

NORTH DAKOTA LEGISLATIVE MANAGEMENT

Minutes of the

LEGACY AND BUDGET STABILIZATION FUND ADVISORY BOARD

Monday, December 3, 2018
Sakakawea Room, State Capitol
Bismarck, North Dakota

Representative Keith Kempenich, Chairman, called the meeting to order at 9:30 a.m.

Members present: Representative Keith Kempenich, Gary Kreidt; Senators Jim Dotzenrod, Jerry Klein; Citizen Members Joe Morrissette, Ryan Rauschenberger

Member absent: Eric Hardmeyer

Others present: Representative Corey Mock, Grand Forks, member of the Legislative Management
See [Appendix A](#) for additional persons present.

It was moved by Representative Kreidt, seconded by Senator Klein, and carried on a voice vote that the minutes of the May 24, 2018, and July 27, 2018, meetings be approved as distributed.

STATUS OF THE BUDGET STABILIZATION FUND

At the request of Chairman Kempenich, Mr. David J. Hunter, Executive Director/CIO, Retirement and Investment Office, presented information ([Appendix B](#)) regarding the status of the budget stabilization fund, including investment performance, the fund balance, and the investment policy statement. Mr. Hunter said the budget stabilization fund had a net return of 0.32 percent compared to a policy benchmark return of 0.25 percent for the 1-year period ended September 30, 2018. He said the fund had a net return of 1.33 percent compared to a policy benchmark return of 0.72 percent for the 5-year period ended September 30, 2018. He said as of September 30, 2018, the balance of the fund was \$114 million. He said the asset allocation of the budget stabilization fund is 97 percent short-term fixed income and 3 percent cash and equivalents.

In response to a question from Chairman Kempenich, Mr. Hunter said the budget stabilization fund investment policy is more risk adverse and its investments are highly liquid.

In response to a question from Senator Klein, Mr. Hunter said because the budget stabilization fund is a "rainy day" fund, it needs to be more liquid and historically the fund has been invested in a more risk adverse method.

STATUS OF THE LEGACY FUND

At the request of Chairman Kempenich, Mr. Hunter presented information ([Appendix C](#)) regarding the status of the legacy fund, including investment performance, the fund balance, and investment management fees. Mr. Hunter said the legacy fund had an overall net return of 6.04 percent compared to a policy benchmark return of 5.51 percent for the one year period ended September 30, 2018. He said net earnings for the fiscal year to date through September 30, 2018, totaled \$121.2 million. For the biennium, he said, the fund has generated \$306.5 million of earnings pursuant to the definition of earnings in North Dakota Century Code Section 21-10-12. He said the market value of the fund was \$5.89 billion on September 30, 2018. He said the actual asset allocations of the legacy fund are within 1 percent of the target allocations reflecting the investment policy benchmark of 50 percent equity investments, 35 percent fixed income, and 15 percent real assets. He said investment management fees for the legacy fund totaled \$16.6 million in fiscal year 2018, or 0.31 percent of the average market value of the fund's assets. He said the Legislative Assembly, in Section 11 of House Bill No. 1015 (2017), estimated \$200 million of earnings will be transferred from the legacy fund to the general fund at the end of the 2017-19 biennium. He said as of September 30, 2018, earnings of the legacy fund eligible for transfer to the general fund at the end of the 2017-19 biennium total \$306.5 million.

Chairman Kempenich expressed concern regarding the possibility of losses to the fund in the event of a declining stock market.

In response to a question from Senator Klein, Mr. Hunter said interest, dividend and other investment income, excluding realized and unrealized earnings, of the legacy fund is estimated to generate \$210 million for the 2017-19

biennium.

In response to a question from Chairman Kempenich, Mr. Hunter said the asset allocation study recently completed affirmed the current allocation.

Senator Klein suggested building the principal balance of the legacy fund as much as possible.

Representative Kreidt said he would not support spending the principal of the legacy fund.

In response to a question from Senator Klein, Mr. Hunter said with a fund balance of \$10 billion and a return of 3 percent, the fund would generate \$600 million per biennium.

In response to a question from Mr. Rauschenberger, Mr. Hunter said investment managers make the decision to sell investments which generates the realized earnings and losses. He said the investment managers' strategy focuses on long-term investments.

Ms. Kelly L. Schmidt, State Treasurer, said that the cash flows into the legacy fund are sufficient to meet cash flow needs; therefore, selling existing investments should not be necessary to provide the transfer of earnings to the general fund at the end of the biennium.

No further business appearing, Chairman Kempenich adjourned the meeting at 10:26 a.m.

Chris Kadmas
Fiscal Analyst

ATTACH:3