NORTH DAKOTA LEGISLATIVE MANAGEMENT

Minutes of the

GOVERNMENT FINANCE COMMITTEE

Wednesday, March 7, 2018
Roughrider Room, State Capitol
Bismarck, North Dakota

Senator Ronald Sorvaag, Chairman, called the meeting to order at 10:00 a.m.

Members present: Senators Ronald Sorvaag, John Grabinger, Jordan Kannianen, Lonnie J. Laffen, Gary A. Lee, Terry M. Wanzek; Representatives Rick C. Becker, Joshua A. Boschee, Jeff Delzer, Ron Guggisberg, Craig Headland, Corey Mock, Mike Nathe, Gary Paur, Shannon M. Roers Jones, Mike Schatz, Don Vigesaa

Member absent: Representative Brandy Pyle

Others present: Senator Donald Schaible, Mott, and Representative Jim Schmidt, Huff, members of the Legislative Management
Allen H. Knudson, Legislative Council, Bismarck
See Appendix A for additional persons present.

It was moved by Representative Boschee, seconded by Representative Vigesaa, and carried on a voice vote that the minutes of the December 7, 2017, meeting be approved as distributed.

STATE BUDGET INFORMATION

Mr. Joe Morrissette, Director, Office of Management and Budget, presented information (Appendix B) regarding the status of the general fund and other state budget information. He presented the following information on the preliminary status of the general fund for the 2017-19 biennium to date through February 2018:

Unobligated general fund balance - July 1, 2017		$65,000,000
Add		
Revenues collected to date		1,618,831,805
Remaining forecasted revenues		2,738,522,051
Balance obligated for authorized carryover from the 2015-17 biennium		99,271,093
Total estimated available		$4,521,624,949
Less		
2017-19 biennium general fund ongoing appropriations	($4,295,624,415)	
2017-19 biennium general fund one-time appropriations	(14,638,226)	
Balance obligated for authorized carryover from the 2013-15 biennium	(99,271,093)	
Total appropriations and adjustments		(4,409,533,734)
Estimated general fund balance - June 30, 2019		$112,091,215[1]
[1]North Dakota Century Code Section 54-27.2-02 provides that any end of the biennium balance in excess of $65 million must be transferred to the budget stabilization fund, up to a cap of 15 percent of general fund appropriations.		

Mr. Morrissette said actual general fund revenue collections are slightly more than forecasted. He said $32 million has been transferred to the budget stabilization fund and the balance is $38.3 million and the legacy fund balance is $5.47 billion as of February 2018.

In response to a question from Representative Mock, Mr. Morrissette said of the $438 million in the foundation aid stabilization fund, $105 million is unobligated.

STUDY OF STATE FLEET SERVICES PROVIDED FOR STATE AGENCIES

Ms. Robin Rehborg, Director, State Fleet Services, Department of Transportation, presented information (Appendix C) regarding the Department of Transportation's (DOT) review of information collected from the Government Finance Committee's State Fleet Services (SFS) survey sent to all state agencies and an update on the agencies discussion with Enterprise Holdings Inc. She said SFS policies address many of the comments from the survey, some of the comments are items such as having more four-wheel drive vehicles available which would cost more money. She said DOT has met with representatives from Enterprise Holdings Inc. regarding whether or not a partnership to lease vehicles with the company would create some efficiencies for SFS.

STUDY OF TRANSPORTATION-RELATED FUNDING

At the request of Chairman Sorvaag, Mr. Allen H. Knudson, Legislative Budget Analyst and Auditor, presented a summary (Appendix D) of a report relating to the future of the motor fuel tax presented at the National Conference of State Legislatures' (NCSL) Midwest States Fiscal Leaders Meeting. He said the report indicates with continuing increases in fuel efficiency and a shift to electric vehicles, motor fuel tax revenue will decrease while miles traveled increases. Between 2008 and 2014, he said, the average fuel efficiency of cars increased by 22 percent. He said a Bloomberg energy study of electric vehicles indicates electric vehicles will consist of 34 percent of new vehicle sales by 2040. He said the report indicates that states, in the short term, can increase gas taxes, but this will not solve the growing disparity between fuel consumption and miles traveled, and in the long term, states will need to focus on alternative revenue sources.

In response to a question from Senator Wanzek regarding taxing vehicle miles traveled, Mr. Knudson said discussions at the meeting included self reporting and the use of existing technology to report miles traveled, but there are privacy issues to address regarding using technology to report the number of miles traveled to a government entity.

Senator Laffen commented that a change from a $0.184 per gallon federal tax with a $0.05 per mile tax is a five-fold increase to tax revenue and a $0.01 per mile tax would be comparable to the current federal fuel tax of $0.184.

Representative Paur said companies are exploring the possibility of retrofitting existing vehicles with electric vehicle technology to improve fuel mileage.

In response to a question from Representative Guggisberg, Mr. Knudson said some discussion at the meeting indicated the fee per mile for the vehicle mile traveled (VMT) tax could be based on the weight of the vehicle.

Senator Lee said the State of Oregon has tried to implement a VMT type tax for many years without success. He said in rural states such as North Dakota the cost to the residents is much higher. He said with a VMT tax individuals from out of state do not pay the tax without support from other states.

Mr. Shannon Sauer, Chief Financial Officer, Department of Transportation, presented information (Appendix C) regarding highway tax distribution fund revenues allocated to DOT. He said actual collections are currently slightly higher than projections.

In response to a question from Chairman Sorvaag, Mr. Sauer said DOT has been monitoring the decline in highway tax distribution fund revenue from motor fuel taxes as identified in Mr. Knudson's summary of the NCSL conference.

In response to a question from Representative Delzer, Mr. Sauer said DOT expects federal funding to be consistent with prior bienniums through 2021. He said with the new federal transportation funding program proposed by the President, DOT anticipates a reduction in federal funding.

Representative Guggisberg expressed concern regarding potential federal highway funding changes that will place more financial burden on rural states like North Dakota.

Mr. Sauer said DOT has requested an opinion from the Attorney General regarding the constitutionality of administrative expenses being paid from the highway tax distribution fund revenues.

Representative Becker said he has requested an opinion from the Attorney General regarding the constitutionality of highway tax distribution fund revenues being used for ethanol subsidies.

At the request of Chairman Sorvaag, the Legislative Council staff presented a memorandum entitled *Summary of the Design-Build Construction Method and Public-Private Partnership Construction Method*. The memorandum explains the design-build method of construction and the public-private partnership (P3) method of construction.

Senator Laffen explained that most construction projects in the United States are design-bid-build construction projects where a design firm is hired and the project is submitted for bidding at which time a builder is selected. He said in the design-build construction method, one firm is selected for both the design and construction portions of the project. He said the design-build method of construction is beneficial when cost is less important than time. He said this method removes the bidding process which takes time. He said projects that are revenue generating can work for the design-build method. He said the P3 method of construction is the design-build method with the firm also providing financing. He said this type of project can be attractive when the owner does not have money available. For example, he said, if a toll road is built using the P3 method, the firm designs, builds, finances and enters a long-term contract to operate and collect revenues from the public project. He said for a project like this, what may have taken 5 years to pay for the project is now under a 10-year contract resulting in a more expensive project for the public because of lack of competition and loss of revenues. He said the advantage is the project required minimal initial investment and is completed in a shorter time frame.

Representative Schmidt said the Army Corps of Engineers is recommending the Fargo-Moorhead Area Diversion Project be completed as a P3 project. When initially proposed, he said, the federal government was to provide $800 million and after changing it to a P3 type project the federal share is now $400 million.

Senator Laffen said P3 projects extend project costs over a longer period of time.

STUDY OF REVENUE VOLATILITY

Mr. Justin Kringstad, Director, North Dakota Pipeline Authority, presented information (Appendix E) regarding volatility in the oil and gas industry. He said North Dakota oil is discounted about $4 per barrel in comparison to West Texas Intermediate (WTI) crude oil prices. He said the United States Energy Information Administration's (EIA) domestic oil price outlook through 2018 is expecting WTI crude oil prices to decline because of the expectation that supply will exceed demand. He said he expects prices to remain steady over the next 3 to 4 years and increasing after that time frame. He said North Dakota monthly crude oil production has been trending upwards in calendar year 2017. He said the 2016 weighted average discount was $7.71 and from June 2017 through December 2017 the weighted average discount was $4.53, resulting in a $3.18 per barrel improvement since the Dakota Access Pipeline (DAPL) became operational. He said as a result, $73.1 million in additional state revenue was realized. He said at the current price point per barrel of North Dakota oil, 44 percent of the Bakken Formation is economically viable.

In response to a question from Representative Nathe, Mr. Kringstad said DAPL is considering the possibility of increasing its capacity.

Representative Delzer said the Legislative Assembly has attempted to reduce the effect of volatility in oil revenues by setting up the "bucket system" in which oil revenues are deposited into various funds up to specified amounts. He said the volatility issue is more prevalent with the extent to which oil activity affected sales and use tax revenues.

In response to a question from Representative Delzer, Mr. Kringstad said as WTI oil becomes easier to export, domestic oil prices and global oil prices will synchronize.

In response to a question from Representative Delzer, Mr. Kringstad said the cost of completing an oil well in North Dakota is from $7 million to $7.5 million. He said the cost to complete a well in the Gulf Coast region is less.

In response to a question from Representative Becker, Mr. Knudson said the interim Legislative Revenue Advisory Committee (LRAC) has asked its forecasting consultant, IHS Markit, to forecast revenues under three scenarios that will have confidence levels tied to each scenario.

Representative Delzer said the LRAC has asked IHS Markit to provide its forecasts in dollars in addition to a percentage basis.

Mr. Jon Godfread, Insurance Commissioner, presented information regarding changes in insurance premium tax revenue since the 2011-13 biennium, including major reasons for the changes, and projections for the 2017-19 and 2019-21 bienniums. He said the current fluctuation in insurance tax revenues is due to the timing of collections and by the end of the biennium, collections should be similar to the forecasted amount. He said as changes in property valuations occur in 1 year, the insurance premiums will change the following year resulting in a 1-year lag between valuation changes and changes to insurance tax premiums. He said in 2009 there were 48,000 licensed insurance providers in the state and in 2018 there are 75,000. He said 2019-21 biennium insurance premium tax revenues should be approximately $130 million.

Mr. Ryan Rauschenberger, Tax Commissioner, presented information (Appendix F) regarding the estimated impact of the federal Tax Cuts and Jobs Act of 2017 to the state. He said regarding individuals, there are still seven tax brackets with changes to the tax rates in each bracket, the standard deduction was increased from $6,350 to $12,000 for individuals and from $12,700 to $24,000 for married filling joint returns, personal and dependent exemptions were removed and the child tax credit was increased from $1,000 to $2,000. He said the state and local tax deduction is now limited to $10,000.

Mr. Rauschenberger said the corporate rate effective after December 31, 2017, is now 21 percent compared to a variable schedule. He said a 20 percent passthrough deduction will be allowed for individuals with business income from a qualified passthrough entity which is yet to be determined by the Internal Revenue Service (IRS). He said the department estimates the changes to the federal tax laws will reduce 2019-21 biennium income tax revenues from individuals and corporations by $28.9 million.

In response to a question from Representative Roers Jones, Mr. Rauschenberger said the IRS has 18 items for which it needs to provide guidance on and who qualifies as a passthrough entity is one of those items. He said service providers will most likely not be able to utilize the 20 percent passthrough deduction.

In response to a question from Representative Delzer, Mr. Rauschenberger said changes to the double weighted and single weighted corporate sales apportionment factor is included in the analysis.

Representative Mock requested the Tax Commissioner to provide information regarding the number of corporations selecting the single weighted sales factor.

At the request of Chairman Sorvaag, the Legislative Council staff presented a memorandum entitled *Authority to Purchase Oil and Gas Tax Revenue Put Options*. The memorandum provides information regarding statutory authority to purchase oil and gas tax revenue put options.

Mr. David J. Hunter, Executive Director/CIO, Retirement and Investment Office, presented information (Appendix G) regarding estimated costs of using oil puts to reduce revenue volatility. He said purchasing put options is similar to buying insurance. He said a premium is paid to protect against oil prices dropping. He said if the state would purchase a put option for an oil price of $47 per barrel, the premium cost from July 2019 through June 2020 would be $3.85 per barrel or 8.2 percent per barrel. He provided an example of purchasing WTI crude oil put options cost $48.6 million to protect $1.2 billion of revenue for 18 months.

Representative Paur presented information (Appendix H) regarding Dr. William W. Wilson with the Department of Agribusiness and Applied Economics at North Dakota State University. He requested, and Chairman Sorvaag approved, to ask Dr. Wilson to present information at a future meeting on his study of oil prices, volatility, and risk for government budget revenues.

At the request of Chairman Sorvaag, the Legislative Council staff presented a memorandum entitled *Summary of Utah's Budget Stress Testing*. The memorandum provides information regarding Utah's experience in stress testing its state budget.

OTHER DUTIES OF THE GOVERNMENT FINANCE COMMITTEE

Mr. Brad Darr, Maintenance Division Director, Department of Transportation, reported (Appendix C) on the results of DOT's study of options to consolidate transportation facilities within Williams County and the Williston district headquarters, pursuant to Section 11 of 2017 Senate Bill No. 2012. He said based on the study's findings, it was determined the consolidation of facilities would not be beneficial due to the cost of the infrastructure needed.

Representative Vigessa suggested that DOT provide an update on highway maintenance site closings along with driver's license service site closings, including the effect on services.

Representative Mock suggested DOT be asked to provide statistics to show the effect of the sites closing.

In response to a question from Representative Vigessa, Mr. Darr said the following political subdivisions are or are planning to operate highway maintenance sites which were selected to be closed by DOT--Hettinger County, the City of Gackle, and the City of Starkweather. He said highway maintenance sites closed by DOT in the following areas are not being operated by the political subdivisions--Courtenay, Litchville, and Steele County. He said DOT is still operating the Hillsboro site, but the political subdivisions in the area are not interested in operating the site.

In response to a question from Senator Wanzek, Mr. Darr said vehicles had been staged in areas where highway maintenance sites were closed in preparation for major snowfall. He said DOT will be reporting its findings from its snow and ice control study as soon as it is complete.

In response to a question from Representative Delzer, Mr. Mark Nelson, Deputy Director for Driver and Vehicle Services/Business Support, Department of Transportation, said DOT has not received any information from the public regarding the closing of driver's license service sites, which went into effect in August 2017.

Chairman Sorvaag asked that DOT report to the committee at its next meeting on DOT's cost to produce driver's licenses, the cost for the driver's license test, and vehicle license plates in comparison to fees charged for such services.

Representative Becker suggested DOT include in its information any changes to the cost to produce a driver's license based on the length of time a license is effective.

In response to a question from Representative Schaible, Mr. Nelson said 30 to 31 percent of driver's licenses are renewed online.

In response to a question from Representative Nathe, Mr. Nelson said DOT is expanding its kiosk program.

No further business appearing, Chairman Sorvaag adjourned the meeting at 2:53 p.m.

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Chris Kadrmas
Fiscal Analyst

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