

NORTH DAKOTA LEGISLATIVE MANAGEMENT

Minutes of the

GOVERNMENT FINANCE COMMITTEE

Wednesday, April 23, 2014
Roughrider Room, State Capitol
Bismarck, North Dakota

Representative Jeff Delzer, Chairman, called the meeting to order at 9:00 a.m.

Members present: Representatives Jeff Delzer, Larry Bellew, Joshua A. Boschee, Bette Grande, Craig Headland, Rick Holman, Kylie Oversen, Don Vigesaa, Clark Williams; Senators Dwight Cook, Gary A. Lee, Donald Schaible, Ronald Sorvaag, Terry M. Wanzek

Members absent: Representative Lisa Meier; Senator Rich Wardner

Others present: John Bjornson, Legislative Council, Bismarck
Representative Jim Schmidt and Senator Ray Holmberg, members of the Legislative Management, were also in attendance.

See [Appendix A](#) for additional persons present.

It was moved by Representative Grande, seconded by Senator Wanzek, and carried on a voice vote that the minutes of the March 13, 2014, meeting be approved as distributed.

PRESENTATIONS BY POTENTIAL CONSULTING ACTUARIES FOR THE COMMITTEE'S STUDY OF STATE EMPLOYEE RETIREMENT PLANS

Chairman Delzer said a request for proposal (RFP) was issued for a consultant to provide an actuarial review of state employee retirement plan information. He said four finalists were invited to present their proposals to the committee.

The Legislative Council staff distributed a memorandum entitled [Study of Main Public Employees Retirement System Plan - Information Regarding the Request for Proposal and Proposal Responses](#), which summarizes the RFP that was issued on March 24, 2014, and the proposals received in response to the request.

Chairman Delzer called on the four finalists to present their proposals to the committee. He said the order of presentations is based on the order in which the proposals were received.

The Nyhart Company

Mr. John L. Dowell, Manager, The Nyhart Company, Indianapolis, Indiana, presented information ([Appendix B](#)) regarding the Nyhart proposal. He said the Nyhart proposal provides for the following:

1. Review current information, including:
 - a. Actuarial reports by The Segal Company.
 - b. Plan provisions.
 - c. Actuarial assumptions.
2. Create scenarios:
 - a. Existing retirement plan until 100 percent funded.
 - b. Existing retirement plan assuming as of Friday, January 1, 2016, new employees enter defined contribution plan.
 - c. Existing retirement plan assuming as of January 1, 2016, new employees enter defined contribution plan and a lump sum payment is made to 100 percent fund the plan.
 - d. Separate projection for political subdivisions.
 - e. Existing plan if closed to state and political subdivisions as of January 1, 2016.

3. Reconcile scenarios.
4. Prepare and present the final report.

In response to a question from Representative Grande, Mr. Dowell said Nyhart provides actuarial services for the Indiana State Teachers' Retirement Fund. He said Nyhart assisted the retirement fund in adjusting the fund's actuarial assumption for return on investment.

In response to a question from Representative Grande, Mr. Dowell said younger employees generally change jobs more frequently than older employees. He said short-term employees generally benefit more from a defined contribution plan than a defined benefit plan.

Milliman, Inc.

Mr. Timothy J. Herman, Principal and Consulting Actuary, Milliman, Inc., Brookfield, Wisconsin, presented information ([Appendix C](#)) regarding the Milliman proposal. He said the Milliman proposal provides for the following:

1. Replicate fund actuary's July 1, 2013, valuation results, including:
 - a. Collect plan documentation and historical information.
 - b. Attempt to replicate and review the fund actuary's methodologies, assumptions, and results. This would include the development of the unfunded actuarial accrued liability, normal cost rate, unfunded accrued liability rate, and the resulting required contribution rate.
 - c. Compare these results to the July 1, 2013, actuarial valuation report to determine reasonableness.
 - d. Review actuarial assumptions and recommend changes if any.
2. Perform the projections for the five scenarios identified in the RFP.
3. Prepare a written report and present the report.

In response to a question from Chairman Delzer, Mr. Herman said the Milliman proposal does not include a review of the financial impact to new employees participating in a defined contribution plan.

In response to a question from Representative Grande, Mr. Herman said Milliman provides actuarial services for various Minnesota public employee retirement plans. He said the Minnesota plans have an aggressive investment policy which results in a higher return on investment for the plans.

In response to a question from Chairman Delzer, Mr. Herman said the Milliman proposal assumes that the number of participants in the state retirement plan will remain the same in the future.

In response to a question from Representative Holman, Mr. Herman said the Milliman proposal could include an adjustment to the variable regarding the number of new employees participating in the state employee retirement plan.

Arthur J. Gallagher & Co.

Mr. Doug Anderson, Actuarial Lead Consultant, Arthur J. Gallagher & Co., Bloomington, Minnesota, presented information ([Appendix D](#)) regarding the Gallagher proposal. He said the Gallagher proposal provides for the following:

1. Provide separate and independent review, including:
 - a. Obtain participant data as used for the July 1, 2013, valuation from The Segal Company.
 - b. Run independent valuation.
 - c. Attempt to match July 1, 2013, actuarial valuation results and reconcile differences with The Segal Company.
 - d. Review the appropriateness of the actuarial assumptions used by The Segal Company and provide recommendations for changes, if any.
 - e. Prepare cost projections for five scenarios as outlined in the RFP.
 - f. Prepare additional cost projections to reflect recommended assumption changes, if any.
 - g. Attempt to reconcile differences from The Segal Company's results.
 - h. Prepare a final report with findings and recommendations and present results to the committee prior to Monday, September 1, 2014.

In response to a question from Chairman Delzer, Mr. Anderson said the Gallagher proposal includes various cost projections using different assumptions. He said the Gallagher proposal also includes an optional service to receive and review raw census data.

In response to a question from Senator Sorvaag, Mr. Anderson said the Gallagher proposal includes a review of the actuarial assumptions used by The Segal Company.

Cheiron, Inc.

Mr. Steve McElhaney and Ms. Fiona Liston, Principal Consulting Actuaries, Cheiron, Inc., McLean, Virginia, presented information ([Appendix E](#)) regarding the Cheiron proposal. Mr. McElhaney said the Cheiron proposal provides for the following:

1. Initial planning meeting.
2. Data request.
3. Data collection and data check using The Segal Company's processed valuation data, or using raw data from the system.
4. Review of actuarial assumptions and methods.
5. Perform initial analysis using The Segal Company's valuation output, or independent replication of the valuation results.
6. Construct a "p-scan" model and run the projections.
7. Report preliminary results.
8. Draft report and present the report to the committee.

In response to a question from Chairman Delzer, Mr. McElhaney said the Cheiron proposal includes the processing of raw census data, a comparison of the processed data to The Segal Company's processed data, and a reconciliation of the differences between the data.

In response to a question from Senator Cook, Mr. McElhaney said Cheiron has experience providing actuarial services to several state government employee retirement plans.

In response to a question from Senator Holmberg, Ms. Liston said Cheiron recently audited data prepared by the actuary under contract with the Rhode Island state employee retirement plan. She said recent lawsuits regarding the Rhode Island state employee retirement plan are due to changes made to benefits under the plan, and the lawsuit is not related to actuarial data provided.

Other Discussion

Chairman Delzer asked the presenters to comment on the actuarial assumptions that would be reviewed under their proposals. The presenters provided various responses, including investment returns, employee pay increases, mortality rates, and termination rates.

Chairman Delzer announced the committee will consider the proposals later in the meeting.

STUDY OF STATE EMPLOYEE HEALTH INSURANCE PREMIUMS

The Legislative Council staff presented a memorandum entitled [State Employee Health Insurance Premium Information](#). The memorandum summarizes the estimated monthly amount that would be paid by state employees if employees were required to pay a portion of health insurance premiums as follows:

Monthly Premium ¹	1 Percent of Premium	2 Percent of Premium	3 Percent of Premium	4 Percent of Premium	5 Percent of Premium
Single plan - \$472.74	\$4.73	\$9.45	\$14.18	\$18.91	\$23.64
Family plan - \$1,139.34	\$11.39	\$22.79	\$34.18	\$45.57	\$56.97

¹Reflects monthly premiums for the 2013-15 biennium.

The memorandum also summarizes the total estimated biennial amounts that would be paid by state employees for health insurance premiums if employees were required to pay a portion of health insurance premiums as follows:

Estimated Total Biennial Amounts to Be Paid by State Employees for Health Insurance Based on Percentage of Premium Paid						
	Number of Plans	1 Percent	2 Percent	3 Percent	4 Percent	5 Percent
Single plan	3,384	\$384,152	\$767,491	\$1,151,643	\$1,535,795	\$1,919,946
Family plan	11,687	3,194,758	6,392,322	9,587,080	12,781,838	15,979,401
Total	15,071	\$3,578,910	\$7,159,813	\$10,738,723	\$14,317,633	\$17,899,347

In response to a question from Chairman Delzer, the Legislative Council staff said the memorandum assumes that each state employee would pay a percentage of health insurance premiums based on whether the employee is enrolled in a single plan or a family plan.

Chairman Delzer asked the Legislative Council staff to provide information regarding whether the Affordable Care Act requires employees to pay a percentage of premiums based on a single or family plan or if employees could pay a percentage of premiums based on the blended rate used for active state employees.

Representative Holman suggested the committee receive information regarding changes in health insurance premium rates as a result of previously uninsured individuals enrolling in health insurance plans.

Chairman Delzer asked the Legislative Council staff to provide information regarding preliminary estimates for 2015-17 biennium health insurance premium rates.

STUDY OF THE PROCESS OF APPROPRIATING STATE AGENCY SALARIES AND WAGES

Chairman Delzer said the committee was assigned a study of the process of appropriating state agency salaries and wages. He said one area the study is to review is whether funding for state employee salaries and wages should be appropriated in a block grant format to state agencies without authorizing a specific number of full-time equivalent (FTE) employees.

Senator Holmberg said appropriations to North Dakota University System institutions are currently in a block grant format, and the institutions have the ability to adjust FTE positions as needed subject to the availability of funds.

Chairman Delzer asked the Legislative Council staff to research whether any other states have recently changed methods for appropriating state agency salaries and wages.

STUDY OF THE LASTING BENEFITS OF THE LEGACY FUND

The Legislative Budget Analyst and Auditor reviewed a bill draft [[15.0057.03000](#)] clarifying provisions relating to the legacy fund. The bill draft provides several definitions for constitutional provisions relating to the legacy fund and clarifies the process used to determine limitations on expenditures from the legacy fund. The bill draft also provides that earnings transferred from the legacy fund to the general fund at the end of a biennium are to be transferred back to the legacy fund and become principal unless certain criteria are met.

Representative Boschee expressed concern regarding the intent language included in the bill draft relating to the fund earnings being returned from the general fund to the legacy fund. He said the bill draft may be circumventing the intent of the voters by requiring fund earnings to become part of fund principal rather than using the funds for the needs of the state.

Chairman Delzer said the requirement for fund earnings to become principal will allow the fund balance to increase to a level that would be sufficient to replace decreasing oil tax revenues in the event of an economic downturn.

It was moved by Senator Cook, seconded by Representative Grande, and carried on a roll call vote to approve the bill draft relating to provisions of the legacy fund and to recommend the bill draft to the Legislative Management. Representatives Delzer, Bellew, Grande, Headland, Holman, Vigasaa, and Williams and Senators Cook, Lee, Schaible, Sorvaag, and Wanzek voted "aye." Representatives Boschee and Oversen voted "nay."

STUDY OF THE FOUNDATION AID STABILIZATION FUND

The Legislative Council staff reviewed a bill draft [15.0055.02000] clarifying the use of the foundation aid stabilization fund and budget stabilization fund for state school aid payments in the event of a general fund revenue shortfall. The bill draft provides for the foundation aid stabilization fund to be used to offset the first 2.5 percent general fund revenue shortfall relating to state school aid payments. For any revenue shortfall in excess of 2.5 percent, the budget stabilization fund is to be used first to offset the shortfall, and the foundation aid stabilization fund is to be used to offset the shortfall once the budget stabilization fund is depleted.

The Legislative Council staff presented a memorandum entitled [Use of Foundation Aid Stabilization Fund and Budget Stabilization Fund for State School Aid Payments - Based on Bill Draft 15.0055.02000](#). The memorandum provides information on the amount of funding that would be used from the foundation aid stabilization fund and budget stabilization fund to offset a revenue shortfall based on the Tuesday, June 30, 2015, estimated balances of the funds, the 2013-15 biennium appropriations, and the provisions included in the bill draft as follows:

Use of Foundation Aid Stabilization Fund and Budget Stabilization Fund to Offset Allotments - Based on Bill Draft 15.0055.02000			
Allotment/Revenue Shortfall Amount	State School Aid Payments - General Fund	Other General Fund Appropriations	Total
First 2.5 percent - Foundation aid stabilization fund	\$42,384,350	\$0	\$42,384,350
From 2.5 to 11 percent - Budget stabilization fund ¹	\$144,162,591	\$439,383,208	\$583,545,799
From 11 to 44.8 percent - Foundation aid stabilization fund	\$573,052,441	\$0	\$573,052,441

¹The Legislative Assembly in 2013 House Bill No. 1015 provided \$720 million of general fund appropriations be excluded from the calculation used to determine the maximum balance of the budget stabilization fund. Therefore, the current fund balance of the budget stabilization fund is equal to approximately 8.5 percent of total general fund appropriations for the 2013-15 biennium.

Chairman Delzer asked the Legislative Council staff to provide information regarding previous budget allotments and special legislative sessions resulting from revenue shortfalls.

Chairman Delzer said proposals were introduced in both the House and Senate during the 2013 regular legislative session to limit the balance of the foundation aid stabilization fund. He said the maximum fund balance of the budget stabilization fund may need to be adjusted depending on the use of the fund to offset budget allotments of state school aid payments.

Senator Holmberg said discussion during the last legislative session indicated there was consensus that the balance of the foundation aid stabilization fund should be limited.

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

CONSIDERATION OF PROPOSALS SUBMITTED BY CONSULTING ACTUARIES FOR THE COMMITTEE'S STUDY OF STATE EMPLOYEE RETIREMENT PLANS

Chairman Delzer announced the committee will consider the proposals for a consulting actuary to assist the committee in its study of state employee retirement plans.

Representative Grande said she preferred the Nyhart proposal due to the forecasting model and graphs. However, she said, the Gallagher proposal would cost less than the Nyhart proposal.

Chairman Delzer said he also preferred the Nyhart and Gallagher proposals. He said a key item in the proposals is the calculation of the cost to pay future unfunded liabilities of the defined benefit plan if the plan is closed to new employees.

Senator Holmberg said a strong point of certain proposals was the ability to perform multiple calculations using different assumptions.

Senator Cook said all of the proposals were excellent, but he prefers the Gallagher proposal.

In response to a question from Chairman Delzer, Mr. Anderson said the Gallagher proposal includes calculating scenarios using different variables.

It was moved by Senator Cook, seconded by Representative Vigessaa, and carried on a roll call vote to recommend the Chairman of the Legislative Management enter a contract with Arthur J. Gallagher & Co. to provide actuarial information as proposed to the committee, including optional services, as part of the

committee's study of the state employee retirement plan, and to recommend the proposal of The Nyhart Company as an alternate. Representatives Delzer, Bellew, Boschee, Grande, Headland, Holman, Oversen, Vigesaa, and Williams and Senators Cook, Lee, Schaible, and Sorvaag voted "aye." No negative votes were cast.

STUDY OF THE PURCHASE OF THE RESEARCH ENTERPRISE AND COMMERCIALIZATION BUILDING

Ms. Alice Brekke, Vice President for Finance and Operations, University of North Dakota, Grand Forks, presented information ([Appendix F](#)) regarding the Research Enterprise and Commercialization (REAC) building and information regarding office and other space leased by the University of North Dakota (UND) in the Grand Forks area. She said information was received from the federal Economic Development Administration (EDA) regarding options to remove restrictions on the building due to the use of an EDA grant to pay for a portion of building construction costs. She said a maximum of 20 percent of the leasable space in the facility may be used for office space by UND. She said to remove the grant restrictions, UND would need to repay the federal share of building costs which is based on the percentage of federal grant funds used to construct the building compared to total construction costs. She said the federal share is based on the current fair market value of the building, and UND would likely have to repay less than the original grant amount.

In response to a question from Chairman Delzer, Ms. Brekke said she will provide information to the committee regarding whether a new building appraisal is needed to determine the amount UND would be required to repay the EDA to remove the federal grant restrictions on building use.

In response to a question from Chairman Delzer, Ms. Brekke said UND prefers to use the REAC building for its original purpose of life science research. However, she said, it would be beneficial to remove the federal grant restrictions to allow more flexibility in building use.

In response to a question from Chairman Delzer regarding financial reporting of research facilities, Ms. Brekke said management reports specific to institution departments are generally not reviewed at the institution level unless there is a deficit situation or other financial issue. She said State Board of Higher Education policy requires institutions to submit reports to the University System office if there are significant financial issues. She said institution departments are included in the institution's annual financial statements, and audited financial statements are available for related external entities.

Mr. Kevan Rusk, Director, REAC Technology Accelerator, University of North Dakota, Grand Forks, presented information ([Appendix G](#)) regarding the future of the REAC building. He said UND is focusing resources to recruit potential tenants to the REAC building. He said several opportunities exist with potential tenants in the composites, aerospace, and energy sectors.

In response to a question from Senator Holmberg, Mr. Rusk said it would be beneficial to remove the federal grant restrictions on the building to allow flexibility to lease more space in the short term.

In response to a question from Chairman Delzer, Mr. Rusk said approximately 10 percent of leasable space in the REAC building is unfinished. He said the space is being left unfinished to allow potential clients the opportunity to customize the space for their needs.

Mr. John Bjornson, Assistant Code Revisor, Legislative Council, presented a memorandum entitled [University of North Dakota Research Enterprise and Commercialization Building Loan Agreement](#). He said the memorandum provides an overview of the loan contract between UND and Bremer Bank for the purchase of the REAC building. He said it appears unlikely that the contract between UND and Bremer Bank could be voided by the state.

In response to a question from Chairman Delzer, Mr. Bjornson said several states have legislative staff to review programs and state agencies to determine compliance with legislative directives. He said the Attorney General would presumably need to be involved if there was a question regarding whether a state agency was properly following a law or legislative directive.

In response to a question from Senator Holmberg, Mr. Bjornson said it is unusual, and potentially reckless, for a governing board to approve a contract without first reviewing the contract.

Senator Holmberg expressed concern that the State Board of Higher Education and Chancellor of the University System gave UND approval to enter a contract with Bremer Bank prior to the contract being negotiated.

In response to a question from Senator Cook, Mr. Bjornson said there does not appear to be any misrepresentation in the loan contract between UND and Bremer Bank. He said the only entity that may have an argument to void the contract is Bremer Bank.

Senator Holmberg said there is little incentive for Bremer Bank to argue the current loan contract is void. He said the loan provides a favorable interest rate to Bremer and results in Bremer avoiding a potential loss as a result of a previous loan nearing default status.

In response to a question from Chairman Delzer, Mr. Bjornson said contracts with state agencies generally provide that the contract is subject to legislative appropriations. He said the Legislative Assembly could specify which funds, if any, may be used to repay the loan.

Chairman Delzer asked the Legislative Council staff to research options for the Legislative Assembly to stay informed on financial issues involving University System institution departments and foundations.

Senator Holmberg said the Legislative Assembly needs to be aware of the use of institution foundations to finance buildings. He said the State Board of Higher Education needs to be more diligent in approving contracts and building projects.

STATE BUDGET INFORMATION Status of the General Fund

Ms. Sheila Peterson, Director, Fiscal Management Division, Office of Management and Budget, presented information ([Appendix H](#)) regarding the status of the general fund and the current balances of major state funds. She presented the following information on the status of the general fund for the 2013-15 biennium:

Unobligated general fund balance - July 1, 2013		\$1,396,059,186
Balance obligated for unspent emergency appropriation authority		165,874,199
Balance obligated for authorized carryover from the 2011-13 biennium		89,503,462
Total beginning general fund balance - July 1, 2013		\$1,651,436,847
Add		
General fund collections through March 2014	\$2,175,870,244	
Forecasted general fund revenue for the remainder of the 2013-15 biennium	3,445,603,488	
Total revenues		5,621,473,732
Total available		\$7,272,910,579
Less		
Legislative appropriations - One time	(\$2,433,567,701)	
Legislative appropriations - Ongoing	(4,429,019,653)	
Authorized carryover from the 2011-13 biennium	(89,503,462)	
2013-15 emergency appropriations utilized in the 2011-13 biennium	163,812,041	
Total appropriations		(6,788,278,775)
Estimated ending general fund balance - June 30, 2015		\$484,631,804 ¹

¹Pursuant to North Dakota Century Code Section 54-27.2-02, any end-of-biennium balance in excess of \$65 million must be transferred to the budget stabilization fund, up to a cap of 9.5 percent of general fund appropriations.

Status of Major Special Funds

Ms. Peterson presented the following information regarding the balances of major state funds as of March 31, 2014:

Budget stabilization fund	\$583,545,799
Legacy fund	\$1,925,223,172
Foundation aid stabilization fund	\$433,407,614
Property tax relief fund	\$657,000,000
Strategic investment and improvements fund	\$1,018,897,650

In response to a question from Chairman Delzer, the Legislative Budget Analyst and Auditor said 25 percent of revenues designated for deposit in the strategic investment and improvements fund are instead deposited in the legacy fund when the unobligated balance of the strategic investment and improvements fund reaches \$300 million.

Representative Vigesaa said motor vehicle excise tax collection estimates for the 2013-15 biennium were aggressive. He said future estimates of motor vehicle excise tax collections may need to be more conservative.

In response to a question from Chairman Delzer, Ms. Peterson said a revised revenue forecast for the 2013-15 biennium and the preliminary 2015-17 biennium revenue forecast will be released in July or August 2014.

OTHER BUSINESS

No further business appearing, Chairman Delzer adjourned the meeting at 2:40 p.m.

Brady A. Larson
Assistant Legislative Budget Analyst and Auditor

Allen H. Knudson
Legislative Budget Analyst and Auditor

ATTACH:8