

**MINUTES OF THE JOINT EXECUTIVE APPROPRIATIONS
COMMITTEE MEETING
October 19, 2010 at 1:00 P. M.
Room 445, State Capitol, State Capitol Complex**

Members Present: Sen. Lyle W. Hillyard, Co-Chair
Rep. Ron Bigelow, Co-Chair
Rep. Bradley G. Last, Vice Chair
Sen. Daniel R. Liljenquist, Vice Chair
Rep. Douglas C. Aagard
Rep. David Clark, Speaker
Rep. Brad L. Dee
Sen. Scott K. Jenkins
Sen. Patricia W. Jones
Sen. Peter C. Knudson
Rep. David Litvack
Rep. Rebecca D. Lockhart
Sen. Karen Mayne
Rep. Carol Spackman Moss
Sen. Wayne L. Niederhauser
Sen. Luz Robles
Sen. Ross I. Romero
Rep. Jennifer M. Seelig
Sen. Michael G. Waddoups, President

Members Excused: Rep. James R. Gowans

Staff Present: Jonathan Ball, Legislative Fiscal Analyst
Steven Allred, Deputy Director
Greta Rodebush, Legislative Secretary

Speakers Present: Becky Brusco, Governor's Office of Planning and Budget
Patrick Lee, Office of the Legislative Fiscal Analyst
John Harvey, Public Service Commission
Steven Allred, Office of the Legislative Fiscal Analyst
William R. Hallmark, Cheiron, Inc.
Michael J. Noble, Cheiron, Inc.
Sen. Wayne L. Niederhauser
Richard Amon, Office of the Legislative Fiscal Analyst
Richard Ellis, State Treasurer
Ivan Djambov, Office of the Legislative Fiscal Analyst
Dennis Strong, Utah Department of Natural Resources

Note: A copy of related materials and an audio recording of the meeting can be found at www.le.utah.gov.

A list of visitors and a copy of handouts are filed with the committee minutes.

1. Call to Order/Approval of Minutes

Co-Chair Hillyard called the meeting to order at 1:39 p.m. Rep. Gowans was excused from the meeting. No action was taken on the minutes at this time.

Sen. Romero asked the committee members to be mindful of the posted start time. If the committee is going to start late, he suggested notifying the public so as to not inconvenience anyone.

2. Federal Funds/ARRA/Non-Federal Grants Reports

Federal Funds

Becky Bruso, Governor's Office of Planning and Budget, presented the Federal Funds Report through September 30, 2010. There were two new grants and one reapplication of an existing grant requiring legislative action.

Ms. Bruso stated that the Governor's Office approved six new grants. She noted two changes to the Governor's Report. The one reapplication of an existing grant, Department of Community and Culture, NEA Partnership Agreement, was taken off the report and would be presented next month. In addition, the report shows that the Governor's Office approved two revisions of existing grants. A third revision, Human Services, State Health Insurance Information Program, was erroneously listed as a reapplication of an existing grant, item 249, on page A-24 in Appendix A. The Governor also approved this grant as a revision of an existing grant program.

Co-Chair Hillyard recognized Co-Chair Bigelow for a motion.

MOTION: Co-Chair Bigelow moved to approve the minutes of the Joint Executive Appropriations Committee meeting on September 14, 2010. The motion passed unanimously with Sen. Liljenquist, Sen. Knudson, and Sen. Robles absent for the vote.

ARRA

Ms. Bruso presented the ARRA Federal Funds Report through September 30, 2010. There was one new ARRA grant and no reapplications of existing grants requiring legislative action. The Governor's Office approved no new ARRA grants and no reapplications of existing grants.

Non-Federal Grants

Ms. Bruso presented the Non-Federal Grants Report through September 30, 2010. There were no new grants and one reapplication of an existing grant requiring legislative action. The Governor's Office approved one new grant and no reapplications of existing grants.

Co-Chair Hillyard asked about the ARRA grant, Utah Public Service Commission, State Broadband Data and Development Program - Supplemental. The federal award is \$3,151,583 with an in-kind state match

of \$774,396. Co-Chair Hillyard asked if this program is affiliated with Utah Education Network (UEN) in its efforts to connect schools with broadband.

John Harvey, Public Service Commission, briefly explained that this grant will continue broadband data collection, validation, and broadband map development. He stated that the Public Service Commission has made an initial submission of this data to the National Telecommunications and Information Administration (NTIA). Maps will also be available via an internet portal through the Automatic Geographic Reference Center (AGRC). In terms of UEN, the State Broadband Data and Development Program works with UEN from an information, planning, and coordination standpoint. The program is not part of UEN's build out.

Co-Chair Hillyard asked if this grant program helps support rural telephone companies. Mr. Harvey stated that this program shares broadband information with both rural and urban providers and acts as a coordinating entity between the two.

MOTION: Co-Chair Bigelow moved to recommend acceptance of the federal, ARRA, and non-federal grants as outlined on page 1, "Federal/Non-Federal Grants Review and Approval" under the heading, "Grants Requiring EAC Review and Recommendation" and dated today, October 19, 2010. The motion passed unanimously with Sen. Liljenquist absent for the vote.

MOTION: President Waddoups moved that under the signatures of the chairs of the Executive Appropriations Committee, a request go out to the Governor's Office of Planning and Budget, the Fiscal Analyst, and department heads, requesting that the Executive Appropriations Committee receive notice of any requests or changes in budgets which would implement state funding in any programs that are currently being funded through a grant program.

President Waddoups stated that decisions to continue programs using state funding should be based on the merits of a program and not because a grant revenue source expired.

Rep. Dee spoke in support of the motion.

The motion passed unanimously with Sen. Liljenquist absent for the vote.

3. Audit Report of URS Actuaries

Steven Allred, LFA, stated that during the 2010 General Session, the Legislature faced some very difficult decisions regarding the Utah Retirement System (URS). He explained that URS budgets for a 7.75 percent return on its investments, and in 2008, the system experienced a minus 22 percent return which created an estimated \$6.5 billion unfunded liability in the retirement system. The State was faced with significant increases in the contribution rate over at least twenty-five years to make up that loss.

Mr. Allred stated that the Legislature debated several structural changes to the retirement system. The debate was based on actuarial information provided by the Utah Retirement System (URS) and their contract actuary, Gabriel Roeder Smith (GRS). In January of 2010, the Retirement and Independent

Entities Appropriations Subcommittee issued a Request for Proposals for an independent actuarial firm to audit GRS' projections. The Legislature proceeded to make retirement reforms in Senate Bill 43 and Senate Bill 63, knowing that the independent audit would be completed during the 2010 interim. On May 19, 2010, the Retirement Subcommittee selected Cheiron, a national actuarial firm, to conduct the audit.

Mr. Allred explained that Cheiron would brief EAC on the results of its audit followed by a more in-depth report to the Retirement and Independent Entities Interim Committee on October 20, 2010.

Bill Hallmark and Mike Noble, Cheiron Actuaries, presented a brief overview of the audit's key findings. The full report, "Audit of Long-Term Actuarial Projections Relating to State Retirement System," is found behind tab 3 in the committee binders.

The principal findings from the actuarial audit indicate that Cheiron (1) agreed with the substantive results produced by GRS; (2) observed that employee choice in the Tier II hybrid system could lead to extreme funding positions many years in the future depending on future investment returns; and (3) cautioned that GRS' models could make the Defined Contribution program appear more favorable.

Mr. Hallmark and Mr. Noble discussed a table showing a replication of GRS's long-term actuarial projections using a baseline of 7.75 percent investment return every year, and a table showing the impact of investment experience relating to Senate Bill 63 issues.

Mr. Hallmark and Mr. Noble responded to committee member questions regarding market volatility, investment strategies, rates of return, contribution rates and funding policies, mortality rates, and structural changes and market valuation models in other states.

Speaker Clark asked if Utah is better off with the structural changes made to Utah's Retirement System, and if they are sustainable. Mr. Hallmark stated that in general, Utah is better off, and that over the next ten to fifteen years, Utah's program will have less risk. He did point out that a lot depends on the experience Utah has with the hybrid plan and the choices employees make.

Speaker Clark commented that Utah will need to be diligent in managing the process and mitigating those types of concerns.

Sen. Liljenquist thanked Mr. Hallmark and Mr. Noble for their report. Cheiron has validated GRS's projections and raised some concerns going forward. Sen. Liljenquist stated that if we assume a more conservative rate of return and require contributions to be higher than they are now, the state maybe able to eliminate some of the volatility issues. Mr. Hallmark confirmed that with the current assumed rate of 7.75 percent, there may be too much volatility. Sen. Liljenquist stated that the Legislature will address the issue this year. He stated that the goal of pension reform was to gradually reduce the bankruptcy related risk of the State's defined benefit pension system.

4. Bill on Performance Review Notes

Senator Niederhauser presented draft legislation entitled, "Joint Rules Resolution on Fiscal Note Process," which would require a performance note on legislation that creates a new program, agency, or

an appropriation for new funding. The legislation outlines the duties and responsibilities of government entities, bill sponsors, the Office of the Legislative Fiscal Analyst, the Legislative Auditor General, and the Executive Appropriations Committee in the performance review note process.

Sen. Niederhauser discussed the current fiscal note format, a draft when a performance note is not required, and a draft when a performance note is required.

If a performance note is required, the bill sponsor would work with the government entity to provide a note stating the purposes, services, goals, resources, benchmarks, and performance measures of the new program or agency. If the sponsor rejects the agency's performance note, the sponsor can submit an alternative performance note.

Sen. Niederhauser pointed out that the performance note would not only provide information for discussion and debate in committee and on the floor, but would also create a process to evaluate and compare actual outcomes against expected outcomes.

Sen. Niederhauser further explained that the Legislative Auditor General would have the responsibility of reviewing each new program or new agency to determine whether the goals or impacts and performance measures have been met. If the goals or impact or performance measures have not been substantially met, the Legislative Auditor General would notify the government entity, the sponsors, and the chairs of the Executive Appropriations Committee. Upon receipt of a notice, Executive Appropriations Committee would place the determination on the agenda for review and consideration.

Committee discussion

President Waddoups, Sen. Jones, and Speaker Clark expressed concern that this legislation would significantly increase the workload for the Legislative Auditor General.

President Waddoups stated that the Auditor General currently receives assignments from the Audit Subcommittee, and that they are understaffed for those requests.

Sen. Jones asked how programs with long-term outcomes will be evaluated and how close to the "bull's eye" would a program have to get to show that its objectives have been met. She stated that sometimes program evaluation can be highly subjective.

Sen. Niederhauser stated that both short and long-term goals could be included in the performance note. He did not discount that there would be subjectivity, but more important, there needs to be accountability.

Sen. Jones asked about the adequacy of current sunset reviews and the shifting of responsibilities. Sen. Niederhauser did not think that every new program or appropriation had a sunset review. The Legislative Auditor General would determine if a new program or appropriation had met the performance measures and not make decisions on whether or not a program or appropriation should be continued.

Sen. Niederhauser stated that the performance review process is open for discussion.

Sen. Niederhauser suggested that the committee needed to hear from the Legislative Auditor General to determine what impact this bill was going to have on their office.

Speaker Clark spoke in support of performance measures but wondered how the Legislative Auditor General would manage the additional audits.

Pres. Waddoups raised the issue of audit workload again, noting that he had sponsored a bill four years ago to increase the number of auditors in the State Auditor's Office by two. The State Auditor at the time felt like he would need six to ten auditors to do justice to the number of performance audits.

Sen. Niederhauser asked the Legislative Auditor General for comment.

Darin Underwood, Legislative Auditor General's Office (OLAG), explained that there are about twenty-one audits on the priority list that have not been assigned staff. In addition, the office is down three to four auditors. He stated that the proposed bill helps clarify what OLAG is already statutorily obligated to do. OLAG currently monitors programs and agencies, providing them with self assessment tools and best practice manuals. Should there be any cause for concern, OLAG may recommend to the Legislative Audit Subcommittee that an audit be conducted.

Mr. Underwood stated that the proposed bill requires OLAG to review new agencies or programs under each of the performance note standards. These reviews will have to compete for resources against the audits that have already been put on the priority list. He commented that the Legislature will have to decide if the Legislative Audit Subcommittee should continue to be the gatekeeper of all the audits.

President Waddoups asked how many new auditors OLAG would need to take on the performance notes. Mr. Underwood stated that OLAG currently has one person that administers the self assessment tool for new programs or agencies. If the Legislature decided to go to the performance note model, this could require another staff person.

Sen. Mayne stated that she chairs the Misclassification of Workers Task Force which is going to produce a fair amount of legislation. She asked who is going to determine which bill requires a performance note. Sen. Niederhauser said that the Legislative Fiscal Analyst would make that determination based on guidelines outlined in the proposed legislation.

Sen. Liljenquist stated that the Legislature needs to invest in the policies it authorizes. He stated that what you measure and inspect, you improve. He thought the investment should include some funding for additional staff. He also suggested using other reporting measures like the Governor's Balance Scorecard. A full audit may not be necessary.

Rep. Moss stated that accountability is a worthy goal. She asked about the number of bills that might carry a performance note, submission issues, and the likelihood that the process might slow down the legislative process. Sen. Niederhauser thought that perhaps 10 to 20 percent of the bills may require a performance note. He stressed that the benefits of legislating for results far outweigh the inconveniences this process may present. It is the responsibility of the sponsor to secure as much correct information as possible.

Rep. Litvack agreed with many of the comments that were made regarding the value of performance measures. He expressed concern that the process gives an agency only three days to prepare a performance note during the legislative session. He stated that it would be important to have good performance measures that add to the value of the evaluation component.

Sen. Niederhauser said that this process is going to take a different mind set, a different paradigm.

Rep. Dee expressed his support for outcome-based budgeting and the performance review process. He suggested partnering with the Governor's Office of Planning and Budget (GOPB).

MOTION: Co-Chair Bigelow moved to amend the proposed bill on line 166: After the word "and", insert the words, "as prioritized by the Legislative Audit Subcommittee."

Co-Chair Bigelow stated that this motion will remove concerns that the bill would require the Legislative Auditor General to review performance measures across state government without sufficient staff and direction from the Legislative Audit Subcommittee.

President Waddoups spoke in favor of the motion.

Sen. Niederhauser thanked the committee for their comments and questions. He stressed the importance of getting the process right. He said that he was convinced that this is the right direction for Utah in its budgeting process. He noted that he has been working with GOPB, and that he supports this amendment.

A vote was taken on the motion to amend. The motion passed unanimously with Sen. Liljenquist absent for the vote.

MOTION: Rep. Bigelow moved to adopt the bill as amended, "Joint Rules Resolution on Fiscal Note Process," as an Executive Appropriations Committee bill.

Co-Chair Bigelow stated that until we get this process underway we will not be able to refine it. He agreed with Sen. Niederhauser that it will take some time, perhaps over several legislative sessions, to get the process right.

Rep. Litvack agreed with the sponsor that we are moving in the right direction with performance measures. However, he does not support the legislation as it is written. The committee has not heard from the departments that will be implementing this process. Moving the bill forward this quickly may be premature. Rep. Litvack would like to work with the sponsor to get the process perfected.

Sen. Romero agreed with Rep. Litvack's assessment. He suggested that one other strategy might be to look at some empirical information and community support to determine if a program has value before it is rolled out. He was not in favor of the motion at this time, but stated that the process makes some sense.

Co-Chair Bigelow stated that this bill will help the Legislature evaluate whether taxpayer money is being used effectively or not.

A vote was taken on the motion. The motion passed with Sen. Mayne, Sen. Jones, Sen. Romero, Sen. Robles, and Rep. Litvack voting in opposition. Sen. Liljenquist was absent for the vote.

5. Build America Bonds

Rich Amon, LFA, offered some introductory remarks regarding the Build America Bonds program and presented the Issue Brief, "Build America Bonds Federal Subsidy."

The State Treasurer and the State Bonding Commission issued five bond series using the federal Build America Bonds (BAB) program. The BAB program requires issuers to sell bonds at higher taxable interest rates and provides a subsidy back to the issuer in the form of an IRS refund. Mr. Amon illustrated how this principle works using the example found in Table 2, "2009CD Highway and Building Projects." The BAB program saved the State \$21 million over the life of the \$982 million 2009CD issuance.

Mr. Amon stated that recently the bond rating agencies provided direction to issuers using the BAB program to budget debt service gross of the federal subsidy. This practice protects debt service payments to bond holders should the federal government stop, defer, or reduce the payment of the BAB subsidy. The Analyst views this preference by the rating agencies as an indication of the risk associated with the BAB subsidy.

Mr. Amon discussed Table 4 that shows the BAB subsidies by fiscal year and compares them to the annual debt service. Typically, the State budgets bonds net of a revenue source (like the BAB subsidy). This practice allows the State to reduce state fund appropriations to debt service by the amount of the revenue. Budgeting debt service gross of the subsidy will require a change in budgeting practice for debt service.

Mr. Amon discussed some additional risk and compliance issues associated with the Build America Bonds as well as some solutions to help mitigate those risks. One risk is the way the IRS treats the BAB subsidy as an overpayment of tax, and therefore can reduce the amount of the subsidy to collect any outstanding taxes or obligations owed to the federal government (through the Tax Treasury Offset Program). In order to avoid the risk associated with the Treasury Offset Program, the State must be aware of potential liabilities to the federal government.

Mr. Amon finished his presentation by reviewing several options to budget debt service and the BAB subsidies.

Sen. Hillyard commented that at a recent NCSL conference, a speaker raised two issues - what if in the future, the federal government starts putting conditions on the bonds they subsidize, and what if people with high net worth start looking elsewhere to invest their money to avoid not having tax-free income.

Richard Ellis, State Treasurer, stated that the debt they have issued to this point does not have federal strings attached. This is not the direction the State would want to go. In regards to high net worth, they have found that through the BAB's program the rates on tax exempt bonds have become lower because supply has diminished. There are several entities pushing to keep tax exempt bonding as the primary

funding source rather than taxable bonds. The tax exempt tool is our primary way of accessing the markets into our benefit.

Co-Chair Hillyard asked if local entities can issue these bonds, and if so, can they be issued like a revenue bond, approved by a city council or a governing board, or a GO bond that has to be approved by the vote of the people. Mr. Ellis responded that local entities can issue bonds either way.

6. Water Resources Revenue Bonds

Ivan Djambov, LFA, presented the Issue Brief, "Water Resources 2010 Revenue Bond."

Mr. Djambov explained that in February 2010, the State Bonding Commission issued \$65.8 million of "AA" rated Water Resources revenue bonds without notifying the Legislature. There was no violation of any statute involved in the process. Under current statute, the State Treasurer and the State Bonding Commission do not need authorization or approval of the Legislature to issue revenue bonds on behalf of certain loan funds.

Mr. Djambov stated that the Legislature should be involved in deciding which type of bond is most appropriate. He went on to discuss some of the advantages and disadvantages of revenue bonds and General Obligation bonds.

Mr. Djambov stated that involving the Legislature in the bonding process will allow for better coordination and planning between capital and operational budgets and will allow the Legislature to better allocate resources and make better budgeting decisions.

Mr. Djambov concluded with the Analyst's recommendation for a change to the State Financing Consolidation Act (63B-1b) to require legislative approval for all revenue bonds issued by revolving loan funds listed in the Act.

Dennis Strong, Director, Division of Water Resources, Utah Department of Natural Resources, talked about the decision to recapitalize bonds for the Provo Reservoir Canal and Enclosure Project. This project replaces a canal with a pipeline from the Provo River to the Point of the Mountain and moves water from irrigation to municipal and industrial uses. The Board of Water Resources provided loans for over \$70 million to construct the enclosure project. Mr. Strong stated that in funding the project, the Board and the Division of Water Resources followed the process as outlined in statute.

Co-Chair Hillyard stated that he was not concerned with the project itself, but rather with the process of issuing bonds during the session without the Legislature knowing about it.

MOTION: Co-Chair Bigelow moved to adopt the recommendations of the Analyst as shown on page 2 of the Issue Brief entitled, "Water Resources 2010 Revenue Bond," and to ask staff to work with the co-chairs to draft legislation as recommended.

Co-Chair Bigelow explained that the recommendations would include language in the State Financing Consolidation Act (63B-1b) similar to the Higher Education statute 53B-21-113 that states:

No bonds may be authorized or issued by the State Board of Regents or the board of any institution under this chapter without prior approve of the Legislature.

President Waddoups asked if the State's "AAA" bond rating is impacted when "AA" bonds are issued. Richard Ellis, State Treasurer, stated that issuing "AA" bonds does not affect the State's overall rating because the source of repayment is secured through the repayment of existing loans equal to 150 percent of the payments going out.

Speaker Clark asked if there were any other entities that might be desirous of issuing bonds under this statute. Mr. Ellis responded that under the State Financing Consolidation Act, there are several entities that have the authority to issue bonds. He mentioned that he was aware that Department of Agriculture was considering a smaller issue, but they have talked to legislative leadership. He was not aware of any others.

Sen. Romero complimented the State Treasurer's Office on the work they have done in securing and maintaining Utah's bond rating.

Co-Chair Bigelow stated that the intent of his motion is to have the bill cover other entities as well.

A vote was taken on the motion. The motion passed unanimously with Sen. Liljenquist and Sen. Jenkins absent for the vote.

7. Other Business

Co-Chair Bigelow called attention to a packet of information that was distributed to the committee. The packet contained a compilation of articles written by agencies, foundations, and groups that have rated Utah high in some areas.

Co-Chair Hillyard recognized Co-Chair Bigelow for a motion.

MOTION: Co-Chair Bigelow moved to adjourn. The motion passed unanimously with Sen. Liljenquist and Sen. Jenkins absent for the vote.

Co-Chair Hillyard adjourned the meeting at 3:56 p.m.