MINUTES
LEGISLATIVE FINANCE COMMITTEE
April 22-24, 2008

Senator John Arthur Smith, Chairman, called the Legislative Finance Committee (LFC) to order on Tuesday, April 22, 2008, at 9:00 a.m.

The following LFC members were present on April 22:

Senator John Arthur Smith, Chair; Representative Luciano "Lucky" Varela, Vice Chair; Representatives Don E. Bratton, Don Tripp (for Brian K. Moore), Patricia Lundstrom (for Rhonda King), Edward C. Sandoval, Jeannette O. Wallace, Nick L. Salazar, and Henry "Kiki" Saavedra; and Senators Sue Wilson Beffort, Mary Kay Papen (for Timothy Z. Jennings), Phil A. Griego, Leonard Lee Rawson, Stuart Ingle (for Joseph J. Carraro), Carlos Cisneros, and Pete Campos. Senator Cisco McSorley attended as a Guest.

Retiree Health Care Budget Update and FY09 Changes in Retiree Contributions.

Tomas Rodriguez, Retiree Health Care Authority (RHCA) acting executive director, introduced several board and staff members to the committee.

Mr. Rodriguez began the presentation by addressing budget and solvency issues, and actions taken. RHCA is striving to maintain financial viability as the program's escalating costs continue and members demand competitive, high-quality health benefits. The major factors contributing to higher health care costs include increasing enrollment and utilization. Actions taken include a premium rate increase for retirees, spouses and dependents, a move toward a single Medicare supplement plan, and the creation of a plan that maintains solvency of the fund for fifteen years into the future. A rate structure sheet provided to the committee further detailed changes.

The FY08 budget forecast detailing revenue sources and expenditures was provided to the committee. Revenue shortfall was originally budgeted to be $10 million in FY08. Budget adjustments to the FY08 budget included additional claims expenditures of $15.1 million. After variances, RHCA is expecting a revenue shortfall of $20.6 in FY08. The projected withdrawal from the investment fund as of January 2008 is $4.4 million.

The original FY09 budget projections included a projected withdrawal from the investment fund of $33 million. Recent actions taken project an adjusted withdrawal from the investment fund of $900 thousand.

The investment fund had a $7 million loss as of March 31, 2008.

A program operations support and information technology update at the RHCA was provided. All customer service representative positions have been filled. Positions still vacant include the executive director, the deputy director, human resources contracts and two financial positions. A new call center has been in place for four weeks and is working better than the old phone system.

All switch enrollment kits will be mailed out by the end of this week. Switch enrollment meetings will be conducted over the next two weeks.

The solvency maintenance plan was detailed to the committee:

- Retirees will be required to pay 50 percent of the cost of their health care.
- Employee/employer EE/ER contributions will increase to no less than 2.4 percent (from 1.95 percent), to nor more than 3 percent.
- Introduce legislation to increase the Department of Taxation and Revenue distributions by $3 million per year.
- Increase the EE/ER contributions for entities whose employees are eligible to retire after twenty years of service.
- Establish in statute that any retiree returning to work must enroll in the health care program of his/her employer.
- Review the current stop loss limits and the value of reinsurance.
- Establish a RHCA coordinating committee to evaluate the maintenance plan and make recommendations to relevant authorities.

Mr. Rodriguez further detailed other support programs and administrative initiatives including a disease management program and cost containment program.

Wayne Propst, LFC analyst, addressed several issues LFC staff has been working with the RHCA on this year. A solvency period is expected to expire in 2014. A $200 million gap exists between the amount of revenues and the amount necessary to adequately fund the system and begin to provide some prefunding for future retirees. The latest actuarial report estimates the state has a $4.1 billion unfunded accrued actuarial liability to fund current and future retirees.

In January 2008, RHCA submitted a budget adjustment request (BAR) to use $15 million in reserves and investments to cover a FY08 short fall in revenues. Mr. Propst further noted that an additional $4.4 million short fall may exist in addition to the BAR of $15 million. The using of reserves and investments in light of recent declines in investment income is of concern to LFC staff. Mr. Propst will be reviewing the FY09 budget projections in greater detail.

Mr. Propst presented a chart to the committee to demonstrate the new retiree contribution and state share under the three plans effective July of 08. David Abbey, Legislative Finance Committee director, emphasized the graph shows that the young retiree who chooses the most expensive plan has the greatest subsidy from the state, even with the new changes.

Mr. Rodriguez clarified that due to changes in the forecast that occurred after reconciliation with CMS, benefit reductions, and other savings, $4.4 as opposed to $15 million is the actual amount projected to be withdrawn from investments.

Alfredo Santistevan, RHCA chairman, restated the RHCA's commitment to improving the program, increasing solvency and solidifying the financial situation of the agency. Chairman Smith and committee members encouraged the RHCA to be more candid with the membership over the seriousness of utilization, benefits and premium issues discussed today.

Vice Chairman Varela stated two additional areas of concern. The number of exempt positions within the authority considering its size, and the issue of improving customer service and response time to members around the state.

Interim Work Plan on Performance and Accountability.

Eugene Moser, LFC analyst, reviewed for the committee the three goals of the LFC staff interim work plan of the performance and accountability group:

- *Accountability in Government* Act (AGA) requires a collateral effort with the executive.
- *Legislating for Results* allows for budget decisions based on performance.
- *Managing for Results* focuses on decision making using performance data.

The impact of the AGA was to transition state agency budgets away from incremental, line-item type appropriations and focus more on giving agencies flexibility to move resources within programs. Legislative hearings are moving away from discussions of line items and budget categories and focusing more on programs and outcomes. There will also be a focus on how agencies are using quarterly reports to manage for results and focus on benchmarking.

Arley Williams, LFC analyst, stated that in putting together the work plan staff wanted to know how best to provide information on best practice to support the committee in putting together budget recommendations. Ms. Williams highlighted the most recent *Grading the States 2008* published in Governing Magazine in March to use as a tool to compare New Mexico with other states in the country in key areas.

Grading the States 2008 has developed a set of criteria to grade the states based on an executive perspective. Ms. Williams detailed the criteria for evaluating both money performance and information performance. The national average for money performance is a B minus and New Mexico scored a B minus. The national average for information performance is a B minus and New Mexico scored a B, better than the national average. The other two categories are for people and infrastructure.

The strongest factor of the New Mexico scoring occurred with "…the state legislature routinely uses cost and performance information to allocate resources and as a basis for program design and redesign".

The information in *Grading the States 2008* can be used to help identify which states can be used as a model of best practice to help New Mexico be more successful with various initiatives.

Major themes within the LFC FY09 work plan will include:

- Collaborating with DFA on an agency performance review manual.
- Sharing information regarding best practices with agency staff.
- Providing information on performance based budgeting by cataloging and providing print and on-line resources.
- Providing training in reviewing, analyzing and developing meaningful performance measures.
- Collaborating with DFA and agencies to improve reporting methods.
- Greater attention to using performance data in developing budget recommendations.
- Greater focus on "reallocation of resources" rather than "cuts" in staff budget recommendations.

Next steps in the work plan will include quarterly and annual presentations to the committee, completing the performance review manual, and continuing with performance subcommittee activities.

Mr. Moser provided a detailed list of important upcoming deadlines for agencies to the committee. The committee recommended looking at deadlines and determining if they are contributing to the effectiveness of the committees' work.

Ms. Williams in closing restated that the underlying purpose of the AGA is to achieve accountability in strategic planning, budgeting, decision making and communication.

Director Abbey said the DFA is slowly working with LFC to expand training and access to SHARE data for the LFC analysts.

Manu Patel, LFC deputy director, presented the committee with an update on the proposed program evaluation work plan.

A proposed evaluation subcommittee meeting is being proposed for June in Albuquerque or Rio Rancho. There will be a report of findings and recommendations for three performance measures within two programs at the Environment Department.

DFA will be working with LFC staff to develop guidelines for agencies to follow in preparing the performance based budgeting monitoring plan. LFC staff will be evaluating the guideline by using it to evaluate 15 performance measures for six programs within the Energy, Minerals and Natural Resources Department.

Additional next priority items will include:

- Procurement division effectiveness, efficiency and staffing.
- A review of selected professional services contracts to ensure the state received the actual services requested.
- A review of particular functions within HED with regards to student financial aide, college affordability, lottery scholarship, student loans programs, etc.
- A review of Medicaid effectiveness.

The committee expressed concerns over student borrower indebtedness. Mr. Patel stated he would take that into account when developing the evaluation plan for the student loan programs at HED.

Second Quarter Performance Report and Data Based Decision Making.

Dorian Dodson, Children, Youth and Families Department (CYFD) secretary provided a presentation to the committee on the department's data-driven management focus for strategic planning purposes.

The protective services division has the most mature data management system within the department and is now being made available to local communities.

The Adoptions and Safe Families Act of 1997 set in place a critical set of measures that look at safety, permanence and well-being of children in foster care. The Federal government has financial penalties in place for states that do not meet these measures. CYFD has aligned these measures with the strategic planning process and measures in the Governor's Performance and Accountability contracts and the Accountability in Government Act.

A comprehensive protective services report was provided to the committee which measures outcomes related to children and families in the child welfare system by county.

Quarterly reviews analyze performance and look at opportunities for people to share data.

A data driven management process flowchart detailed the process to the committee.

Secretary Dodson further detailed the protective services performance measures that align with federal reporting requirements. The committee heard discussion on the status of additional family services, juvenile justice and program support performance measures informed by the data and the ability to collect it.

The department's protective services division exceeded targets in FY07.

Information will be provided at upcoming presentations on using the data to better track juvenile justice performance.

CYFD has recently updated its performance monitoring plan. The plan requires identifying data sources and calculation methodologies for each performance measure.

Investment Portfolio Allocation and Valuation.

Norton Francis, LFC chief economist, introduced the managers, advisors, staff, and board members evaluating and monitoring investment decisions for various state agencies.

Allan Martin, New England Pension Consultants, assists the State Investment Council (SIC) and the Education Retirement Board (ERB) with investment decisions. Mr. Martin presented the theory, motive and benefits of diversification. Diversification was further defined as expanding the number of asset classes to which a portfolio is exposed to improve the ability to earn higher returns. Mr. Martin believes the most risky strategy the state could take would be to limit investments to ordinary stocks and bonds. Further information was provided on the degree to which other funds have made decisions to add alternative asset classes to improve the risk-return strategy.

Return expectations for most asset classes are historically low. Returns for stocks in the next ten years are expected to be 8 percent, bonds 4 to 6 percent, and be very volatile. Volatility compounded through time reduces your average return. The pension funds, ERB and the Public Employees Retirement Association (PERA), must consistently receive an 8 percent to 8.5 percent nominal return in order to fund the states' liabilities and SIC has a target return of 8.5 percent. Mr. Martin believes getting the best possible return results at a level of acceptable volatility can only be achieved by adding alternative asset classes to a portfolio.

The committee heard further discussion of valuing of funds in an uncertain environment. Information on various asset allocations and rate-of return expectations among the best-performing public funds was provided to emphasize the trend toward a more broadly diversified portfolio.

Then each investment entity presented to the committee.

State Investment Office. Gary Bland, state investment officer, introduced the presentation on agency efforts with monitoring investment asset valuation. Mr. Bland stated that it is important to look at themes and concentrations of risk over time.

Adam Levine, deputy state investment officer, provided a presentation on using a derivatives overlay to limit exposure to market fluctuations and risk measurement programs being put into place at the SIC. The current reduction strategy is only to reduce volatility in the assets, and not to speculate. Clients, other than the state permanent funds have the option to participate in the hedged-funds or remain in the unhedged-funds. An example of the type of trade the SIC practices today was provided to the committee.

The committee heard discussion on the importance of being able to measure risk with alternative assets. To do this, SIC has contracted with a third-party aggregator called MeasureRisk to improve investment decisions and management oversight through independent exposure analyses and risk measurement. The committee heard discussion on various methodologies available to SIC to analyze risk and exposures over time such as value-at-risk (VaR) to predict a future outlook, and stress testing which looks at "tail" events, or unlikely but possible events, and unexpected losses. A sample report examining portfolio sensitivities to certain market factors as opposed to exposure to alternative asset classes was provided.

Mr. Bland further stated the benefits of the risk measurement program to identify actual risks, strengths and concentrations driving the portfolio.

The committee continued to hear discussion regarding the current volatility of today's market.

For the last 10 years the return on the fund has been 6.2 percent. For the past 5 years, the rate of return on the fund has been 11.4 percent. The land grant fund is distributing at 5.8 percent until 2015, and will be scaled back down to 5 percent in 2017. The severance tax fund is distributing at 4.7 percent, and contributions remain flat except for earnings.

Educational Retirement Board. Robert Jacksha, New Mexico Educational Retirement Board (ERB) investment officer, presented to the committee a report on alternative investment selection and monitoring. The returns remain very volatile. The 2007 year ended with an asset value of $9.4 billion. As of March 31, 2008 the fund is down 5½ percent, with an asset value of $8.8 to $8.9 billion. Step one for ERB in managing the portfolio is the selection of assets. Step two is the investment consultant selection for advisement on hedge funds, private equity, real estate-related, and infrastructure investments. Mr. Jacksha further detailed the process per ERB policy.

Mr. Jacksha reported on fund manager monitoring at ERB. Individual managers are hired that choose individual hedge funds, and monitor these funds on a daily basis. Risk management systems monitor fund personnel changes and ongoing performance. The committee received sample reports received by ERB from independent third party administrators that value portfolios on a monthly basis. Samples of additional detailed summary reports further illustrated how ERB uses various internal and external sources for oversight and monitoring purposes.

Public Employees Retirement Association. Robert Gish, Public Employees Retirement Association of New Mexico (PERA) investment officer, presented to the committee an investment performance analysis. Mr. Gish introduced Steve Nesbitt, Cliffwater LLC, PERA's special consultant for alternative assets. Mr. Nesbitt presented a review of valuation of alternative assets and transparency issues.

A regression analysis of comparative fund performance back fifteen years was provided to the committee. Returns for the year ending December 31, 2007 were 7.25 percent and below the benchmark of 8.46 percent.

Mr. Francis provided a brief which highlighted the rigorous investment decision making process in place at the three agencies. A breakdown of all alternative asset funds and the investment advisor due diligence provided to SIC and ERB with regard to alternatives was also provided.

Chairman Smith adjourned the committee at 5:00 p.m.

Senator John Arthur Smith, Chairman, called the Legislative Finance Committee (LFC) to order on Wednesday, March 23, 2008, at 8:40 a.m.

The following LFC members were present on April 23:

Senator John Arthur Smith, Chair; Representative Luciano "Lucky" Varela, Vice Chair; Representatives Don E. Bratton, Don Tripp (for Brian K. Moore), Rhonda King, Patricia Lundstrom (for Henry "Kiki" Saavedra), Edward C. Sandoval, Jeannette O. Wallace, Nick L. Salazar, and ;and Senators Sue Wilson Beffort, Bernadette Sanchez (for Timothy Z. Jennings), Phil A. Griego, Leonard Lee Rawson, Carol Leavell (for Joseph J. Carraro), Carlos Cisneros, and Pete Campos. Representative Richard Berry attended as a Guest.

Debt Finance: Current Market Conditions and How the State Protects Itself.

John Bonow, PFM Group managing director, provided a presentation to the committee on the current credit and capital markets.

Dennis Waley, PFM Group, began with a brief history of capital markets developments from 2000 until the present time. In 2005 because of relaxed lending policies and access to credit, real estate speculation and record home ownership grew to 69 percent with sub prime loans 20 percent of the market, as opposed to 9 percent in 1996. From July 2005 to January 2008 existing home sales experienced a 30 percent decline, and new homes a 57 percent decline. Forty three percent of the foreclosures started in the third quarter of 2007 were sub prime adjustable rate mortgages. In 2007 mortgage defaults and the decline of property values began to affect investment bank ratings, bond insurer ratings and auction rate securities.

The committee heard discussion on how national credit and capital market problems affect both fixed and variable rate transaction participants in New Mexico. New Mexico issuers of debt exposed to bond insurers are affected by higher interest rates and insurance costs.

The New Mexico Finance Authority (NMFA) and NM Student Loans have variable rate demand bonds, auction rate securities and student loan bonds outstanding. Large investment banks experiencing losses have significantly reduced the ability and willingness to commit capital to bond transactions.

The committee heard further discussion on the sub prime impact on interest rate swap markets. As bond insurers' ratings decline, bond issuers may be required to post collateral.

An overview of bond insurance was provided. Bond insurers in the low risk municipal bond market were not as negatively affected as entities that were insuring bundled mortgage packages or other leveraged securities. A chart showing the exposure of various New Mexico issuers to bond insurer coverage was provided.

What is happening in the bond insurance community largely does not affecting general obligation bonds, severance tax bonds or NMFA fixed debt because most are fixed rate. However, student loan bonds and other state issuers such as UNM have variable rate debt. It remains a question as to what effect negative effects in the market will have on the variable rate on auction rate securities or variable rate demand bonds. The consensus market view is that the auction rate securities market is defunct, largely because there may not be a willing buyer to provide the liquidity investors require.

Interest rates are also going up for variable rate bonds. Variable rate bond insurers provide both bond insurance, and a line of credit which offers a liquidity feature to pay back the investor. The line of credit can terminate if a bond insurer is downgraded. Variable rate demand programs that do not have that termination provisions trade well. The committee heard further discussion on conversion and refunding options for auction rate bonds to variable rate demand bonds or other alternatives. Most issuers of variable rate have gone to new issues, conversions or refundings.

Then the committee heard reports from New Mexico's agencies that issue debt.

New Mexico Finance Authority. William Sisneros, New Mexico Finance Authority (NMFA) chief executive officer, provided an update on NMFA products in the marketplace used to diversify the debt at the state level.

Mr. Sisneros provided an overview of the GRIP financing plan and debt management policy to provide for lowest-cost financing. In 2004, bonds had 78 percent in fixed rate debt, zero percent in variable rate debt, and 22 percent in interest rate swap covered debt. In 2006, variable rate debt was introduced. In 2006, bonds had 75 percent in fixed rate debt, 2.6 percent in variable rate debt, and 22 percent in swap debt. GRIP debt policy constraints allow for no more than 30 percent in swap-covered debt and for no more than 20 percent in SWAP based debt.

In 2006, NMFA structured a forward starting swap to get an interest rate of under 5 percent to keep the mortgage payment low for DOT. Other bonds issued under the 2006 GRIP finance plan in 2006 were for the construction fund, refinancing of existing debt, and the BNSF escrow fund for the Railrunner.

The bond and investment portfolio managed by NMFA on behalf of the state transportation commission achieved higher than expected investment earnings since the start of GRIP 1. Investment earnings total $68.2 million. Over and above special earnings total $43 million, and were further detailed.

The GRIP program used auction rate securities to remarket $470 million weekly. The downgrade in ratings for bond insurers is drying up the pool of investors for auction rate securities. Mr. Sisneros detailed actions taken when bond insurers were downgraded by rating agencies in February. NMFA obtained a direct pay letter of credit covering liquidity and default for $335 million of the $470 million, to convert the auction rate securities to variable rate demand notes. One bank cancelled their obligation to provide a letter of credit for the remaining $135 million. NMFA decided as an alternative, to issue a variable rate demand note backed by a liquidity only letter of credit for remarketing purposes.

NMFA converted $335.2 million of auction rate securities on April 11, 2008, which traded well. NMFA will be converting the remaining $135.2 million on May 19, 2008.

Interest rates NMFA has had to pay because of the auction rate failures have cost $1.4 million. The cost of restructuring and refunding of auction rate securities is about $2.5 million and final results are pending.

Vice Chair Varela requested a copy of the report on bond activity from the custodian, Bank of Albuquerque.

NM Student Loans. Elwood "Woody" Farber, New Mexico Student Loans (NMSL) president, provided a background on the legislation that ultimately created NMSL. NMSL has issued $2.8 billion in bonds since 1981. Currently $1.04 billion in bonds is outstanding. There are $939 million in student loans outstanding that NMSL earns income from students and the federal government. Ninety-seven percent of student loans are federally guaranteed.

New Mexico student borrower default rate is 2.2 percent, the national average is 4.8 percent. Most of the students that default do so because they are not able to finish the program.

NMSL issues bonds every year to fund the loans for the academic year. Due to market concerns, NMSL decided to move away from auction rate securities to other asset backed bonds last fall. Auction rate securities make up 78 percent of NMSL outstanding bonds. All bonds are AAA rated, maintained in a trust estate, and meet all the stress testing and debt service requirements of the rating agencies.

NMSL will be issuing $65 million in taxable bonds this year to meet the needs of the students.

A direct pay letter of credit for $436 million was obtained from Bank of America, Royal Bank of Canada, and Lloyds of London to refinance half of the auction rate bonds outstanding. By Memorial Day, NMSL expects to have $436 million in bonds restructured of the $900 million. Two years after this conversion, NMSL expects to see a savings of $7.5 million in interest. By September, NMSL expects to have all auction rate securities converted into another interest mode.

Student private loan borrowing is discouraged due to costs. The federal Pell grant followed by the lottery scholarship should be the first consideration for students attending post secondary schools. Private loans should be the last avenue for students and families. Any New Mexico resident attending schools in or out of the state may seek loans from NMSL. The committee expressed concerns over rising student borrower debt.

NMSL rates to student borrowers are set by the United States economist and are fixed at 6.2 percent. Legislation passed by Congress and signed by the President will require rates to go down .6 percent each of the next three years until they reach 3.4 percent.

Chairman Smith requested an update from NMSL in three months.

Representative Varela requested a report from New Mexico Higher Education Department on the 529 education trust fund run by the Oppenheimer foundation for parents.

State Treasuer's Office. Mark Valdez, deputy state treasurer, provided additional information to the committee on bond ratings, insurance and the state's liquidity needs.

At the current time, municipal bonds are being rated under the same system as corporate bonds. Historically there have been significant more defaults on the corporate side than on the municipal side. A separate ratings system for bonds could improve the ratings, lower the interest rates and reduce the cost of borrowed funds.

The state board of finance does not insure their bonds. Other governmental entities that use bond insurance do so to enhance ratings to gain lower rates and borrowing costs. Currently there are only two AAA bond insurers. Consideration could be given by the state to developing a bond guarantee program or insurance for state bond issues.

There is a national crisis on liquidity. Liquidity is required as a stand-by bond purchase agreement for issuers of variable bonds or other short term paper in case of failed remarketing. Current conditions have made it more difficult to obtain liquidity. Consideration could be given by the state to develop a state funded liquidity pool or reserve fund.

Randylynn Lord, State Treasurers Office (STO) legal counsel, addressed the due diligence of the state treasurer's office regarding legal issues when NMFA requested STO to bid on NMFA auction rate securities. There was a question of whether the state treasurer could purchase the auction rate securities. The determination was "yes" based on review of state statute and investment policy. There were also a question about whether the state treasurer's office purchase of the auction rate securities would be considered an issuer purchasing its own debt perhaps preventing any future bond reissue under Securities and Exchange Commission (SEC) and Internal Revenue Service (IRS) rule.

On March 14, the SEC provided a "No Action" letter stating no concerns as long as disclosure was provided by the issuer. On March 25, the IRS stated purchase could move forward only under certain conditions to not be considered debt extinguishment.

Joelle Mevi, STO chief investment officer, addressed the due diligence of STO regarding investment issues when requested to bid on NMFA auction rate securities. Consideration needed to be given as to whether this action would be considered a good investment using investment principles of safety, liquidity and yield. The committee heard discussion on the various points under consideration.

Quarterly Status Report on Capital Projects Greater than $1 million and the Capital Project Monitoring Systems.

Linda Kehoe, LFC analyst, provided a quarterly update on outstanding capital outlay. Representatives from various agencies were present to answer questions.

The number of projects given to local government division outpaces their ability to oversee capital management projects.

The capital monitoring system is being used to track projects as capital funding has not been incorporated into SHARE. A LFC comparison revealed that state agencies are updating the capital monitoring system as intended and the data is reliable.

The LFC is tracking $997.6 million on the projects $1 million or greater with the cooperation of state agencies. A detailed brief was provided to the committee on the rating system developed for this purpose. Spreadsheets and summaries of unexpended funds by county and sponsor were also provided.

The legislature appropriated $3.7 billion for 19,140 projects between 2002 and 2008. $2.3 billion remains unexpended for 9,283 projects, which includes $595 million appropriated last session for nearly 2,000 projects. A breakdown by funding source of the amounts outstanding and summary of reversion dates for outstanding projects was provided.

Some agencies with local projects are having difficulty getting the information necessary to provide updates.

Select projects requiring additional funds, appropriations made between 2004 and 2006 with uncommitted balances, bonds sold but unexpended, projects with no activity since the last report, or inactive projects due to a lack of staff for project management was further detailed. The committee participated in further discussion of various outstanding projects.

Chairman Smith encouraged members to work toward resolving outstanding capital outlay funding issues.

The committee requested more direction on potential anti donation issues with regards to public funding. Ms. Kehoe offered to assist with that effort.

Ms. Kehoe closed with the following comment. Capital outlay funds and projects do not require mandatory audits. Consideration should be given to developing an effective, independent audit of certain appropriations. An examination of project development and expenditures would insure financial standards and project objectives meet executive and legislative intent.

Quarterly Report of Information Technology Projects.

Roy Soto, Department of Information Technology secretary, presented to each member of the committee the new state government telephone directory.

Aurora Sánchez, LFC IT program evaluation manager, presented the third quarter report for information technology projects.

Ms. Sánchez provided an inventory list of all information technology projects $1 million and greater funded in HB 2 from 1997 to 2008, which totaled $345.4 million.

Information technology projects, partial failures or major delays over the years has necessitated the implementation of oversight through agency monthly self-reporting, validation of self-reporting by DoIT and LFC, creation of strong contracts and educating agency staff on enforcement.

Agency reporting requires stricter oversight through timely, accurate and complete reporting of information technology project information.

Information technology projects on the LFC "watch list" were provided.

A detailed hand out on information technology project statistics was provided. Total certified projects over the past three quarters are 61 with 30 $1 million or over. New projects pending certification are 19, and successfully closed projects are 5. The total count of all projects monitored by DoIT is 85 for a total of $231.9 million.

DoIT uses national standards to set the criteria for monthly reporting and provided a diagram on a project's life cycle. A spreadsheet tracking information technology projects $1 million or greater was provided. The committee heard discussion on the status of various projects.

DoIT has developed a staff training plan and will be receiving a staff training appropriation of $1.9 million to further support SHARE. The committee requested a copy of the plan.

The Governor recently reissued a 2004 executive order to state agencies clarifying the intent and authority of DoIT. Mr. Patel agreed to provide a copy of the order to committee members.

The IT commission makes recommendations on initiatives that impact state agencies and provides strategic planning. Representative Varela requested that LFC staff look further at the commission's functions.

The conversion to digital will require the state to build more towers because the distance between digital towers is 30 miles and the difference between analog towers was 60 miles.

The Legislative Education Subcommittee is still not comfortable with the Student and Teacher Accountability Reporting System (STARS) data. LFC only looked at the data from small districts which may not be a true test of how STARS will work for larger districts. The committee requested LFC to continue to give reports on what needs to be done to improve the quality of the data. Ms. Sanchez reminded the committee that in 2006 LFC recommended the 40^{th} day for the Public Education Department (PED) reporting purposes be an actual calendar date, as opposed to a moving target, by which all schools would be required to report. PED has not proposed any changes to the legislation during the 2007 or 2008 legislative sessions.

The legislation that created the cyber academy required PED to promulgate rules for operation. Those rules have not yet been promulgated, which hampers the ultimate success of a project.

The committee heard discussion on the status of additional IT projects of interest to members.

DFA tracks the computer system enhancement fund. Agencies need to request release of funds. The committee requested a status report on funds available and the reason for agencies not spending the appropriations on pending projects.

The committee requested continuous reports on IT development projects.

Chairman Smith adjourned the committee at 5:30 pm.

John Arthur Smith, Chairman, called the Legislative Finance Committee (LFC) to order on Thursday, April 24, 2008, at 8:30 a.m.

The following LFC members were present on April 24:

Senator John Arthur Smith, Chair; Representative Luciano "Lucky" Varela, Vice Chair; Representatives Don E. Bratton, Don Tripp (for Brian K. Moore), Rhonda King, Patricia Lundstrom (for Henry "Kiki" Saavedra), Edward C. Sandoval, Jeannette O. Wallace, Nick L. Salazar, and ;and Senators Sue Wilson Beffort, Linda Lopez (for Timothy Z. Jennings), Phil A. Griego, Leonard Lee Rawson, Carol Leavell (for Joseph J. Carraro), Carlos Cisneros, and Pete Campos. Representative Raymond Begaye attended as a Guest.

Election Readiness and Budget Projections.

Mary Herrera, Secretary of State, confirmed that an election training school was conducted last week for all county clerks and voting machine technicians.

In 2007, a team completed testing of all state-wide voting machines. Election supplies have been ordered and will be delivered directly to the county clerks. A second testing of cards used with the M100 voting equipment is in process. The agency was awarded a Help America Vote Act (HAVA) grant and used the funds to create a video for poll worker training. A limited supply of HAVA compliant equipment is available and will be sent to various polling places.

On Friday prior to Election Day a representative from ES&S (the vendor) will be on site at the Secretary of State's office to assist individual counties with roster printing issues that arise with the voter registration system. A team of attorneys from the Attorney General's Office (AG) will be present at key locations on Election Day to assist the county clerks, staff and presiding judges.

A phone bank will be open during Election Day to assist the county clerks. A new website at the Secretary of State will be up April 28. Preparations are being made for early and absentee voting and the state will be able to report unofficial election night results. The public financing voter act program forms, procedures and instructions have been revised. All qualifying candidates received their eligible funding. Several voter information manuals have been updated and were distributed to the county clerks.

Additional voting machines were issued to counties who created new precincts within their jurisdiction. One extra voting machine was issued to each county for an optional process of tallying absentee and provisional ballots. Eight voting machines will be on reserve for emergency circumstances. Three thousand draft ballots have been printed for county certification. Ballots statewide will be ready for absentee voting beginning May 6, and early voting May 17.

Don Francisco Trujillo, deputy secretary of state, noted that the agency received a $3 million appropriation to cover costs associated with the 2008 primary election. The agency still had a $595.3 thousand shortfall and requested a loan from the board of finance (BOF) which was approved.

Neither the hardware, firmware nor software supporting the election process is under warranty. The Secretary of State is working with the BOF for an additional loan of $305 thousand for the firmware, software, maintenance and support on all the voting machines on behalf of the counties. The vendor has been determined to be the sole source provider for the firmware and software on their own voting machines. The Secretary of State can enter into a one year contract for the firmware and software to cover both the primary and general elections.

Legal counsel at the AG is determining if the Secretary of State has the legal authority to transfer ownership of the state-purchased voting machines to the counties.

The Secretary of State's Office is $1.2 million short for the general election in November. A request was made to the legislature for $4 million, and $3 million was appropriated. There is $600 thousand remaining in the BOF loan fund this fiscal year. If the Secretary of State's office borrows $300 thousand for the firmware, software, maintenance and support there will be a balance of $300 thousand in the loan fund. The Secretary of State will be requesting in June to borrow this remaining balance of $300 thousand in the loan fund. An additional $900 thousand will be requested the start of the new fiscal year which together with the $300 thousand will provide the $1.2 million that is short for the general election in November. Should the Governor call a special election, the Secretary of State will submit an appropriation request to pay back the BOF to conduct the primary and general elections.

Cheryl Nichols, president of the Association of County Clerks and Los Alamos County chief deputy clerk, and Denise Lamb, Santa Fe County chief deputy clerk, expressed concerns on behalf of county clerks over the voter registration system and lack of support from the vendor regarding functionality issues. Since its 2000 installation the voter registration system has never run an absentee roster correctly. There is concern there are not enough extra memory cards to protect against card failure. There is a lack of administrative rules for statutes enacted by the Legislature since 2007 that changed procedures in the election code. The most serious problems with the voting equipment are not covered under maintenance contracts. Memory card failure has been experienced with these voting machines in every election the counties have held.

A detailed list of additional concerns facing the county clerks in the primary election was provided to the committee.

There is one vendor who owns the state wide voter file, all the voting equipment and the campaign reporting software. The counties are facing over $1.3 million in maintenance costs built in by the vendor, with no protection afforded the state. The vendor is not required to train county technicians on maintaining equipment.

Representative King stated when the state moved to a paper ballot system, it changed the process by which voting machines are purchased. State statute provided that county clerks had that responsibility. County clerks would request from the BOF a loan from the election fund to purchase voting machines. Existing statute required the county clerks to maintain the voting machines. With passing of the statute that moved the process to a paper ballot system, the legislature gave the authority to the Secretary of State to purchase the machines. The former Secretary of State purchased paper ballot machines with state and HAVA funds. Representative King introduced legislation that was vetoed which included a hold harmless provision for the county clerks for the remaining $1.3 million owed on the old voting machines.

Representative King requested the LFC prepare a letter to the AG addressing concerns to ensure the state has accurate elections.

The committee also expressed concerns over maintaining voter confidence in the election process in New Mexico.

The projections for the number of ballots needed is based on the number of registered voters eligible, not on voter turnout. The Secretary of State has purchased ballots for 150 percent of that number to allow for provisional ballots, mistaken ballots, ballots for voters who by law are to be sent absentee ballots, and to simply be prepared if all voters do turnout to vote.

Secretary of State Herrera stated New Mexico always has a close race on election night. There are thousands of provisional ballots that cannot be counted on election night during the canvas.

Representative Begay requested the secretary of state to provide more detail on the locations of voting machines on Indian lands to ensure Native American communities are prepared for the primary and general elections.

The committee heard discussion on an administrative ruling established by Secretary Herrera to allow for remarking in the case of voter error. The committee expressed concerns with canvassing staff remarking ballots and the perceived integrity of the election process.

Secretary Herrera expressed confidence to the committee that the state is ready to run the primary election and that all rules have been issued.

Action Items

Vice Chairman Varela moved to adopt the March 2008 minutes, Senator Smith seconded the motion, and it passed with no objection.

The committee adopted amendments to professional services contracts for Helen Gaussoin of $3.5 and New Mexico State University for $10.0. Vice Chairman Varela moved to adopt the amendments, Senator Smith seconded the motion, and it passed with no objection.

Director Abbey presented proposed dates and locations for the interim meeting calendar. An updated calendar will be mailed Monday, April 28, to committee members.

A field trip report for Chihuahua, Mexico in September was provided to the committee. A representative from NMSU was available to answer questions about suggested activities within the trip report.

Information Items

Director Abbey provided the following reports to the committee:

- The LFC Budget Status for March 2008
- The LFC Cash Balance Report for January 2008
- The LFC Budget Adjustment Report for March 2008
- The LFC Operating Budget for FY09

Chairman Smith adjourned the committee at 11:00 a.m.

Chairman

5-7-08

Date