

NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

BUDGET COMMITTEE ON GOVERNMENT FINANCE

Wednesday, April 22, 1998
Harvest Room, State Capitol
Bismarck, North Dakota

Senator David E. Nething, Chairman, called the meeting to order at 9:00 a.m.

Members present: Senators David E. Nething, Rod St. Aubyn, Bob Stenehjem; Representatives Rick Berg, Jeff W. Delzer, Bette Grande, Roy Hausauer, Matthew M. Klein, William E. Kretschmar, Elwood Thorpe, Ben Tollefson, Gerry Wilkie

Members absent: Senator Harvey D. Tallackson; Representatives Keith Kempenich, Ronald Nichols

Others present: See attached appendix

Chairman Nething announced that without objection the minutes of the previous meeting are approved.

Mr. Rod Backman, Director, Office of Management and Budget, presented a general fund status report for the 1997-99 biennium. Mr. Backman said through March 1998, biennium-to-date revenues have exceeded the 1997-99 legislative forecast by \$27.9 million. He said the current projection for the June 30, 1999, general fund balance is \$38.8 million.

A copy of the report is on file in the Legislative Council office.

Senator Nething suggested that the Office of Management and Budget provide general fund status reports to the Board of Higher Education at its meetings.

Mr. Paul Kramer, Senior Fiscal Analyst, Legislative Council, presented a memorandum entitled *Oil Tax Revenues, Oil Production, and Oil Market Prices for the 1997-99 Biennium*. Mr. Kramer said an average of 13 oil rigs were operating in North Dakota in March 1998. Mr. Kramer said actual oil and gas production tax collections were \$336,000 less than estimated in February 1998 while oil extraction tax collections were \$174,000 less than estimated in February 1998. Mr. Kramer said February 1998 oil production was 69,000 barrels less than the forecast while the price per barrel was \$6.63 less than forecast.

Mr. Kramer responded to committee questions from a previous meeting relating to the effect the

oil price has on oil production in the state. He said production has now decreased as a result of low oil prices. He said two areas of oil production are still increasing--horizontal wells and unit production. He said price does not have as much of an impact on these types of oil production because of:

1. The cost of drilling a horizontal well is less in relation to the amount of oil produced.
2. The large size and enhanced recovery methods utilized in unitized fields.

Mr. Kramer said in February 1998, 39.2 percent of oil production in North Dakota resulted from unitized fields while 25.2 percent was from horizontal wells. Mr. Kramer distributed a document showing oil production from unitized and horizontal wells.

Mr. Jim Smith, Assistant Legislative Budget Analyst and Auditor, presented a memorandum entitled *Department of Human Services AFDC/TANF and Medical Assistance*. He said the AFDC/TANF program's biennium-to-date expenditures are \$9.8 million, \$3 million less than estimated. Regarding medical assistance, Mr. Smith said actual expenditures through February 1998 totaled \$171.2 million, \$3.1 million less than originally estimated.

Representative Delzer asked for the estimated unspent general fund appropriation authority of the Department of Human Services for the 1997-99 biennium. Mr. Smith said the department currently estimates \$2.9 million of general fund savings for the biennium. He is unaware of any potential reallocations the department may make with these funds prior to the end of the biennium.

Mr. Kramer presented a memorandum entitled *Comparison of Estimated and Actual FTE, Expenditures, Revenues, and Populations at the Charitable and Penal Institutions for the Period July 1, 1997, Through December 31, 1997*. Mr. Kramer said total expenditures at the charitable and penal institutions for this period were \$35.6 million,

\$1.8 million (4.7 percent) less than estimated expenditures of \$37.4 million. He said total revenues for this period were \$15,487,000, \$27,000 (.2 percent) less than estimated revenues of \$15,514,000.

Mr. Kramer said the monthly student, resident, and inmate population at these institutions averaged 1,814, 71 fewer than the estimated population of 1,885. He said the full-time equivalent (FTE) positions for these institutions totaled 1,494, 71 fewer than the authorized total of 1,565.

The Legislative Council staff presented a memorandum entitled *Comparison of Estimated and Actual Expenditures, Revenues, and Enrollments at the Institutions of Higher Education for the Period July 1, 1997, Through December 31, 1997*.

The Legislative Council staff said expenditures at the institutions of higher education for this six-month period totaled \$108 million, \$7.5 million (6.5 percent) less than estimated expenditures of \$115.5 million. The Legislative Council staff said income for this period totaled \$38.1 million, \$2.7 million (6.7 percent) less than estimated income of \$40.8 million. The Legislative Council staff said headcount enrollment at the higher education institutions for fall 1997 totaled 33,231, 1,776 (5.1 percent) less than estimated headcount enrollment of 35,007.

Mr. Joe Morrisette, Senior Fiscal Analyst, Legislative Council, presented a memorandum entitled *Status Report on Foundation Aid and Other Payments to School Districts*. Mr. Morrisette said the 1997 Legislative Assembly estimated the number of weighted student units for the 1997-98 academic year at 125,691. He said the current estimate is 123,968 or 1,723 less than estimated. For the 1998-99 academic year the current estimate of weighted student units is 123,359, 2,226 less than the estimate made by the 1997 Legislative Assembly of 125,585. As a result, he said, the end-of-biennium undistributed foundation aid balance is estimated to be \$9.7 million from the general fund. Mr. Morrisette said if these funds were distributed as foundation aid per student payments, approximately \$78 per weighted student unit could be provided for one year.

Mr. Morrisette said state tuition fund distributions are currently estimated to be \$212 per census unit for the 1997-98 academic year, \$8 more than the legislative estimate of \$204 per census unit.

Representative Berg expressed concern that fall 1997 enrollment at the institutions of higher education was 1,700 students less than anticipated. He asked that the next budget monitoring report presented to the committee also include

FTE student comparisons. Chairman Nething said this would be provided and asked the Legislative Council staff to also include estimated enrollment for fall 1998 in the next budget monitoring report.

BUDGET PROCESS STUDY

The Legislative Council staff presented a memorandum entitled *Budgeting Methods in North Dakota and Other States*. The Legislative Council staff said information was added for Florida, Louisiana, Michigan, and Texas in the following budget categories:

1. General budgeting methods.
2. Legislative budget systems.
3. Revenue forecasting.
4. Appropriation bills.
5. Performance measures.
6. Agency flexibility to move funds between line items.
7. Unspent appropriation authority at the end of budget cycle.
8. Budget monitoring and program reviews conducted between legislative sessions.
9. Involvement of legislators in the budgeting process.
10. Fiscal notes.

The Legislative Council staff said that of the four states added, Texas prepares a legislative budget as an alternative to the executive budget; Florida, Louisiana, and Michigan use a consensus method of forecasting revenues; and Florida, Louisiana, and Texas utilize performance budgeting in the development of the state budget.

The Legislative Council staff presented a memorandum entitled *Legislative Fiscal Staff Services Among the States*. The Legislative Council staff said legislative fiscal services provided to state legislatures varies among the states. Some states such as North Dakota, South Dakota, Vermont, West Virginia, and Wyoming have four or five fiscal staff professionals each while Michigan has 46 fiscal staff professionals and Texas has 99 fiscal staff professional positions.

The Legislative Council staff said that 14 of the 50 states provide funding for a legislator to hire the legislator's own full-time professional staff.

The Legislative Council staff reviewed a memorandum entitled *Zero-Base Budgeting* and its use in North Dakota and other states. The Legislative Council staff said the purpose of zero-base budgeting is to reevaluate and reexamine all programs and expenditures for each budgeting cycle by analyzing workload and efficiency measures to determine priorities or alternative levels of funding for each program or expenditure. The Legislative Council staff said that through this

system each program is justified in its entirety each time a new budget is developed.

The Legislative Council staff said during the 1977-78 interim, the Budget Section reviewed zero-base budgeting and although North Dakota did not adopt zero-base budgeting as its primary budgeting tool, a number of its components were incorporated into budget request forms used by agencies over the years in preparation of their budget requests submitted to the Office of Management and Budget and to the Legislative Assembly. The Legislative Council staff said these components include:

1. Preparing decision packages that identify agency services that would be provided at a funding level less than 100 percent of the agency's current funding level, usually 80 or 90 percent.
2. Requiring agencies to submit a 95 percent or 97 percent budget request compared to current funding levels.
3. Ranking agency activities in priority order above a certain level.
4. Identifying program goals and objectives.
5. Explaining the effect of not funding an activity within an agency.

The Legislative Council staff said other states that report utilizing zero-base budgeting to some extent in their budget preparation process are Colorado, Iowa, Nebraska, and Oregon. The Legislative Council staff said Colorado utilizes zero-base budgeting for the preparation of approximately six agency budgets and intends to increase the number of agencies using zero-base budgeting each year. The other three states, Iowa, Nebraska, and Oregon, use a modified zero-base budgeting system that does not require agencies to prioritize all of their programs but only those over a certain percentage of current funding or to prepare reduction decision packages below 100 percent of the current funding level.

Representative Tollefson expressed support for the zero-base budgeting concept. He said it is a good management tool for agencies to utilize in the development of their budget. He noted that some states used both zero-base budgeting and performance budgeting. He said that combining these budgeting systems may provide valuable information for both agencies and the Legislative Assembly in the budgeting process.

Representative Berg indicated that both performance budgeting and zero-base budgeting attempt to achieve the same goal--to examine programs independently to determine benefits received. Using these systems, he said, the Legislative Assembly can make more informed decisions on funding levels for specific programs.

The Legislative Council staff reviewed a memorandum entitled *Legislative Budget* presenting procedures that could be involved in the development of a legislative budget. The Legislative Council staff said the legislative budget would be finalized by the close of the legislative session.

The Legislative Council staff said interim committee responsibilities would be expanded to include the following activities:

1. Monitor the implementation of agency budgets.
2. Conduct selected agency program reviews or studies.
3. Conduct budget tours.
4. Receive agency and public testimony regarding the implementation of the agency's current budget and the development of the next biennial budget.
5. Provide input for agency budget development.
6. Review agency budget requests.
7. Identify major budget issues and priorities.
8. Request specific budget-related information, including alternative budget scenarios.
9. Make observations and report major budget findings.
10. Make budget recommendations either for select agencies or related to all budgets.
11. Monitor revenue collections and be involved in preliminary revenue estimate development.

During the legislative session the Legislative Assembly and Appropriations Committees would have additional resources available to use when determining funding levels for agencies of state government. The Legislative Council staff said these resources would include agency budget requests; the executive budget recommendation; analyses prepared by the legislative fiscal staff during the session; and information included in the Legislative Council's budget report resulting from the interim committee activities that may include legislative budget recommendations and priorities, legislative budget initiatives and priorities, and additional budget-related information including alternative budget scenarios.

Senator Nething indicated that as the committee considers options for preparing a legislative budget, it should address committee size, number of meetings, timeframes, and additional funding that may be necessary. He said as the various interim committees are given agency assignments, there may need to be guidelines developed for interim committees to follow as

they recommend funding levels for agency budgets.

Mr. Chester E. Nelson, Jr., Legislative Budget Analyst and Auditor, commented that under the proposed scenario, the interim committees would not develop specific funding recommendations for a total state budget during the interim but this would continue to be done by the Appropriations Committees during the session. He anticipates the interim committees would focus on major agency issues, legislative concerns, budget initiatives, and alternative budget scenarios during the interim rather than recommending a specific funding level for an entire agency's budget.

Representative Wilkie indicated that during the session much information is provided to legislators relating to agency budgets and it is difficult to find adequate time to review this information. He expressed support for expanding interim committee involvement in the budget process and allowing for legislative input earlier in the budget process.

Senator Nething indicated that an additional benefit to expanding interim committee budget responsibilities is the familiarity with agency budgets that a legislator would gain by serving on an interim budget committee. He said the legislator may subsequently serve on Appropriations Committees for the first time during the next session.

It was moved by Representative Berg, seconded by Senator St. Aubyn, and carried on a voice vote that the Legislative Council staff prepare a bill draft to establish a legislative budget.

Representative Berg suggested a bill draft be prepared incorporating the key points of performance budgeting. After discussion, Representative Berg said it may be possible to incorporate these items in the bill draft requested earlier.

Representative Tollefson expressed support for performance budgeting and indicated that it should be expanded in order to be more effective within state government.

Senator St. Aubyn suggested that if performance budgeting is expanded, legislative staff be involved in reviewing measures and performance and present summary reports to the committees.

Representative Berg indicated that legislative fiscal staff will be a key component of a legislative budget system and that additional staff may be necessary.

Representative Delzer suggested the committee review the number of committees that may be involved, additional staff that may be necessary, and associated costs of developing a legislative budget.

Chairman Nething asked the Legislative Council staff to prepare for the committee's next meeting information on the number of interim committees that may be necessary, timetables, additional staff that may be required, and associated costs for developing a legislative budget.

The committee recessed for lunch at 12:15 p.m. and reconvened at 12:45 p.m.

INVESTMENT PROCESS STUDY

Mr. Steve Cochrane, Investment Director, Retirement and Investment Office, commented on the investments of the bonding fund and fire and tornado fund. Mr. Cochrane said for the eight-month period July 1997 through February 1998 the total return on investments of the bonding fund and fire and tornado fund was 10.5 percent. He said if these returns continue through June 1998 the funds would realize an approximate 15 percent annual return.

Mr. Cochrane said the cash equivalent funds of the bonding fund and fire and tornado fund are invested at the Bank of North Dakota.

A copy of the report is on file in the Legislative Council office.

Representative Kretschmar asked for the annual returns of the bonding fund and fire and tornado fund prior to the new asset allocation policy. Mr. Cochrane said the fire and tornado fund realized a 6.45 percent annual return in fiscal year 1996 and in 1997 after the reallocation the total return was 9.67 percent. He said for the bonding fund, the fiscal year 1996 total return was 6.98 percent and in fiscal year 1997 that increased to 9.49 percent.

Mr. Bob Olson, Fire and Tornado Fund and Bonding Fund Administrator, Insurance Department, commented on the status of the fire and tornado fund and on the status of claims resulting from the 1997 Red River Valley flood.

Mr. Olson said the fire and tornado fund has closed 45 claims and paid \$1.5 million. He said ten claims remain to be finalized including claims from the University of North Dakota and Grand Forks County. He estimates that approximately \$3.5 million will be paid to finalize these 10 claims.

Mr. Olson distributed a report showing information on payments made by the fire and tornado fund on flood claims. A copy of the report is on file in the Legislative Council office.

Senator St. Aubyn asked what effect the flood claims will have on the balance in the fire and tornado fund. Mr. Olson said current projections indicate the fire and tornado fund balance should remain above the \$12 million level. He said if the

fund balance becomes less than \$12 million, the North Dakota Century Code requires the Insurance Commissioner to levy assessments on fire and tornado fund policyholders in order to return the balance to \$12 million.

Mr. Bob Olheiser, Executive Director, Board of University and School Lands, presented a report on the status of investments of the Land Department. Mr. Olheiser said the asset value of the 13 permanent educational trusts increased by \$13.3 million during the six-month period ending December 31, 1997. He said the equity portfolio continues to provide higher than estimated returns.

Mr. Olheiser said the Land Board is intending to increase the percentage of assets invested in equity and convertible securities from the current rate of approximately 40 percent of total assets to 50 or 60 percent over the next eight to 12 years. A copy of the report is on file in the Legislative Council office.

TRANSPORTATION FUNDING STUDY

Mr. Marshall Moore, Director, Department of Transportation, presented information on the status of federal highway funds available to North Dakota and on advanced construction approved for the 1998 construction season.

Mr. Moore said Congress has not yet approved the next federal highway bill. He said under the Senate proposal, North Dakota would receive an estimated \$184 million in federal funding per year which is \$84 million more than the current federal allocation for North Dakota of approximately \$100 million per year. He said under the House bill, North Dakota would receive an estimated \$129 million per year. In addition, he said, the House bill contains over 12,000 demonstration projects which have been identified for special funding. He said the bill contains two demonstration projects for North Dakota totaling \$10 million, a bypass around Jamestown and a project on Highway 52 north of Minot.

Mr. Moore said that because the federal highway bill has not yet been approved, North Dakota is using a concept of advanced construction which utilizes 100 percent state funds for projects in anticipation of federal reimbursement once the federal highway bill is approved. He said North Dakota is planning to use this concept for \$26.5 million of projects this summer.

Mr. Moore said in anticipation of the new federal highway bill, the Department of Transportation is planning for a 1999 construction season based upon a \$130 to \$150 million federal aid program.

A copy of the report is on file in the Legislative Council office.

Mr. Marv Skar, First Vice President, North Dakota Motor Carriers Association, commented on highway funding issues. Mr. Skar said the trucking industry plays a vital role in North Dakota's economy. He said a good transportation system is necessary for the state to attract new industry and sustain economic growth. He expressed support for providing funds to improve the state's highway system and indicated the association's willingness to work with the Legislative Assembly to develop equitable methods of funding infrastructure needs.

Mr. Skar presented a schedule estimating that \$12,956 of federal and state taxes are paid per year on an 80,000-pound tractor semitrailer with an annual mileage of 100,000 miles.

Mr. Skar suggested that the committee consider the following options to provide additional funding for highways in North Dakota:

1. Consider recommending that the 1999 Legislative Assembly appropriate 50 percent of the funding for the Highway Patrol from the general fund and 50 percent from the highway fund rather than the current method of funding the Highway Patrol almost entirely from the highway fund.
2. Move the point of fuel tax collections from the retailer to the terminal. He presented a schedule showing a number of states that have made this change and report an increase in fuel tax collections as a result.

A copy of the report is on file in the Legislative Council office.

Senator Nething asked for the number of fuel terminals in North Dakota. Mr. LeRoy Ernst, Executive Director, North Dakota Motor Carriers Association, indicated that there are fewer than 12 terminals located within North Dakota.

Senator Nething commented that changing the fuel tax collection point from the retailers to the terminals would simplify fuel tax collections.

Representative Wilkie expressed concern regarding this change because farmers would initially pay special fuel taxes when purchasing fuel and would need to file for a refund at the end of the year. He said this change would not benefit farmers.

Representative Delzer indicated that it would be difficult for a farmer's cash flow to pay the fuel taxes when purchasing the fuel and have to wait for up to one year to receive a refund.

Mr. Moore suggested that the Tax Department be asked to comment to the committee at a

future meeting on this concept because of the research it has done regarding this concept.

Chairman Nething asked that the Tax Department, the North Dakota Petroleum Marketers Association, and farmers' organizations be asked to comment at the next committee meeting on changing the point at which fuel is taxed to the terminals.

BUDGET TOUR

The committee traveled to the Youth Correctional Center in Mandan. The committee toured the Youth Correctional Center including the vocational education program, auto tech program, welding shop, Hickory Cottage, Pine Cottage, Centennial Hall, Brown Cottage, the power house, the gym renovation project, and Maple Cottage.

Mr. Al Lick, Director, Division of Juvenile Services, commented on the programs of the Youth Correctional Center. He said the center currently has 98 residents.

Mr. Darrel Nitschke, Superintendent, Youth Correctional Center, commented on the status of the 1997-99 budget and 1999-2001 budget needs. He said the center is authorized 85.89 FTE positions. Because of an acute medical situation for one of the students at the center, Mr. Nitschke said a deficiency appropriation may be requested from the 1999 Legislative Assembly for additional institution medical fees funding.

Regarding the 1999-2001 biennium budget request, Mr. Nitschke said additional funding will be requested to increase salaries of the teachers at the center in accordance with the salary schedule proposed by Central Personnel. Under operating expenses, he said, approximately \$60,000 from the general fund may be requested to continue child psychiatric services at the center for two days per month. He said the center has received grant funding from the Department of Human Services since the 1995-97 biennium for these services but has been informed that the funding may not be available beyond this biennium.

Mr. Lick commented on capital improvement needs at the Youth Correctional Center. He said the 1997 Legislative Assembly approved \$1.4 million of bonding authority to remodel the gymnasium. He said the project is underway and should be completed by late this fall. He said the second phase of the gymnasium project is to construct an addition at an estimated cost of \$1 million. He said \$1.8 million is also needed to construct an addition to Pine Cottage to make it a self-contained unit for the more difficult students at the center. He said of the \$1.8 million, an estimated \$400,000 of federal funds may be available for this project.

Mr. Lick said the department has had discussions with the National Guard and the Department of Transportation to construct a new entrance road to the center. He said the railroad crossing at the current entrance makes it difficult to access the facilities because of the number of trains passing. He said the National Guard would construct a road during the summer of 1999 and the Department of Transportation would pave the road in the fall of 1999 if approved.

A copy of the report is on file in the Legislative Council office.

The committee adjourned subject to the call of the chair at 5:00 p.m.

Allen H. Knudson
Senior Fiscal Analyst

Chester E. Nelson, Jr.
Legislative Budget Analyst and Auditor

ATTACH:1