



## TRANSFER OF LEGACY FUND EARNINGS

### POTENTIAL CONCERNS WITH THE CURRENT ADMINISTRATIVE PROCESS

- **Cashflow** - Even though the earnings are transferred to the general fund on the last day of the biennium, the funding associated with the earnings is included in the current biennial budget as revenue; therefore, the earnings may be appropriated and spent up to 24 months before the cash from the earnings is available to pay for the expenditures. This could result in the general fund having insufficient cash to pay for the expenditures. This issue will become more of a concern as the earnings become a greater share of state revenues.
- **Budgeting** - Under the current process, the Legislative Assembly must finalize the revised revenue forecast for the current biennium as well as develop the state budget for the next biennium prior to the earnings amount being known. Because the earnings are generated from the performance of investments, the earnings can be volatile making it difficult to determine a reasonable and reliable estimate. Any significant variance in the earnings affects the budgets of both bienniums.
- **General fund balance** - Because the earnings are recognized as part of the current general fund budget in which the earnings are transferred on the last day, if the investments experience losses in the last couple months of the biennium, the final general fund balance could become negative which would require the Governor to direct agencies to reduce budgets in the final days of the biennium. Alternatively, the general fund could have a large surplus if the investments of the legacy fund experience gains in the last couple months of the biennium.
- **Replacing oil revenues** - The primary purpose of the fund is to replace oil and gas tax revenues when oil and gas development activity decreases. Legacy fund earnings may not be sufficient to replace declining oil and gas tax revenues if the earnings are fully committed to supporting ongoing spending items before oil production declines.
- **Appropriate use of legacy fund earnings** - The committee is studying the potential uses of legacy fund earnings, which includes consideration of how the earnings can be used for the state's current and future needs.

### POTENTIAL BENEFITS OF USING A SPECIAL FUND

- **Cashflow** - Transferring the legacy fund earnings to a special fund removes the funding from the general fund budget and provides a cash balance for spending in the subsequent biennium. As a result, the cashflow should be sufficient to pay for the expenditures.
- **Budgeting** - Using the percent of market value based on historical fund values to calculate the amount available to be spent from the special fund allows the Legislative Assembly to budget with known amounts rather than estimates. Although investment earnings can vary significantly, the general fund budget would not be directly impacted by changes in the investment earnings that occur after the calculation.
- **General fund balance** - The general fund balance would not be directly impacted by the legacy fund earnings if the legacy earnings are transferred to a special fund. As a result, any potential shortfall or surplus in the general fund would not be attributed to the legacy fund earnings.
- **Replacing oil revenues** - Separating the legacy fund earnings from the general fund budget allows the Legislative Assembly to identify the spending of the earnings and may help to ensure the spending levels are balanced with the need to replace declining oil and gas tax revenues.
- **Appropriate use of legacy fund earnings** - If the earnings are transferred to a special fund, the Legislative Assembly will be able to identify the spending of legacy fund earnings and will be able to evaluate the appropriateness of the spending.

### **CONSTITUTIONAL RESTRICTIONS**

The State Treasurer is required to transfer the earnings of the legacy fund to the general fund at the end of each biennium pursuant to Section 26 of Article X of the Constitution of North Dakota. After the earnings are transferred to the general fund, the Legislative Assembly may appropriate or transfer the funding for any legally authorized purpose. The constitution does not limit the purposes for using the legacy fund earnings after the earnings are transferred to the general fund. As a result, the legacy fund earnings may be transferred to a special fund after being deposited in the general fund.