NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

BUDGET COMMITTEE ON GOVERNMENT FINANCE

Tuesday, October 21, 1997
Harvest Room, State Capitol
Bismarck, North Dakota

Senator David E. Nething, Chairman, called the meeting to order at 8:30 a.m.

Members present: Senators David E. Nething, Rod St. Aubyn, Bob Stenehjem, Harvey D. Tallackson; Representatives Jeff W. Delzer, Bette Grande, Roy Hausauer, Matthew M. Klein, William E. Kretschmar, Ronald Nichols, Elwood Thorpe, Gerry Wilkie

Members absent: Representatives Rick Berg, Keith Kempenich, Ben Tollefson

Others present: See attached appendix

It was moved by Senator Tallackson, seconded by Senator St. Aubyn, and carried on a voice vote that the minutes of the previous meeting be approved as mailed.

GENERAL FUND STATUS

Mr. Rod Backman, Director, Office of Management and Budget, presented a report on the status of the general fund. Mr. Backman said the 1997-99 biennium revenues through September have exceeded forecast by $5.1 million or 3.2 percent. He said the largest favorable variances were in corporate income tax, individual income tax, and motor vehicle excise tax collections. As a result, Mr. Backman said the projected general fund balance on June 30, 1999, is estimated to be $16 million compared to the $10.9 million projected by the 1997 Legislative Assembly. Mr. Backman said while revenues have exceeded estimates for the first three months of this biennium, other factors which may require funding and which may affect future revenues need to be considered, including the additional funding that will be needed as a result of the 1997 flood in the Red River Valley and that gross income from wheat production is estimated to decrease by $400 million for the 1997 growing season.

Mr. Backman reviewed economic activity in North Dakota and the major provisions of the 1997 federal Taxpayer Relief Act. He said the Act allows a $400 child care credit in 1998 which for North Dakota will amount to an estimated $50 million and a $500 child care tax credit in 1999 which, in North Dakota, will amount to an estimated $63 million.

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

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 that through August 1997 oil and gas production tax collections have exceeded estimates by $99,000 and oil extraction tax collections have been less than projections by $402,000.

Mr. Kramer said oil production for July 1997 was 105,000 barrels more than projected; however, the average market price for the first three months of the biennium has ranged from $1.56 to $1.78 less than projections.

Senator St. Aubyn asked the Legislative Council staff to research whether any activity has resulted from the 1997 Legislative Assembly providing an oil extraction tax exemption for a period of 60 months on land within an Indian reservation. Mr. Kramer said the staff would research the question and provide the information to the committee.

Representative Kretschmar asked the Legislative Council staff to research the amount of oil extraction tax collections transferred to the common schools trust fund as a result of the constitutional amendment approved by the voters in 1994. Mr. Kramer said that information will be provided to the committee.

BUDGET PROCESS STUDY

The Legislative Council staff presented a memorandum entitled *Budgeting Methods in North Dakota and Other States*. The Legislative Council staff said the memorandum provides information on budgeting methods used in North Dakota, Arizona, Colorado, Iowa, Minnesota, Montana, New Hampshire, New Mexico, Oklahoma, South Dakota, Wisconsin, and Wyoming. The information is organized into the following major categories:

1. General budgeting methods.

2. Legislative budget systems.
3. Revenue forecasting.
4. Appropriations bills.
5. Performance measures.
6. Agency flexibility to move funds between line items.
7. Unspent appropriation authority at the end of a budget cycle.
8. Budget monitoring or program reviews conducted between legislative sessions.

The Legislative Council staff reviewed the general budgeting methods among the states and reported that three of the 12 states have biennial legislative sessions and seven of the 12 approve biennial budgets. The Legislative Council staff said that in the majority of the states the executive budget is not presented until the legislature begins its regular session while in North Dakota, South Dakota, and Wyoming the executive budget is presented a month before the regular session begins. The Legislative Council staff reported the primary budgeting method used in the majority of these states is incremental, the same as in North Dakota. Incremental budgeting begins with the current budget level for an agency and any change to that must be explained and justified.

The Legislative Council staff reviewed three states that prepare legislative budgets in addition to the executive budget. The states include Arizona, Colorado, and New Mexico.

The Legislative Council staff said that in Arizona the legislative budget is prepared primarily by legislative staff and leadership from September through December before the legislative session. Legislative staff members meet with agencies in the development of the budget, but no formal hearings are held. Both the executive recommendation and the legislative budget are presented to the legislature during the first week of the regular session.

In Colorado, a Joint Budget Committee, consisting of six members, including the chairman of the House and Senate Appropriations Committees and one majority and one minority member from each Appropriations Committee, is responsible for developing the legislative budget. The executive budget recommendation is presented to the joint committee in November of each year. The executive budget is the starting point for the Joint Budget Committee to develop its legislative budget. The Joint Budget Committee develops its budget from November through March by meeting three to four days per week. The legislature is generally in session from January through April of each year. The Joint Budget Committee holds two sessions of hearings. The first, from November through December, involves agencies explaining the executive recommendation, and the second, from January through March, involves the Governor's office responding to Joint Budget Committee recommendations on behalf of agencies and public testimony on the budget recommendations. The Joint Budget Committee concludes its work by the end of March at which time it prepares the appropriation bill for introduction. The appropriation bill is referred to the Appropriations Committees and although the Appropriations Committees could change the bill, they never have. The bill, however, is sometimes amended on the floor.

In New Mexico, the legislative budget is prepared from September through December of each year preceding the legislative session by an interim Legislative Finance Committee consisting of 16 members appointed by the Speaker of the House and President of the Senate and includes the House and Senate Appropriations Committee chairmen. The committee meets three to four days per week from September through December to develop the budget with the assistance of the legislative fiscal staff. The Legislative Finance Committee holds public hearings from September through December which are open to the public as it develops the legislative budget. The committee provides budget guidelines to the legislative staff and the staff uses these guidelines to develop the budget recommendations for each agency which are then approved by the committee. Both the executive and legislative budgets are presented to the legislature on the first day of the regular session which begins in January.

Senator Nething asked the Legislative Council staff to determine how states that develop legislative budgets determine funding levels in the proposed budget for the legislative branch and the judicial branch, which in North Dakota are not changed in the development of the executive budget recommendation.

The Legislative Council staff reviewed methods used in each of the states for projecting state revenues for use in developing the state budget. The Legislative Council staff said that in five of the 12 states, the legislative branch develops its own revenue forecast in addition to the forecast developed by the executive branch. The Legislative Council staff said that in five of the 12 states, a consensus or other group is responsible for developing the revenue forecast and in most of these states, the amount may not be changed by the legislature. In three of the states, Colorado, Montana, and New Hampshire, the revenue forecast is included in a bill or resolution which is introduced to the legislature and referred to committees for public hearings and the bill or resolution may be amended by the legislature in order to change the revenue forecast.

Representative Kretschmar asked the Legislative Council staff to prepare information showing a history of actual revenue collections in North Dakota to legislative estimates. Chairman Nething indicated that the staff would be asked to prepare this information for presentation to the committee at a future meeting.

Mr. Chester E. Nelson, Jr., Legislative Budget Analyst and Auditor, said the Office of Management and Budget invites legislative input into the early discussions of the revenue forecast, which involves reviewing economic assumptions to be used in the development of the forecast.

The Legislative Council staff reviewed information on funding amounts included in appropriation bills when introduced, the type of line items in the appropriation bills, and the level of detail included in the appropriation bills. The Legislative Council staff said eight of the 12 states contacted consider one major appropriation bill, while the other four, including North Dakota, consider a number of appropriation bills. Regarding amounts that are included in the appropriation bills when introduced, the Legislative Council staff said that in six states, including North Dakota, the executive budget recommended amounts are the amounts contained in the appropriation bill when introduced. In the other states, the Appropriations Committees prepare the appropriation bills after agency budget hearings are held. Regarding the types of line items and detail included in the appropriation bills, three states, including North Dakota, appropriate funds by object code (salaries and wages, operating expenses, etc.) to an agency or major division of an agency. Five states appropriate funds by program to an agency or major division of an agency. Two states appropriate funds by object code for each program of an agency or major division of an agency, and two states use a variety of detail to appropriate funds to agencies ranging from lump sum appropriations for an agency to a number of object codes for a program of an agency.

The Legislative Council staff reviewed the status among the states of the development of performance measures in the budgeting process, the use of the performance measures by legislators, and extent to which performance measures are monitored and how the results are reported to the legislature. The Legislative Council staff said that all 12 states, to some extent, are utilizing performance measures. In some states, state law requires agencies to develop performance measures while in others it is a part of the budget preparation process. The Legislative Council staff said while performance measures are a more recent development in most states and a few of the states indicated that the measures may be used more in the future, most states indicated that the performance measure information is not being used as anticipated when the performance measure concept was first initiated. The Legislative Council staff said the responses varied among the states regarding the extent to which the performance measure information is used. The majority of the states reported the legislature does not utilize the information even though the agencies prepare it; however, Montana reported that 13 state agencies are involved in a performance budgeting pilot project and for these agencies, the performance measures are included in the agency's appropriation bill.

Senator St. Aubyn asked how the performance measure information can be utilized by legislators. Mr. Nelson indicated that because of time restraints legislators experience during the legislative session, legislators may not be able to use the information as much as they would like. He anticipates that although performance budgeting may not continue in its current format, some aspects of the performance budgeting concept may be incorporated into the traditional budget process.

Senator Nething said the performance measure information may be useful to agencies whether or not the Legislative Assembly uses the information.

The Legislative Council staff reviewed the flexibility agencies have among the states to move funds between line items after an appropriation has been approved by the legislature. The Legislative Council staff said five states allow agencies to transfer funds between line items with executive branch approval only, while four states allow agencies to transfer funds between line items with legislative branch approval only. Two states require approval by both the executive and legislative branches.

The Legislative Council staff reviewed the status among the states of unspent agency appropriation authority remaining at the end of a budget cycle. The Legislative Council staff said that in nine of the 12 states, including North Dakota, any unexpended appropriation authority is canceled at the close of the budget cycle unless an exemption is provided by the legislature. In Iowa, an agency may retain 25 percent of its unspent appropriation authority that relates to the agency's general operating costs as determined by the Department of Management for technology improvements during the next fiscal year. In Oklahoma, agencies may continue any unspent annual appropriations; however, the estimated amount of the unspent authority is identified and used to reduce the next fiscal year's appropriation. In South Dakota, any unspent general fund appropriation authority may be continued for one year to pay for contractual obligations as approved by the Bureau of Finance and Management; however, any other unspent general fund authority is canceled at the close of the budget cycle and funds in the amount of the unspent general fund authority are transferred to a budget reserve fund (rainy day fund) up to a cumulative maximum of five percent of the state's general fund appropriation.

The Legislative Council staff reviewed the extent to which legislatures monitor agency expenditures between sessions and review and evaluate agency programs. The Legislative Council staff said the amount of legislative monitoring of agency expenditures and evaluating agency programs varies among the states. Some states like Montana, Oklahoma, and South Dakota do minimal monitoring and no evaluating of programs, while other states have either legislative audit staffs to conduct performance reviews or program evaluation staffs to conduct program evaluations. North Dakota utilizes its fiscal staff to conduct agency visits and to prepare reports on compliance with legislative intent and assigns an interim committee to monitor major state agency expenditures between legislative sessions. In Arizona, the Legislative Council staff said the Joint Legislative Budget Committee staff and the Governor's budget staff conduct program authorization reviews of state agency programs between sessions to determine their effectiveness. The review involves an agency program self-assessment and a program analysis by both the Joint Legislative Budget Committee staff and the Governor's budget staff. A joint report is prepared and presented to the interim Legislative Program Authorization Review Committee and the committee determines whether any legislation should be introduced affecting the program.

The Legislative Council staff presented a memorandum entitled *Budget Process Study - Issues, Examples, and Options*, which provides information on the major budget areas identified in the resolution directing the budget process study to be addressed by the committee. The major areas include:

1. Feasibility of developing a legislative budget.
2. Agency unspent appropriation authority.
3. Effect of budget recommendations on future budgets for possible benefits of new technology on budget development and budget presentations.
4. Types of information to support budgets, including information provided on fiscal notes.
5. Other areas, including budgeting timelines, revenue forecasting, appropriation bills, appropriation committee hearings, performance measures, agency flexibility to move funds between line items, and budget monitoring or program evaluations.

Chairman Nething commented on the feasibility of a legislative budget. He asked that the staff provide additional information on the states that prepare legislative budgets, including:

1. How legislators, other than those on Appropriations, are more involved in the budgeting process.
2. The amount of time legislators spend on the legislative budget.
3. How legislative staff could be involved to a greater extent in developing the information and reporting to an overview committee.

Senator St. Aubyn expressed concern regarding the amount of time legislators now spend on agency budgets during the legislative session. He suggested any additional time spent on agency budgets would benefit the legislative process.

Senator Nething suggested that more agency budget discussions be conducted prior to the session because of the time pressures during legislative sessions.

Representative Klein expressed concern regarding the Colorado system that involves only six legislators in the development of the legislative budget.

Senator Nething commented on the items that affect future budgets, including one-time revenues, one-time expenditures, new program expenditures, discontinued program expenditures, leases or other contractual obligations, and delayed effective date legislation. He suggested this information would assist legislators when developing the state budget and suggested that better ways to present this information be considered.

Senator Nething expressed concern regarding the information provided on fiscal notes. He suggested the information could be presented more clearly in some instances and that the information could be reviewed more closely to determine the accuracy of the fiscal note.

Senator St. Aubyn asked the staff to review how other states develop fiscal notes and how the assumptions used in the fiscal note are debated. Chairman Nething indicated this information will be provided by staff at a future meeting.

Mr. Nelson said that currently, by motion of a committee or by request of a legislator, the Legislative Council fiscal staff can develop alternative scenarios based on the fiscal note information. In addition, Mr. Nelson said on fiscal notes that affect the legislative budget status system, both the Legislative Council fiscal staff and Office of Management and Budget staff discuss and review the fiscal note information.

Chairman Nething asked the Legislative Council staff to review other states' methods of preparing fiscal notes and the extent to which other states include the impact on local governments.

Senator St. Aubyn indicated that the budget information available on-line is adequate; however, the process of accessing the information could be improved.

Senator Nething commented on the budget monitoring and program evaluation systems. Senator Nething expressed support for the budget tours and suggested that options be considered to enhance budget tours and to strengthen the budget monitoring system in order to inform more legislators on agency budgets.

Mr. Nelson said that in his discussions with legislators regarding the feasibility of a legislative budget, a major concern expressed is the difficulty in recommending programs that differ from those included in the executive budget primarily because of the way a change is reported in relation to the executive budget. From a legislative perspective, he said, priorities may differ from the executive budget. He suggested the committee may wish to consider how these should be reported in legislative documents.

Senator Nething suggested any new programs included in the executive budget be identified separately. This could allow legislative programs to be proposed as an alternative.

Senator Nething said how budget information is received and transferred to other legislators is a key area that needs to be addressed.

Mr. Nelson commented on the legislative intent report prepared by the fiscal staff. He asked committee members to inform the staff of any areas that should be included in the report.

Representative Nichols asked that the legislative intent report address the status of funding increases provided to the Department of Human Services for direct care staff salary increases.

Senator Nething suggested the report include the effectiveness of the higher education salary pool approved by the 1997 Legislative Assembly.

Ms. Arvy Smith, Budget Analyst, Office of Management and Budget, presented information on agency performance measures in North Dakota. Ms. Smith reviewed the development of the statewide strategic plan used as a basis for developing the performance measures for each agency involved in the pilot project. Ms. Smith said the Office of Management and Budget used the Texas strategic plan as a model in developing North Dakota's plan. Ms. Smith said although the state has not received substantial resident or customer input in the development of the plan, more input will be sought if performance budgeting becomes the primary budgeting method for the state.

Ms. Smith addressed how the performance measure information is used. She said agency personnel, Office of Management and Budget staff, and legislators should use the performance measure information when making decisions on how to use state resources. She said the performance measure information is used by agencies to assist in obtaining federal grants and by the Office of Management and Budget in the development of the executive budget recommendation. She said legislators are indirectly using the information by the questions they ask agencies to respond to. Ms. Smith said without the structure of the performance budgeting system, there is no consistent method to determine whether agency programs are within the state vision.

Ms. Smith reviewed information included in performance reports of Central Services, Land Department, and Parks and Recreation Department. The information provided comparisons of actual agency performance to performance measure estimates.

Ms. Smith said legislative decisions on agency funding should be related to the effect the funding decision has on the performance of the agency.

Senator Nething asked how actual performance information is compiled. Mr. Jim Kapp, Director, Central Services, reported that Central Services sends customer surveys and based on the information included in the surveys returned, it compiles its actual information for applicable measures.

Senator Nething asked whether performance budgeting may be a short-term budgeting method used by states. Ms. Smith believes performance budgeting is not a short-term budgeting method. She said performance budgeting is being extensively studied by universities and other organizations. She said although the Government

Accounting Standards Board is not mandating performance budgeting, it is defining and setting guidelines on performance measures. In addition, she said, the federal government is moving toward performance measure budgeting for its agencies.

Senator St. Aubyn expressed concern that the Legislative Assembly will have available only one year's actual data for the most recent biennium to evaluate when making budget decisions during legislative sessions. He said the performance budgeting system may be more appropriate as a tool for the Office of Management and Budget or other agencies.

The committee recessed for lunch at 12:15 p.m. and reconvened at 1:00 p.m.

INVESTMENT PROCESS STUDY

The Legislative Council staff presented a memorandum entitled *1995-96 Investment Study Findings,* which reviews the 1995-96 interim Budget Committee on Government Finance study of state investments. The Legislative Council staff said the committee conducted a survey of state agencies and asked for suggestions to improve investment returns on state investments. Major suggestions included:

1. Allow for additional investment options.
2. Change the responsibility for investing funds.
3. Be allowed to keep more or all of the earnings on the fund instead of the earnings going to the general fund.
4. Increase the interest rates at the Bank of North Dakota.

The Legislative Council staff reviewed interest rates paid by the Bank of North Dakota, which during the 1995-97 biennium were slightly higher or very close to the average North Dakota financial institution and slightly less than the United States Treasury rates.

Representative Kretschmar indicated he was a member of the 1995-96 interim committee that conducted this study and said the committee chose not to change the current policy requiring state funds to be deposited at the Bank of North Dakota.

The Legislative Council staff reviewed a memorandum entitled *Fire and Tornado Fund and Bonding Fund - Assessments, Premium Waivers, and Loan Options*. The Legislative Council staff said state statute provides that if the balance in the fire and tornado fund is less than $12 million, the Insurance Commissioner shall levy an assessment against every policy in effect in accordance with the formula included in the section. The Legislative Council staff said the Insurance Commissioner would calculate the amount necessary to provide a $12 million balance in the fund and increase the premium on each policy of the fund for the next year by the percentage necessary to return the fund to the $12 million level.

The Legislative Council staff said if the balance in the bonding fund drops below $2.5 million, premiums, as determined by the Insurance Commissioner, must be collected until the fund balance is $3 million, at which time the premiums are waived. Currently, the Legislative Council staff said, premiums are not charged on the bonding fund because the balance is above the $2.5 million level.

The Legislative Council staff reviewed an option for increasing investment returns on the fire and tornado fund and bonding fund. The Legislative Council staff suggested that provisions could be added in statute that would enable the Insurance Commissioner to invest more fire and tornado fund and bonding fund moneys in longer term investments by authorizing the Insurance Commissioner to obtain loans from the Bank of North Dakota to pay major claims or other major payments which may arise until the moneys invested are available.

The Legislative Council staff presented schedules of bonding fund and fire and tornado fund claims and fund balances since 1991.

Senator St. Aubyn asked the Legislative Council staff to determine the reasons for the substantial increases in fire and tornado fund claims in fiscal years 1995 and 1996. Chairman Nething asked the staff to provide this information when available.

Senator St. Aubyn asked the Legislative Council staff to develop a sample scenario to determine whether the loan option suggested by the staff could result in additional investment income to the bonding fund and fire and tornado fund. Chairman Nething said this information would be provided at a future meeting.

Mr. Ken Rood, Insurance Department, commented on fire and tornado fund and bonding fund investments. He said the Insurance Department works with the State Investment Board in investing these funds. He said Mr. Scott Engmann, Executive Director, State Investment Board, would be providing information on the specific investment policies relating to the investments of the fire and tornado fund and bonding fund.

Mr. Engmann said the State Investment Board has pooled the moneys of the various insurance-related funds, including the fire and tornado fund and bonding fund, into an insurance trust pool which will enable the State Investment Board to improve investment returns on these funds by having a larger pool of funds to meet cash flow needs. He said on August 1, 1997, the State Investment Board began investing funds under its new investment policy. He said the new policy, while still fiscally conservative, is more aggressive in its investments of these funds which should improve investment returns. Mr. Engmann presented information on investment returns of the fire and tornado fund and bonding fund for the first two months of fiscal year 1998. He said while investment returns may vary for the remainder of the fiscal year, if the first two months' returns remained constant for the remainder of the year, the fire and tornado fund and bonding fund would realize fiscal year 1998 returns of 13 to 14 percent. A copy of the report is on file in the Legislative Council office.

Representative Grande asked that the State Investment Board provide additional information at a future meeting on the specific types of investments and the duration of the investments.

Representative Klein indicated that the investment policy on these funds has been substantially changed. He asked what led to these policy changes. Mr. Engmann said the Insurance Department and State Investment Board staffs met and, with the assistance of a consultant, developed various investment policy scenarios which would meet the investment goals and yet maintain safety and liquidity of the funds to meet statutory requirements. He said the new policy is the result of these discussions.

Representative Klein asked for the number of investment managers used by the State Investment Board and how many are based in North Dakota. Mr. Engmann said the State Investment Board utilizes approximately 15 investment managers and only the Bank of North Dakota is based in the state.

The Legislative Council staff asked whether the State Investment Board believes the loan option suggested by the Legislative Council staff could potentially increase investment returns for these funds. Mr. Engmann said the loan option should be considered by the committee. He believes it could affect the cash flow needs of these funds.

Mr. Bob Olheiser, Executive Director, Board of University and School Lands, presented a status report on the investments of the Land Department. Mr. Olheiser said the long-range goal of Land Department investments is to increase both principal and income at a rate greater than or equal to the rate of inflation. He said in order to accomplish this goal, the board intends, over the next eight to 12 years, to increase the percentage of assets invested in equity and convertible securities from the current rate of approximately 39 percent of total assets to approximately 50 to 60 percent. Mr. Olheiser said the board is currently meeting or exceeding its investment goals.

Mr. Olheiser said the board values its fixed income securities at cost and other investments at market.

Representative Grande expressed concern that the board values its fixed income investments at cost rather than market. Mr. Olheiser indicated the board relies on the income of the securities or loans and because it does not plan to sell these, the current market value of these instruments is not important to the Land Board.

Representative Grande expressed concern that the Land Board is investing approximately 40 percent of its equity funds in small capital companies.

Mr. Olheiser said the Land Board has chosen to be more aggressive in these investments because it has other funds to utilize for meeting cash flow needs so it will not be forced to sell at a time which will not benefit the funds.

Representative Klein asked that the Land Board provide additional information to the committee on each of its asset managers, including information on the management fee paid, return on equity to asset ratio, and asset turnover ratio. Chairman Nething asked that the Land Department make this information available to the committee.

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

Mr. John Hoeven, President, Bank of North Dakota, presented information on state investments at the Bank of North Dakota. Mr. Hoeven said Bank of North Dakota interest rates paid on state deposits are competitive compared to interest rates paid by other North Dakota financial institutions and on United States Treasury instruments. The schedule below compares the Bank of North Dakota rates to other North Dakota financial institutions and the United States Treasury:

Length of Investment	Average North Dakota Financial Institution	Bank of North Dakota	United States Treasury Rates
90 days	4.38%	4.13%	5.10%
180 days	5.18%	4.29%	5.26%
One year	5.34%	5.50%	5.42%
Two years	5.61%	5.75%	5.73%
Three years	5.78%	5.85%	5.81%
Four years	5.85%	5.90%	5.87%
Five years	6.00%	6.00%	5.92%

Mr. Hoeven said because Bank of North Dakota profits are transferred to the general fund, based on the Bank of North Dakota's 1996 earnings, the state will receive an additional 7.5 percent return on its investments. A copy of the report is on file in the Legislative Council office.

TRANSPORTATION FUNDING STUDY

The Legislative Council staff presented a memorandum entitled *Highway Revenue Distributions - 1997-99 Biennium*. The Legislative Council staff reviewed the sources and uses of funds in the highway tax distribution fund and the highway fund.

The Legislative Council staff said that four major revenue sources provide funds to the highway tax distribution fund--gasoline and gasohol taxes, motor vehicle registration fees, special fuels tax, and special fuels excise tax. Funds are distributed from the highway tax distribution fund to the highway fund, counties, cities, Game and Fish Department, Parks and Recreation Department, and the Agricultural Products Utilization Commission.

The Legislative Council staff said the major sources of funds for the highway fund are the distribution from the highway tax distribution fund, truck registration fees, driver's license fees, and other sources. For the 1997-99 biennium, the state highway fund is the source of funding for the Department of Transportation and the Highway Patrol.

At the request of Chairman Nething, the Legislative Council staff reviewed a memorandum entitled *Department of Transportation Aircraft Evaluation.* The Legislative Council staff said the 1997 Legislative Assembly provided that the Department of Transportation evaluate the continued use of its 1978 model Cessna airplane. The evaluation is to include an analysis of the cost of continued maintenance and repair of the plane and options for replacement which may include selling or trading the airplane and leasing or purchasing a new or used airplane. The department is to present a report on its evaluation to the Budget Section by November 1998. The Legislative Council staff said the department has begun its cost study and has projected that two engines will need to be replaced in three to four years at an estimated cost of $126,000. The department is currently not planning to purchase a different airplane during this biennium, but consideration may be given to leasing a different airplane. The department plans to continue its evaluation and develop a recommendation in the next few months to be presented to the Budget Section.

Mr. Marshall Moore, Director, Department of Transportation, presented a report on the department's analysis of the statewide transportation system, status of the multistate infrastructure bank, and on the status of federal funds available to North Dakota for highway construction projects.

Mr. Moore said the highway fund balance on October 17, 1997, was zero. He said the department has asked the Industrial Commission for a $10 million line of credit as authorized in the Century Code. He believes this amount should be adequate to meet cash flow needs of the department.

Mr. Moore said as part of the Governor's state of the state address, the Governor indicated that the department would be working with cities and counties to analyze the statewide transportation system. He said the department is just beginning to conduct this study since the 1997 construction season is now coming to a close.

Mr. Moore commented on the multistate infrastructure bank. He said the Department of Transportation is working with the states of South Dakota, Nebraska, and Wyoming on developing the bank to assist in financing transportation projects. He said the department is currently waiting for Federal Highway Administration approval of the project. He said if approved, North Dakota will receive a $1.7 million grant to begin the infrastructure bank. North Dakota would need to provide approximately $430,000 of state matching funds.

Regarding federal funding proposals, Mr. Moore said the Intermodal Surface Transportation Efficiency Act expired on September 30, 1997; however, a continuing resolution has been approved. He said both the House and Senate are developing their own transportation bills. He said the House bill would lower North Dakota's share of federal highway funding from the current allocation of approximately .62 percent to approximately .48 percent. He said under this proposal, North Dakota would receive approximately $116 million per year.

In the Senate, Mr. Moore said North Dakota's share would increase to approximately .73 percent and would receive approximately $161 million per year of federal highway funds. Mr. Moore anticipates that neither bill will pass in its existing form but major compromises will occur to resolve the funding issue.

Mr. Moore reviewed the highway construction projects for 1998, 1999, and 2000. He presented the following schedule providing average improvement costs on the state highway system:

Improvement	Cost Per Mile (1996)
Sealcoat (by contract)	$12,000
Four-inch asphalt overlay	$150,000
Asphalt surfacing reconstruction (includes subgrade repair and resurfacing)	$370,000
Total reconstruction (includes grading and asphalt surfacing)	$500,000
Interstate concrete recycling (two lanes in one direction)	$900,000

Mr. Moore said the department plans on making 151 miles of improvements to the state highway system in 1998, 142 miles in 1999, and 152 miles in 2000. He said in order to maintain a 20-year cycle for highway improvements, the state should be improving approximately 400 miles per year.

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

Representative Thorpe asked for an overview on how the Department of Transportation prioritizes its highway construction projects, including the criteria used. Chairman Nething asked the department to provide this information at a future meeting.

Senator Stenehjem asked for a list of urban projects planned for the next three years and for a history of the gallons of fuel taxed in North Dakota. Mr. Moore indicated the department would provide this information.

Senator St. Aubyn asked when the department's analysis of the current highway system will be completed. Mr. Moore said the department's goal is to complete the study by June 1, 1998.

Representative Thorpe asked whether the trucking industry is paying appropriate fees in North Dakota compared to neighboring states. Mr. Moore indicated the department will provide information on licensing fees among surrounding states and North Dakota.

Senator Stenehjem expressed concern regarding the lack of highway funding in North Dakota. He said the committee needs to consider all funding options, not only increasing fuel taxes. He suggested the committee could consider recommending reprioritizing the use of funds currently collected. He indicated $98.5 million is deposited in the general fund from motor vehicle excise tax collections that could potentially be used for highway projects.

Chairman Nething announced that the next committee meeting is tentatively scheduled for Wednesday, January 14, 1998, in Bismarck.

The committee adjourned subject to the call of the chair at 3:30 p.m.

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Allen H. Knudson
Senior Fiscal Analyst

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

ATTACH:1