

## Natural Resource Funds



# North Dakota

## North Dakota Legacy Fund



**Market Value**

**North Dakota**  
\$1.3 billion

Santiago  
Compliance  
Index  
  
not rated

Resource  
Governance Index  
Natural Resource  
Fund Score  
  
not yet rated

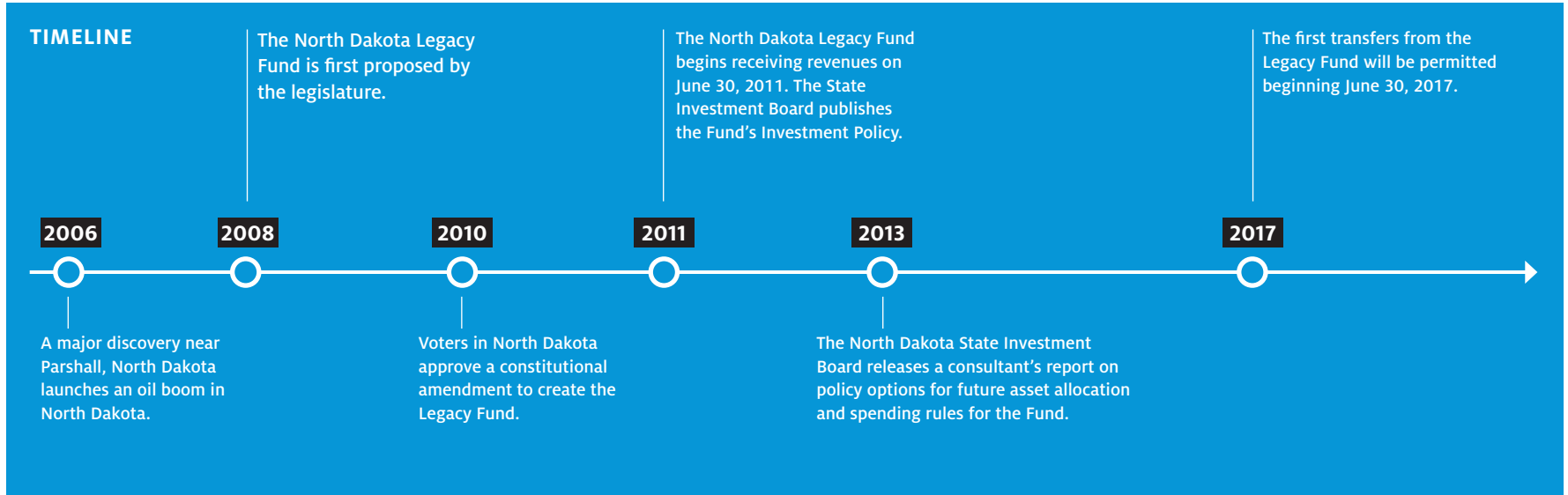
Truman Sovereign  
Wealth Fund  
Scoreboard  
  
not rated

Good Governance Fundamentals	
Clear Deposit Rules	yes
Clear Withdrawal Rules	yes
Clear Investment Rules	yes
Transparent	yes
Publicly Available Audits	yes
Effective Oversight	yes

**Fund Highlights**

- North Dakota’s government first proposed the Legacy Fund in 2008. Following a statewide vote approving a constitutional amendment, it was established in 2010 to save a portion of oil and gas revenue windfalls from the development of the Parshall Oil Field.
- 30 percent of taxes from oil and gas exploration and production are deposited into the Fund.
- The principal and earnings of the Legacy Fund may not be withdrawn until 2017. Thereafter, withdrawals from the principal will still require a two-thirds majority vote from each house of the state legislature. No more than 15 percent of the Fund’s principal may be spent during a two year period.

- While the Fund is subject to broad investment guidelines, the State Investment Board retains a high degree of discretion in choosing specific assets.
- Thanks to a comprehensive oversight and accountability system, Fund assets are safeguarded and governance rules are followed.
- While generally transparent, the Fund does not divulge specific assets it holds.



## Fund Inception

- Article 10, Section 26 of the North Dakota State Constitution, a constitutional amendment passed by state voters in 2010, established the North Dakota Legacy Fund.<sup>1</sup>
- North Dakotans voted 64 percent to 36 percent in favor of establishing the fund and enacting fiscal rules to save a portion of oil and gas revenues.

## Fund Objectives

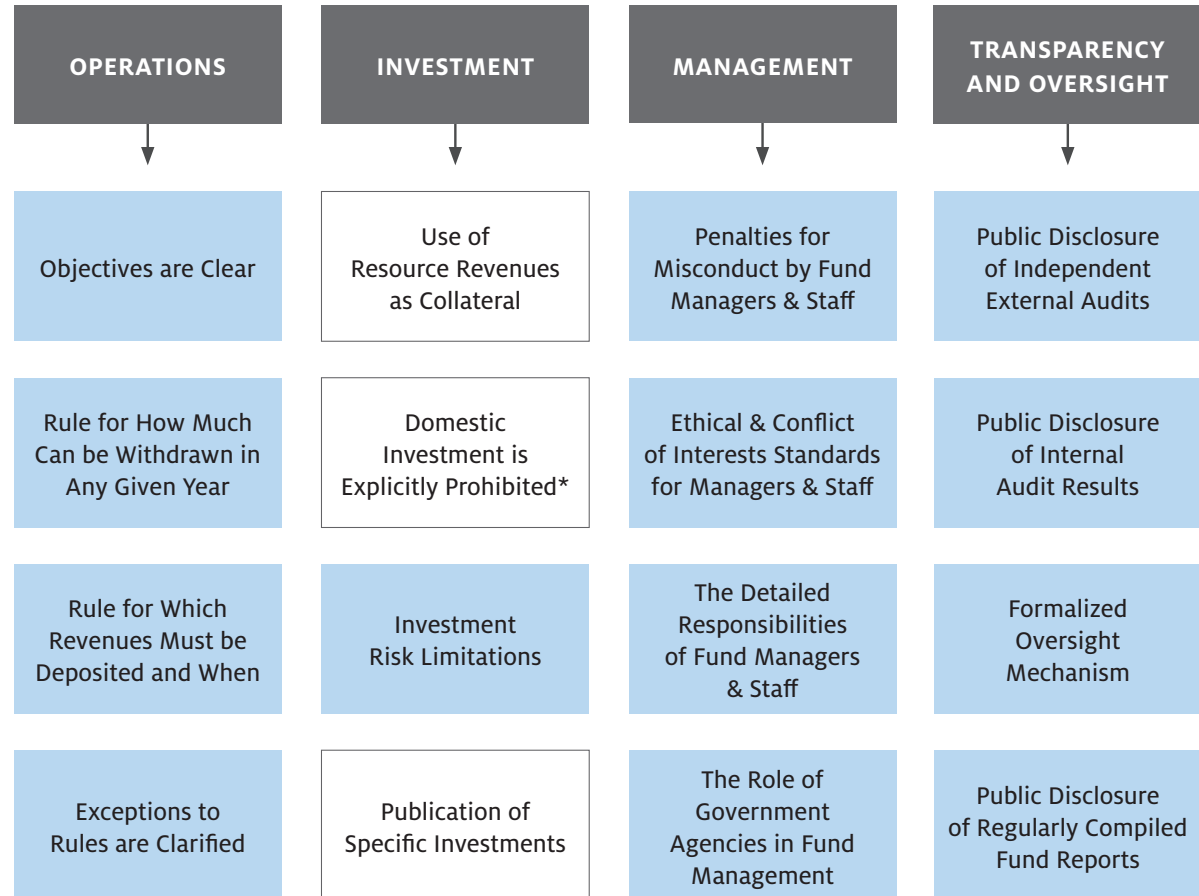
- The North Dakota Legacy Fund is a savings and future generations fund. The Fund seeks to preserve a portion of present oil and gas revenues for the benefit of future generations.<sup>2</sup>


## Good Governance Standards and Gaps in Regulation


Each box represents a regulatory standard essential for promoting consistent use of and safeguarding resource revenues. White boxes highlight regulatory gaps in fund governance.

# 13/16

Good Governance Standards Met



 Presence of Regulation

 Absence of Regulation

\*According to the Fund's Investment Policy, "[w]here investment characteristics, including yield, risk, and liquidity are equivalent, the Board's policy favors investments which will have a positive impact on the economy of North Dakota."

## Operational Laws, Rules and Policies

*The Legacy Fund uses a bird-in-hand fiscal rule to limit withdrawals, meaning only the return on investments may be spent. Exceptions are possible but require a two-thirds majority vote by the Legislative Assembly.*

### Fund Deposit Rules<sup>3</sup>

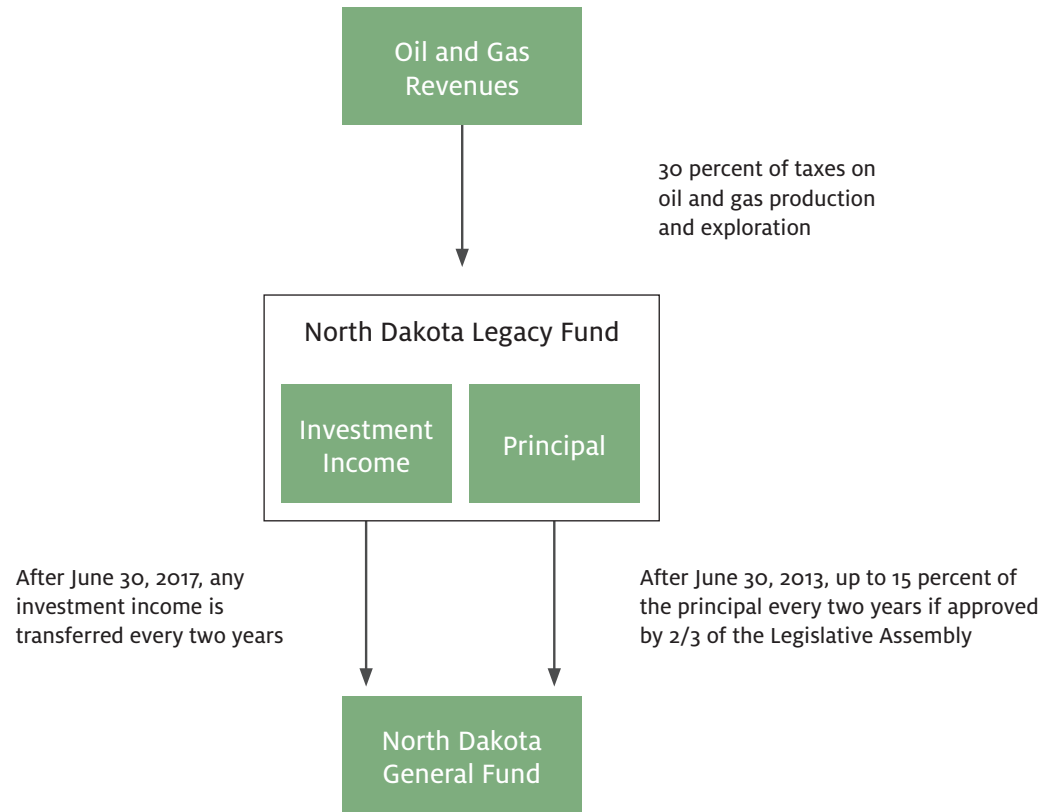
- North Dakota's Constitution mandates that thirty percent of taxes received by the state on any oil and gas exploration and production must be deposited into the North Dakota Legacy Fund.
- The Legislative Assembly may also transfer other funds into the North Dakota Legacy Fund at its discretion.
- Since withdrawals of any kind are prohibited until June 30, 2017, all of the Fund's investment income is currently reinvested.

### Fund Withdrawal Rules<sup>4</sup>

- No withdrawals of either the Fund's principal or its investment income can be made until after June 30, 2017.
- After June 30, 2017, any investment income accrued by the Fund will be transferred to the State's general fund every two years.
- Any withdrawals from the Fund's principal after June 30, 2017 will require a two-thirds vote in both houses of the North Dakota Legislative Assembly. In this case, a maximum of 15 percent of the Fund's principal can be withdrawn once every two years.

# Operational Laws, Rules and Policies

## Flow of Funds



## Investment Laws, Rules and Policies

### Investment Authority<sup>5</sup>

Ultimate responsibility for the North Dakota Legacy Fund lies with the North Dakota State Investment Board, which receives recommendations on the Fund’s investments from the Legacy and Budget Stabilization Fund Advisory Board.

### Investment Strategy<sup>6</sup>

- In making investments, the State Investment Board must apply a “prudent investor rule” that requires that the Board to “[...] exercise the judgment and care, under the circumstances then prevailing, that an institutional investor of ordinary prudence, discretion, and intelligence exercises [...].”
- The Fund’s current target asset allocation is as follows:
  - 20 percent cash and cash equivalents.
  - 70 percent short term bonds.
  - 10 percent bank loans.
- The Fund prohibits social investing (investing with an aim other than maximizing returns) and economically targeted investing (investing to stimulate growth in a particular geographic area or sector) unless the following conditions are met:
  - Cost does not exceed fair market value at time of investment.
  - The Fund receives an equal or greater rate of return to a similar investment with similar risk and time horizon.
  - The Fund is able to maintain adequate liquidity.
  - The investment adheres to the prudent investor rule.

### Investment Objectives<sup>7</sup>

The Fund expresses its investment objectives as expected reward/risk relative to benchmarks set by the State Investment Board.

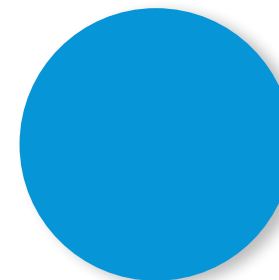
- Rate of return and performance, minus expenses, should at the minimum, equal the State Investment Board’s benchmarks for rate of return and performance.
- Risk should not exceed 115 percent of the benchmark for risk set by the State Investment Board.

### Allocation by Asset Class<sup>8</sup>

As of June 2012

Short-term Fixed  
Income Securities

**100%**



### Policy on In-State Investments<sup>9</sup>

Fund assets may be invested in North Dakota.

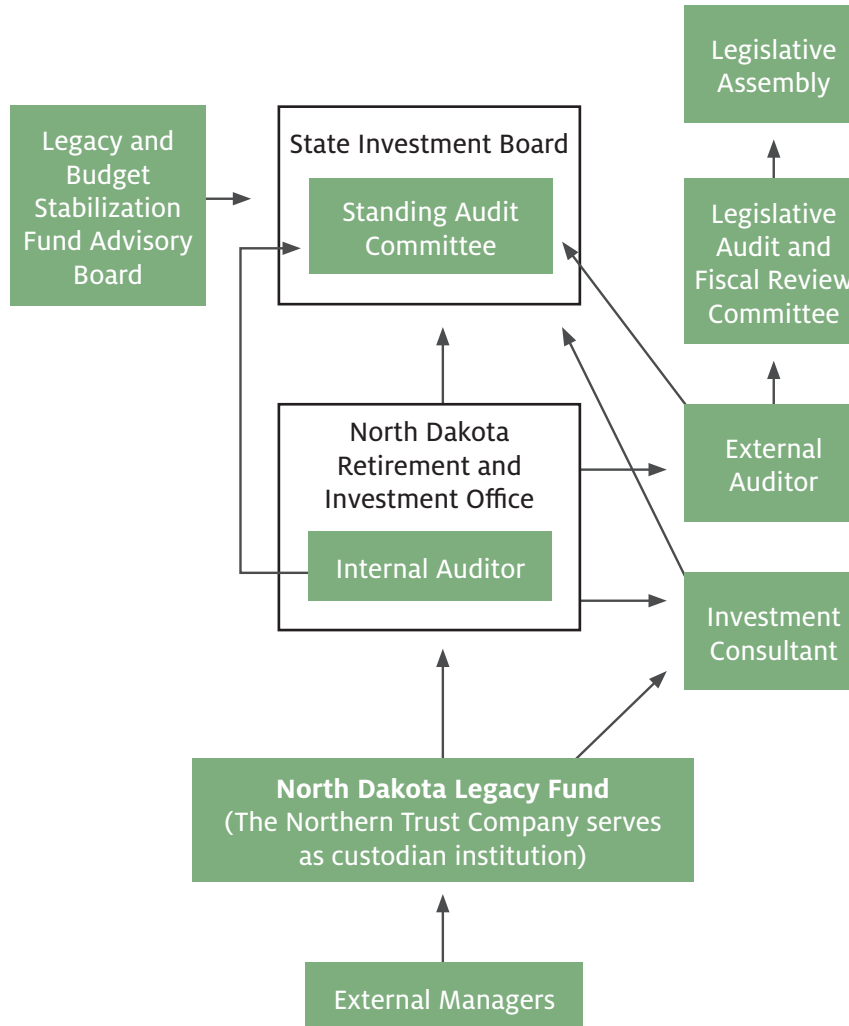
## Management and Accountability

### Management and internal accountability

The State Investment Board is ultimately responsible for the Fund and sets investment policy. It consists of the Governor, the State Treasurer and other senior government officials. The State Investment Board's Standing Audit Committee is responsible for overseeing internal and external audits.

The Legacy and Budget Stabilization Fund Advisory Board provides the State Investment Board with recommendations on the Fund's investments. The Advisory Board consists of members of the legislature, government officials and the executive of the state-owned Bank of North Dakota.

The North Dakota Retirement and Investment Office assists the State Investment Board in day-to-day operations of the Fund and prepares annual reports that are released to the Standing Committee, the Legislative Assembly, and the public.



### External accountability

Withdrawal of the Fund's principal requires a 2/3 majority vote by the Legislative Assembly.

The Legislative Assembly's Audit and Fiscal Review Committee receives annual reports from the external auditor.

An external audit is conducted by either the State Auditor or an external auditing firm contracted by the State Auditor.

A private sector investment consultancy firm is selected by the State Investment Board to monitor Fund performance and adherence to investment objectives and policies.



## Oversight and Safeguards

*The Fund is safe-guarded by a comprehensive accountability system, including regular and independent audits, legislative oversight and citizen engagement.*

### Oversight Mechanisms

- The State Investment Board appoints an **external investment consultancy firm** to monitor the Fund's performance to ensure compliance with investment policies and goals.
- Finances are subject to **regular and comprehensive internal audits**.
- Fund finances are subject to a **regular and independent external audit** that meets international standards.
- The Legacy Fund is imbedded in State law, having been established through a constitutional amendment. Any significant strategic or operational **changes require legislative approval**.
- **Arbitrary withdrawals of the principal are not allowed** and require a two-thirds vote in both houses of the North Dakota Legislative Assembly following a lifting withdrawal restrictions on June 30, 2017.
- There is **some monitoring** by citizens and civil society organizations.

### Common Oversight Mechanisms or Safeguards Not Present in North Dakota

- There is **no regular monitoring** by federal government entities.

## Transparency Laws, Rules and Policies

**There is public disclosure of the following:**

When or how often Fund reports are published and made publicly available	yes	
Which individuals or organizations are responsible for publishing Fund reports	yes	
Size of the Fund(s)	yes	
Deposit and withdrawal amounts	yes	
Returns on investments	yes	
Detailed asset allocation – geographic location		no
Detailed asset allocation – asset class	yes	
Detailed asset allocation – specific assets		no
Natural resource prices and other fiscal assumptions used to calculate deposit and withdrawal amounts allowed under fiscal rules		no

## **Annex:** List of Applicable Laws

### **North Dakota State Constitution: Article X, Section 26**

<http://www.legis.nd.gov/files/constitution/ArticleXFinanceandPublicDebt.pdf>

### **North Dakota Century Code: Chapter 21.10**

<http://www.legis.nd.gov/cencode/t21c10.pdf>

- 1 North Dakota State Constitution, Art. X (26). Available at: <http://www.legis.nd.gov/files/constitution/ArticleXFinanceandPublicDebt.pdf>
- 2 State Investment Board Investment Policy Statement. Available at: <http://www.legis.nd.gov/assembly/62-2011/docs/pdf/lbs090611appendixc.pdf>
- 3 North Dakota State Constitution Art. X (26). Available at: <http://www.legis.nd.gov/files/constitution/ArticleXFinanceandPublicDebt.pdf>
- 4 North Dakota State Constitution Art. X (26). Available at: <http://www.legis.nd.gov/files/constitution/ArticleXFinanceandPublicDebt.pdf>
- 5 North Dakota Century Code, Chapter 21.10. Available at: <http://www.legis.nd.gov/cencode/t21c10.pdf>
- 6 State Investment Board Investment Policy Statement. Available at: <http://www.legis.nd.gov/assembly/62-2011/docs/pdf/lbs090611appendixc.pdf>
- 7 State Investment Board Investment Policy Statement. Available at: <http://www.legis.nd.gov/assembly/62-2011/docs/pdf/lbs090611appendixc.pdf>
- 8 North Dakota Retirement and Investment Office. "Comprehensive Annual Report 2012," p. 103. Available at: <http://www.nd.gov/rio/SIB/Publications/CAFR/AnnualReport-Investment.pdf>
- 9 State Investment Board Investment Policy Statement. Available at: <http://www.legis.nd.gov/assembly/62-2011/docs/pdf/lbs090611appendixc.pdf>