aid to various programs at the local level.

Representative Delzer asked for additional information on why oil and coal distributions to political subdivisions declined for the 2007-09 biennium.

Representative Boucher asked for information on the percentage of county budgets that is provided by state aid. Chairman Carlson suggested a small, medium, and large county could be used as an example to provide this information.

Senator Christmann suggested that the property tax relief proposal approved by the 2007 Legislative Assembly should be considered as state aid to political subdivisions.

STUDY PLAN

The Legislative Council staff said the committee may wish to proceed with its potential duties and responsibilities as follows:

1. October 2007-October 2008	Receive reports from OMB on the status of the general fund and other selected special funds, including revenue collections and expenditures
2. October 2007-January 2008	Review current budget forms and guidelines, consider any appropriate changes, and provide a recommendation to the Budget Section
3. January-June 2008	Receive reports from selected state agencies regarding the status of the 2007-09 biennium budget, including any budget-related concerns, federal funds changes, and programmatic changes
4. January-August 2008	Review information from state agencies and institutions on deferred maintenance issues relating to facilities and other infrastructure throughout state government
5. March-August 2008	Receive information from selected state agencies regarding anticipated costs to continue and other budget needs for the 2009-11 biennium
6. January-August 2008	Receive information from industry and academic representatives on the status of the state's economy, state revenue impact, and expectations for the 2009-11 biennium
7. March-April 2008	Receive information from representatives of Moody's Economy.com on the state's economy, including strengths and weaknesses and provide input on the development of the July 2008 revenue forecast
8. March-October 2008	Review preliminary information on 2009-11 estimated revenue and appropriation requirements, including cost to continue items
9. July-August 2008	Receive the July 2008 revised revenue forecast
10. October 2008	Review projected revenues, expenditures, and fund balances of major state funds

11. October 2008	Review federal fund receipts for the 2007-09 biennium compared to appropriated amounts and anticipated 2009-11 changes
12. March-October 2008	Discuss possible legislative initiatives that would affect the budget
13. March-October 2008	Discuss possible methods of returning excess revenues to North Dakota taxpayers
14. March-October 2008	Identify key budget issues for the 2009 legislative session
15. July-October 2008	As appropriate, develop recommendations and prepare any legislation necessary to implement the recommendations
16. October 2008	Prepare a final report for submission to the Legislative Council

Chairman Carlson said it is his intent that the committee spend the majority of its time focusing on major budgetary items, including education, human services, corrections, and transportation.

Representative Svedjan suggested the committee consider the development of budget parameters to provide to the 2009 Legislative Assembly to assist it in determining appropriate revenue and spending levels for the 2009-11 biennium.

Chairman Carlson suggested the committee receive status reports from state agencies authorized one-time expenditures for the 2007-09 biennium.

Chairman Carlson suggested the committee monitor and analyze the potential impact of the proposed initiated measures affecting state tax revenues that may need to be addressed by the 2009 Legislative Assembly.

Chairman Carlson said that recommendations or legislation being made or proposed by other Legislative Council interim committees will be available for review by this committee as it identifies major budget issues for the 2009 legislative session.

It was moved by Senator Holmberg, seconded by Representative Skarphol, and carried on a voice vote that the committee proceed with its responsibilities as follows:

1. October 2007-October 2008	Receive reports from OMB on the status of the general fund and other selected special funds, including revenue collections and expenditures
2. October 2007-January 2008, or later as appropriate	Review current budget forms and guidelines, consider any appropriate changes, and provide a recommendation to the Budget Section
3. December 2007-June 2008	Receive reports from selected state agencies regarding the status of the 2007-09 biennium budget, including any budget-related concerns, federal funds changes, and programmatic changes
4. December 2007-August 2008	Receive status reports from state agencies authorized one-time expenditures for the 2007-09 biennium

5. December 2007- August 2008	Review information from state agencies and institutions on deferred maintenance issues relating to facilities and other infrastructure throughout state government
6. March- October 2008	Monitor and analyze the potential impact of proposed initiated tax measures on future state revenues
7. March- August 2008	Receive information from selected state agencies regarding anticipated costs to continue and other budget needs for the 2009-11 biennium
8. January- August 2008	Receive information from industry and academic representatives on the status of the state's economy, state revenue impact, and expectations for the 2009-11 biennium
9. March- April 2008	Receive information from representatives of Moody's Economy.com on the state's economy, including strengths and weaknesses and provide input on the development of the July 2008 revenue forecast
10. March-October 2008	Review recommendations of other interim committees that if approved will affect the 2009-11 biennium budget
11. March- October 2008	Review preliminary information on 2009-11 estimated revenue and appropriation requirements, including cost to continue items
12. July- August 2008	Receive the July 2008 revised revenue forecast
13. October 2008	Review projected revenues, expenditures, and fund balances of major state funds
14. October 2008	Review federal fund receipts for the 2007-09 biennium compared to appropriated amounts and anticipated 2009-11 changes
15. March- October 2008	Discuss possible legislative initiatives that would affect the budget
16. March- October 2008	Discuss possible methods of returning excess revenues to North Dakota taxpayers
17. March- October 2008	Identify key budget issues for the 2009 legislative session
18. July-October 2008	Consider development of budget parameters to assist the 2009 Legislative Assembly in determining its appropriate revenue and spending levels for the 2009-11 biennium
19. July- October 2008	As appropriate, develop recommendations and prepare any legislation necessary to implement the recommendations
20. October 2008	Prepare a final report for submission to the Legislative Council

GENERAL FUND STATUS REPORT

Ms. Pam Sharp, Director, Office of Management and Budget, presented information on the status of the general fund, major revenue variances to date, unspent 2005-07 biennium general fund appropriation authority, and 2005-07 biennium appropriations continuing into the 2007-09 biennium.

Based on Ms. Sharp's testimony, the following schedule compares the actual July 1, 2007, balance to the estimate made during the legislative session and the current estimate of the June 30, 2009, balance to the estimate made during the legislative session.

	April 2007 Forecast	Actual Balance	Additional Funds Available
Beginning balance - July 1, 2007			
General fund	\$218,350,170	\$295,541,176	\$77,191,006
Budget stabilization fund	200,000,000	200,000,000	0
Permanent oil tax trust fund	136,666,681	143,270,662	6,603,981
Total	\$555,016,851	\$638,811,838	\$83,794,987
	April 2007 Forecast	Current Estimate	Increase (Decrease)
Ending balance - June 30, 2009			
General fund	\$18,656,179	\$134,073,252	\$115,417,073
Budget stabilization fund	200,000,000	200,000,000	0
Permanent oil tax trust fund	136,967,547	143,572,066	6,604,519
Total	\$355,623,726	\$477,645,318	\$122,021,592

Ms. Sharp said the \$77 million of additional general fund money available on July 1, 2007, was the result of revenues exceeding projections by \$74 million and 2005-07 general fund turnback being \$3 million more than the \$10 million anticipated. Ms. Sharp said the June 30, 2009, general fund ending balance has increased by an additional \$38 million due to general fund revenues exceeding the forecast during the first three months of the 2007-09 biennium.

Ms. Sharp said in October 2007 OMB transferred, pursuant to Section 12 of 2007 Senate Bill No. 2032, \$115 million from the permanent oil tax trust fund to the general fund.

Ms. Sharp presented a schedule listing each agency's unspent 2005-07 biennium general fund appropriation authority which totaled \$13,069,134.

Senator Holmberg asked for additional detail on the unspent appropriation authority of the North Dakota University System office. Ms. Sharp said she would provide that information to the committee.

Chairman Carlson asked the Legislative Council staff to prepare a schedule showing the possible budget stabilization fund transfer at the end of the 2007-09 biennium based on projected ending general fund balances.

Ms. Sharp presented a schedule listing the 2005-07 biennium appropriations authorized to continue for the 2007-09 biennium. Ms. Sharp said that the gross unexpended general fund appropriation authority at the end of the 2005-07 biennium totaled \$30.9 million; however, approximately \$2.2 million was continued into the 2007-09 biennium for capital construction projects, \$14.9 million due to statutory exemptions from NDCC Section 54-44.1-11, \$726,000

relating to bills with emergency clauses, and \$43,000 for other adjustments, leaving a net unexpended general fund appropriation authority of \$13.1 million. A copy of the report is on file in the Legislative Council office.

Representative Skarphol asked that OMB include in future reports a schedule showing the distribution of oil and gas-related tax collections to local governments. Ms. Sharp said that information will be included on future reports.

The committee recessed for lunch at 12:05 p.m. and reconvened at 1:00 p.m.

EXECUTIVE BUDGET PREPARATION PROCESS AND FORMS

Ms. Sheila Peterson, Director, Fiscal Management Division, Office of Management and Budget, provided information on the executive budget preparation process, budget forms, and anticipated budget guidelines and forms for the 2009-11 biennium budget.

Ms. Peterson said the budget preparation process begins at the beginning of each even-numbered year by OMB releasing instructions and guidelines to state agencies for the preparation of their budget request for the upcoming biennium. Ms. Peterson said in April preliminary information on buildings and infrastructure is due from agencies and is used for building and infrastructure formulas. She said in July the preliminary revenue forecast is completed and July 15 is the statutory deadline for agencies to submit their budget requests. She said extensions may be granted to agencies upon a written request to OMB. Ms. Peterson said extensions are often granted to allow agencies to include the most current information in the preparation of their budget request.

After the budget requests have been submitted by the agencies and certified by the executive budget analysts, budget hearings are held on agency budget requests and, subsequently, the budget analysts complete their recommendations for each budget. Ms. Peterson said the executive budget revenue forecast is completed in November and recommendations are finalized. She said the executive budget is presented to the Legislative Assembly at the beginning of December prior to the legislative session.

Ms. Peterson reviewed the revenue projection process and said that most tax-related forecasts are developed with the assistance of the Tax Department and Economy.com. She said OMB projects interest income and departmental collections categories of the revenue forecast.

Ms. Peterson reviewed the budget forms completed by agencies as part of their budget requests and statutory requirements for the budget data presented as part of the executive budget.

In response to a question from Representative Carlson, Ms. Peterson said the executive budget office asks agencies to complete a 95 percent, 98 percent, or hold-even budget. She said this results in agencies needing to explore and develop more efficient methods of providing their services.

In response to a question from Representative Berg, Ms. Peterson said OMB plans to identify one-time expenditures as part of the executive budget; however, she does not anticipate the information will be available on the budget forms prepared by agencies. Representative Berg encouraged OMB to include one-time expenditures on the budget forms to be completed by state agencies and that this information be a part of the budget analysis and reporting system (BARS).

Representative Carlson suggested that agencies on the budget forms identify in more detail the cost to continue changes, which will allow for an accurate compilation of statewide costs to continue.

Representative Berg suggested that OMB encourage agencies to be innovative in their budget development in order to provide better services to the citizens of North Dakota, to become more efficient, and to incorporate the best practices of other states.

Ms. Peterson said in the past, the executive budget has recommended that agencies be allowed to retain a portion of their unspent appropriation authority to use the following biennium for one-time purposes; however, the Legislative Assembly has not approved this proposal.

Representative Skarphol said agencies have not been consistent in charging information technology expenditures to the appropriate object codes. He asked whether in the future these expenditure items will be more accurate. Ms. Peterson said OMB has worked with the Information Technology Department to improve the reporting of information technology-related expenditures of state agencies and that the information should now be more consistent among the agencies.

In response to a question from Representative Skarphol, Ms. Peterson said OMB will provide a listing of funds appropriated for 2005-07 biennium deferred maintenance items and the amounts spent by agencies for these purposes.

Representative Delzer suggested the committee consider including the number of full-time equivalent positions authorized for each agency in appropriation bills.

Chairman Carlson announced the next committee meeting is tentatively scheduled for Thursday, December 13, 2007.

The committee adjourned subject to the call of the chair at 2:15 p.m.

Allen H. Knudson
Assistant Legislative Budget Analyst and Auditor

Jim W. Smith
Legislative Budget Analyst and Auditor

ATTACH:1