MINUTES
LEGISLATIVE FINANCE COMMITTEE
January 14, 15, 16, 2009

January 14, 2009

The following members were present on Wednesday, January 14th: Chairman John Arthur Smith, Vice-Chairman Luciano "Lucky" Varela, Representatives Donald E. Bratton, Rhonda King, Don Tripp (for Brian K. Moore), Edward C. Sandoval, Jeanette O. Wallace, Nick L. Salazar, Henry "Kiki" Saavedra; and Senators Carlos R. Cisneros, Sue Wilson Beffort, Carroll H. Leavell (for Leonard Lee Rawson), Phil A. Griego, Mary Kay Papen, and Pete Campos. Representatives Larry Larranaga, John A. Heaton, Mimi Stewart, and Senators Cisco McSorley, and Bernadette M. Sanchez attended as guests.

Update on US and New Mexico Economy and Energy Markets. Laird Graeser, Chief Economist, Department of Finance and Administration introduced Dr. Jim Nunns, Taxation and Revenue Department, and Norton Francis, Chief Economist, Legislative Finance Committee. Mr. Graeser began his presentation by saying a mid-session review would be delivered to the committee on February 13th. A stimulus package that President-Elect Obama has discussed is expected to create between three and four million jobs by the end of 2010. Tax cuts, especially temporary ones, and fiscal relief to the states are likely to create fewer jobs than direct increases in government purchases. However, because there is a limit on how much government investment can be carried out efficiently and in a short time frame, and because tax cuts and state relief can be implemented quickly, they are crucial elements of any package aimed at easing economic distress.

Certain industries such as construction and manufacturing are likely to experience particularly strong job growth under a recovery package that includes an emphasis on infrastructure, energy, and school repair. General simulative measures, such as middle class tax cuts and fiscal relief to the states, as well as the feedback effects of greater employment in key industries, mean jobs are likely to be created in all sectors of the economy.

More than 90 percent of the jobs created are likely to be in the private sector. Many government jobs are likely to be for professionals whose jobs are saved from state and local budget cuts by state fiscal relief. It is also likely to move many workers from part-time to full-time work.

Fiscal effects in New Mexico need to be divided into direct support for the general fund and indirect support through other economic activities. New Mexico will be funded primarily through the federal medical assistance percentage (FMAP). Vice-Chairman Varela asked if money would go directly to departments or to the general fund and if there was control over it. Mr. Francis explained that the general fund appropriation for Medicaid is matched by the federal government and would increase from 71 percent to 75 percent without changing general fund appropriations. Vice-Chairman Varela suggested the committee adopt a policy that if and when funds are received and the Legislature is not in session, the Legislative Finance Committee establish a hearing on the budget increases that will occur as a result of the stimulus package.

Mr. Graeser said in addition to the important direct support of the state general fund, there will be additional direct money to agencies. Funds will not flow out within one year; they will flow out over a 27-month period. A lot of the proposals that will be enacted in February will be back-dated either to the beginning of the federal fiscal year or to January 1st.

Dr. Nunns continued with the stimulus package and said it includes increases in food stamp spending and unemployment benefits. The broad outlines of the proposed tax cuts are known, but do not include details. Individual tax cuts include $500 for single tax payers and $1,000 for married tax payers. Four proposals are considered for business tax cuts and include a credit of $3,000 for each new job created by a business, extending the bonus depreciation provision included in the 2008 stimulus package (affecting state revenues), small business expenses increasing the limit of investments (also included in the 2008 stimulus package), and a provision to extend the corporate net operating loss carry backs from two to five years.

Mr. Francis reported that the congressional budget office has projected over 9 percent unemployment in FY10 for the U.S. economy. Consumption has also decreased by more than 1 percent in 2009 and financial markets continue to be strained for at least the short term. New Mexico's employment is forecasted to decrease 0.6 percent in FY09 and decrease another 0.1 percent in FY10 and finally begin to increase in FY11 with a 1.7 percent increase. New Mexico's personal income has very slow growth in FY09 with a 2.3 percent growth compared to FY08's growth of 6.3 percent. The growth will be even slower in FY10 with 1.3 percent growth and will finally begin to increase again if FY11 with a 3.8 percent growth. Mr. Francis also explained the risks to the December 2008 revenue forecast, that included the baseline, optimistic, and pessimistic forecasts from BBER, show key drivers have begun deteriorating since November's forecast. Gross receipts and personal income taxes are driven by New Mexico wages which have dropped 1 percent in FY09 since the November forecast and have dropped 1.3 percent in FY10 since the November forecast.

Mr. Graeser continued with falling energy prices and said New Mexicans purchase 900 million gallons of gas in the course of a year representing on the order of $2 billion in displaced consumption. Oil and gas prices are linked to the fortunes of the national economy; as demand shrinks, it drives prices down. Special attention is given to specific behavior of New Mexico prices compared to the national aggregate. ONGARD prices are higher than expected from the data given by the Department of Energy. Mr. Francis added that the September ONGARD prices are derived from actual production and value in New Mexico, not a country-wide aggregate. In response to Chairman Smith's concern, Mr. Graeser said the consumer confidence index is at a virtual all time low and has been for two months.

Actual revenue numbers from the Financial Control Division have not been received for FY08 and monthly reports have not been received for FY09. The current gap in revenues total $454 million. Mr. Anthony Armijo, Director, Financial Control Division, Department of Finance and Administration said numbers received from the Gentex System from Taxation and Revenue Department (TRD) go through an audit process to make sure numbers are correct. The numbers from the system had not been correct; however, new numbers were received. The system contains a rule specifying if tax receipts cannot be identified within 60 days they are sent to the general fund. It is believed that unidentified tax receipts are going to the general fund prior to the 60 days. Representative King suggested working with LFC staff to resolve these issues.

Mr. Graeser added that the TRD Audit Division contains a section that comprehensively audits all state revenues throughout the ONGARD system on the tax side. Each of the other ONGARD participants audit their own pieces of the overall system. In addition, a federal audit is devoted to auditing royalties on federal land. Representative Bratton asked if issues and the disconnect in the audit process are reviewed. Dr. Nunns responded that there will be cases where records for the tax department are not going to match the tax payers records.

Overview of General Fund Solvency Plans for FY09. David Abbey, Director, Legislative Finance Committee proposed four bills addressing fund transfers, appropriation reductions, reinstatement of the quarterly corporate income tax, and capital outlay. These four bills would implement the LFC staff recommendations presented to the Committee in December. Based on the revenue estimates in December and current spending, money will be needed for specials, supplementals, and IT. Director Abbey referred to NMSA 6-4-6, Expenditures authorized to maintain cash flow, and said the general fund appropriation account is always in the red, and, with the current projections, it can not be repaid at the end of the year. HB2 contains a fund transfer section indicating if there is a revenue shortfall; money can be taken out of the operating reserve to cover the appropriations account. Director Abbey suggested for the current year as well as the following year allowing transfer authority in the event there of a revenue shortfall.

Director Abbey recommended rolling back an increased distribution from the Fire Protection Fund to fire districts and moving money from accounts in the treasury to the general fund as one time revenue. Amounts could be transferred without impairing current year or next year's spending that has already been committed. The proposed bills would raise $114 million of general fund.

Director Abbey explained spending reductions and said it is recommended to reduce Medicaid by 1 percent, public education by a net of 1 percent with an additional 1.5 percent reduction offset by 1.5 percent spending from the lock box. It is also recommended to reduce the courts by 1.35 percent and 2.5 percent for all other agencies. Other recommendations include reducing special appropriations by $22.5 million and capital outlay appropriations by $63 million.

The final item involves a transfer from the tax stabilization reserve to the general fund in the amount of $55 million for the personal income tax rebate enacted in special session. To access the tax stabilization reserve it would be useful to have a declaration by the Executive requiring a two-thirds vote of the Legislature. In addition, $21 million for supplementals and deficiencies and $8 million for the Feed Bill would get general fund reserves back to 9.9 percent.

Katherine Miller, Secretary, Department of Finance and Administration, reported the difference between the FY09 revenue estimate and appropriations of $454 million. In FY08, there were better revenues than estimated. In order to maintain ten percent reserves at the end of the year based upon the December revenue estimate, $384 million plus spending initiatives for the 2009 session is needed. The difference between the LFC recommendation and the Executive is $75 million; the Executive set a target of $460 million. Secretary Miller continued to explain the proposed budget solvency plan for the Executive. Recommendations were based on information obtained from agencies totaling approximately $19 million. It is also recommended to de-authorize $32.5 million from the special session. Vice-Chairman Varela asked about the LFC staff recommendation. Director Abbey responded that a $22.5 million reduction was recommended because an amount was identified from TANF funds that could replace some of the reduced funding.

Secretary Miller continued with a summary on potential capital outlay de-authorizations including $58.4 million from public schools. DFA and LFC staff identified projects totaling $59 million for de-authorization including the Governor's initiatives. In addition, projects for agencies and local governments that are not able to show established contracts have been added to the potential list of de-authorizations. Over $42.3 million in projects valued under $50,000 or under that were authorized in the 2007 session or prior have not been expended.

<u>Discussion of Legislation to Transfer Funds to the General Fund and Other FY09 Revenue Measures.</u> Mr. Norton Francis, Chief Economist, Legislative Finance Committee reported on the proposed legislation to transfer funds to the general fund. It is comprised of three sections including a transfer in revenues, a reduction in appropriations, and moving of appropriations and funds to achieve budget solvency. Sections 1 and 2 of the bill reduce legislative appropriations by 2.5 percent and Senate Bill 165 (commonly referred to as the junior bill) by 2.5 percent. Section 3 authorizes a balance transfer of state funds to the general fund that are no longer required for the intended purpose. Section 4 creates a new distribution from the Tobacco Settlement Permanent fund. Under the current law, 50 percent of the master settlement agreement payment goes to the Tobacco Program Fund and 50 percent goes to the permanent fund. The proposal diverts 100 percent of the master settlement agreement payment to the program fund for two years. Section 5 freezes the transfer from the Fire Protection Fund for two years at the current level and restores the transfer. Section 6 reduces the 2008 special session health appropriations to $10 million and pro rates it according to this amount. Section 7 appropriates from federal funds (Temporary Assistance for Needy Families, TANF) to restore amounts appropriated in the special session. The TANF funds will be based on certification by the Board of Finance that the Human Services Department (HSD) has applied for and received funds. Section 8 appropriates from the Tobacco Settlement Program Fund to HSD to replace general fund appropriations in the Medicaid program. Section 9 is an appropriation from the education lock box and is part of the contingency fund. Section 10 transfers $55.7 million from the tax stabilization reserve and funds the 2008 special session rebate rather than using the appropriation account. The final section of the bill repeals House Bill 546, Chapter 50, Laws 2008 which appropriated excess amount in the Tobacco Program fund. Vice-Chairman Varela asked what statute or authorization allows spending in the reserves to cover the general fund at the end of the year. Mr. Francis responded that language would be incorporated into the normal course of passage of House Bill 2.

Mr. Francis reported on the proposed bill for Corporate Income Tax Payments and said it is part of the executive plan to restore an omission in the 2003 tax law that set up new methodology for quarterly payments, but left out the April 15th payment. The bill shifts all the corporate income tax payments forward allowing for $65 million non-recurring revenue in FY09. Vice-Chairman Varela asked if companies and corporations were notified of the change. Mr. Nunns responded that a notice will be sent to companies which made an estimated tax payment and a press release also will provide notification. A follow-up notice will also be done if legislation passes. Senator Beffort suggested sending notices to all chambers of commerce and ACI. Representative Heaton said penalties would also need to be incorporated for the first year. Mr. Nunns said if corporations' profits are lower in the current year than in the prior year, they can use current year estimated profits to determine their estimated payment. Representative Bratton suggested adding language for a threshold to those who qualify to pay half of their first quarter estimates on April 15th and half with the second quarter payment on June 15th. Director Abbey said language would be incorporated into the bill.

Program Evaluation of Medicaid Care (Physical Health). Charles Sallee, Program Evaluation Manager, Legislative Finance Committee, reported that Medicaid constitutes a major source of health care funding in New Mexico. The Human Services Department (HSD) administers Medicaid which is a federal-state-funded program for financing health care services for low income groups and covers over 450,000 New Mexicans. Total spending for the program has reached over $3 billion with the federal share exceeding 70 percent. Since FY04, appropriations from the general fund for Medicaid have nearly doubled from $408 million to almost $790 in FY09 and accounts for 13 percent of state spending. Managed care has become a primary vehicle for financing and coordinating the delivery of physical health services for most Medicaid clients. Approximately 292,000 New Mexicans or 65 percent of all Medicaid clients participate in managed care and may chose from four managed care organizations for their physical health care needs. State law requires HSD to provide Medicaid through a capitation managed care. Capitated managed care is an arrangement in which the state pays managed care organizations a fixed monthly fee per client member to provide or arrange for health care services.

New Mexico implemented managed care in an effort to improve the health status of recipients and stabilize and lower costs. Spending on the physical health portion of Medicaid managed care has increased 30 percent from $888 million in FY06 to $1.1 billion in FY08 and accounts for 35 percent of all Medicaid spending. HSD has experienced an annual growth rate for this program of 14 percent between FY06 and FY07 and 13 percent between FY07 and FY08.

The Legislative Finance Committee (LFC) evaluation staff reviewed the cost of the physical health portion of the Medicaid managed care program and related performance outcomes. Overall, significant opportunities exist to lower the cost of Medicaid managed care and slow future growth in the program expenditures without reducing enrollment or changing benefits. Medicaid managed care needs adjustments to MCO rates bringing state payments in line with program costs, a modernized payment framework for outpatient services, additional oversight of MCO network costs to ensure cost effective use of funding, a functioning market for purchasing health services, and more competition for MCOs to continue HSD's ability to purchase high quality care, but at a lower cost.

Mr. Sallee indicated that during the evaluation, HSD began taking action to address these areas, but continued focus areas are still needed. HSD has ensured the MCOs provide clients with sufficient access to quality services and has extensive oversight mechanisms for monitoring service delivery. Medicaid operates in a complex environment and sometimes produces conflicting policy objectives reducing managed care cost effectiveness. Focused efforts are needed by policy makers and HSD to collaboratively work together to lower the per member cost of managed care in order to afford serving additional (or maintaining) the number of enrollees in Medicaid. Making additional information on both the cost and quality of care in user friendly formats available to clients, the public, and policy makers would increase transparency of the program, aid in decision making, strengthen confidence in the administration of the program and improve accountability to taxpayers. Mr. Sallee reported that the evaluation was hampered by a lack of key information including the contract rates, federally approved rate ranges, and the amounts paid to MCOs for different types of clients.

According to Mr. Sallee, report recommendations are intended to position the physical health Medicaid managed care program to continue providing quality services at more affordable and competitive prices. Medicaid managed care costs were approximately $107 million less than anticipated for FY06 to FY08 generating savings that should be accrued to this date. Proposed rates developed by HSD's actuary anticipate 85 percent of the overall premium will be spent on medical services. HSD contractually requires this amount to be spent on medical services as well. MCOs reported spending approximately 81 percent of all funding received on medical services. HSD used this as a compliance issue as part of the contract, however the contract compliance is not clearly contemplated. It appears that HSD in calculating the contract compliance has grouped the regular Medicaid managed care program and the state coverage initiative program in one calculation.

In the current contract, HSD has lowered the contract target for medical spending from 85 percent to 80 percent; it is recommended that they go back to the 85 percent. Public Regulation Commission (PRC) reports were reviewed on MCOs to look at the overall financial health; all MCOs are financially healthy and have been able to achieve medical costs at a lower level that projected by the state. Medical spending by the MCOs has increased 27 percent and is driven in part by enrollment and a significant portion is related to medical price increases.

Outpatient costs include ambulatory surgical centers, emergency room visits, urgent care, outpatient lab and radiology x-rays, and other. These costs have increased 40 percent and are significantly more costly than inpatient services. The rate of growth is substantial for the program and the average cost experienced by MCOs is growing at uneven rates. The majority of outpatient services operate on a payment methodology where the MCOs pay a percentage of what the provider charges. Other payers such as Medicare and other state Medicaid systems have moved to a prospective payment system. HSD has recognized this problem and is taking intermediate action to address it.

Subcapitation payments have increased 77 percent from FY05 to approximately $67.8 million in FY08. The department needs to gather more information about this service to determine the cost effectiveness with this payment approach. Approximately 89 percent of subcapitation payments are made to manage the care of low income children. It appears that there is one MCO driving the overall cost and as a result has the most expensive medical cost for what is otherwise a relatively inexpensive client group to cover.

Enrollment has rebounded from FY05 and did not reach projected levels until FY08. During FY06, large balances could have accrued at HSD because higher enrollment was projected. At the beginning of each fiscal year, the department makes projections about how many clients they feel are going to enroll into the program. The major client group driving overall enrollment are low income children. Provider fee increases have been a cost driver in the system and additional increases are not warranted. Not all provider fee increases for FY07 and FY08 were needed and should be recouped by the department from the MCOs.

The Legislature appropriated more than $101 million in state and federal Medicaid funding for provider fee increases in FY07 and FY08 across the entire program. The physical health MCOs received 49 percent of the total provider fee increase in FY07 and 40 percent in FY08. These provider fee increases increased the overall medical cost for the physical health MCOs by an estimated 3.5 percent between FY06 and FY07 and less than 2 percent between FY07 and FY08. The methodology that the department's actuary utilizes to develop the managed care organization rates assumes increases in medical prices. MCOs and providers have the ability to negotiate their own rates utilizing the Medicaid fee for service rate as a benchmark. Few primary care providers may have received a significant portion of these fee increases since 15 percent serves over 70 percent of the Medicaid managed care clients. Less than 3 percent have 25 percent Medicaid clients assigned to their care.

In developing the rates and understanding how the network is operated, HSD needs to have a good grasp of what the MCOs are paying for its provider network. Some of the MCOs have affiliates that are within their overall corporate structure and are also providers. It is important for HSD to monitor those relationships making sure payments between an MCO and an affiliate are an appropriate amount.

Other opportunities exist to realign incentives and improve efficiency saving money and creating better value for tax payers purchasing health care for low income New Mexicans. Prior to 2003, the federal government required that managed care cost as much or less than the fee for service program. After 2003, the federal government changed those regulations to a form of cost plus contract. Part of the rate setting process requires the actuary to set an upward bound range and a lower bound range to account for variances in the program. Authority has not been used to exercise price competition and limitations have been placed because of the structure of the program. Using four managed care organizations creates additional inefficiencies in administration and adds a burden for providers.

Mr. Sallee reported HSD has been recognized for having a national best practice for encouraging performance on the part of the managed care organizations. The department withholds a portion of the overall contract and the MCOs have to earn that portion of their overall premium by meeting performance indicators. The department also allows MCOs to keep penalties, but directs them on how they can spend them. Transition to actual health care outcomes would better inform the Legislature and the public regarding the health of the Medicaid population.

Medicaid managed care can have a big impact on the overall health care quality within the system. According to the Department of Health's (DOH) statistics, Medicaid pays for 55 percent of births in the state and as a result, Medicaid performance should have a big impact on birth outcomes. Overall state rankings are worse than average for prenatal care during the first trimester and is an area of focus for the department. Comprehensive prenatal care can help reduce pre-term births and infant low birth weight rates, risks for neurodevelopment handicaps, and congenital anomalies and respiratory illness in infant mortality. According to national estimates, 69 percent of women in New Mexico receive prenatal care during their first trimester. In calendar year 2007, only 25 percent of women in the Salud program (physical health managed care program) were enrolled for their full pregnancy. Early enrollment creates better opportunities for the MCOs to improve the state's performance in this area. Forty-five to 68 percent of women receive the recommended frequency of prenatal care during their pregnancy while enrolled. Given the fact that Medicaid pays for such a large number of births in the state, newborns account for 10 percent of all medical spending. Medicaid does not track or report birth outcomes such as low birth weight, mortality, or newborns receiving intensive care. Childhood asthma is the leading chronic condition for children. Poor control of asthma symptoms can lead to expensive emergency room and hospital costs. Asthma disproportionately affects low income children who also experience higher rates of asthma morbidity and mortality due in part to disparities in treatment. Diabetes is another chronic condition that has a lot of high costs and HSD and the MCOs have begun collecting data.

Mr. Sallee recommended separating the Medicaid block grant appropriation in the General Appropriation Act into smaller components to allow the Legislature to increase budget transparency and authority directing Medicaid resources. The department has noted that MCO rates have been lowered and estimates a $38 million savings; it is recommended that the department continue moving in this direction. It is also recommended the department continue to lower the target for overhead cost to MCOs. The department needs to make requested information available and staff will continue to work with them to develop a workable agreement. The department should collect and require MCOs to report additional information regarding subcapitation arrangements. It is recommended to reduce the number of MCOs in FY11 to no more than three and lock in rates for FY11 and FY12.

Mr. Al Llama, Attorney General's Office reported that the agency received an opinion request regarding information requests to agencies made by the Legislative Finance Committee and the relationship that exists between requests for information under statute by the LFC and Inspection of Public Records requests. The agency did not conduct an analysis or make a determination on the availability of specific Medicaid information under the Inspection of Public Records Act. Instead, the opinion discusses the authority the LFC has to request information from agencies and states that an LFC request is not considered an inspection of public records request. LFC has separate statutory authority to request information and is not considered a third party requests, such as those of the public. In statute there is reference to an agency's ability to decline a request for information if that information is made confidential by law. Mr. Lama stated that there must be some law in order for the agency to decline the provision of documentation. The opinion also discusses the issue of protection for confidential information obtained by the LFC. If information was provided by a department that was not mandated as confidential under law, there is no provision excluding it to a third party. Any agency of government subject to requirements of the law has to comply with provisions and may exclude the provision and information if there is a law, specific exception in the Inspection of Public Records Act, or counter veiling public policy consideration. Counter veiling public policy is a valid justification for non-disclosure of a record under the Inspection of Public Records Act. It can not be used interpretively if there is another statute that authorizes disclosure of information.

Mr. Llama said he does not know of any law that deems the requested Medicaid information confidential. Procedures could be implemented allowing the LFC to review the information, but not take custody or control of it. Another solution is to amend the statute. Vice-Chairman Varela said there is a difference in interpretation from the department. The LFC has the authority to subpoena records that are pertinent to the functions of the committee. Mr. Llama suggested working the department to resolve the disputed issues. References in the letter from the department do not reflect the full scope of the opinion and the decision from the Attorney General. Director Abbey offered to meet with Secretary Hyde to revisit the issues. There is an ongoing concern to obtain good information in order to develop recommendations to the committee and the full Legislature. Vice-Chairman Varela said he is concerned with amending the current statute. In the past, the LFC was able to sign an agreement not divulging information once it was made available. Director Abbey said he would be supportive in offering that agreement. Mr. Llama said it is possible to identify in some form of agreement that the LFC, as the custodian of the document will maintain the same basis for non-disclosure as the department.

Secretary Hyde said there is a very limited amount of information that is being preserved from the public because it helps to obtain lower rates for the state and has been determined in court. There is not a problem with releasing information to the LFC; it is a concern that the LFC would be subject to losing in a court battle and would have to turn the information over. The department has proposed language for statutory change making it clear that the LFC has the ability to keep information confidential once it is obtained.

Secretary Hyde said the department received 28 recommendations and agrees with all or some version of 20 of them and has concerns with eight of them. Ms. Carolyn Ingram, Deputy Secretary, Human Services Department presented an overview of the recommendations that were agreed upon and will be implemented to the extent resources are available. Secretary Hyde presented the recommendations the department disagreed with.

January 15, 2009

<u>The following members were present on Thursday, January 15th:</u> Chairman John Arthur Smith, Vice-Chairman Luciano "Lucky" Varela, Representatives Donald E. Bratton, Rhonda King, Don Tripp (for Brian K. Moore), Edward C. Sandoval, Jeanette O. Wallace, Nick L. Salazar, Henry "Kiki" Saavedra; and Senators Carlos R. Cisneros, Sue Wilson Beffort, Carroll H. Leavell (for Leonard Lee Rawson), Phil A. Griego, Mary Kay Papen, and Pete Campos. Representatives Larry Larranaga, John A. Heaton, Mimi Stewart, Danice Picraux, Robert "Bobby" Gonzales, and Senators Cisco McSorley, and Bernadette M. Sanchez attended as guests.

<u>**Discussion of Legislation to Reduce FY09 General Fund Expenditures.**</u> Mr. Gene Moser, Principal Analyst, Legislative Finance Committee, reported on recommendations for FY09 Solvency and general fund adjustments to the GAA. The proposed bill reduces the GAA appropriations by 2.5 percent for all state agencies except the judiciary which is reduced by 1.35 percent, Medicaid by 1 percent plus $24.55 million, and public school transportation by $4 million. Section 1, subsection A of the bill reduces general fund appropriations in Section 4 by $125.171 million or 2.5 percent. Subsection B reduces the general fund appropriations in Section 4 to the courts and related court offices by $2.046 million or 1.35 percent.

Appropriations are made by agency, program and category; the bill directs the reductions to be made in the same manner. Subsection C reduces the general fund appropriation in Section 4 to the medical assistance program and the Medicaid behavioral health program of the Human Services Department by 1 percent. Subsection D further reduces the general fund appropriations in Section 4 of the GAA to the medical assistance program of the Human Services Department in the other category by $24.5 million. Subsection E reduces the general fund appropriation in Section 4 of the GAA for public school transportation by $4 million appropriating $4 million for supplemental funding to school districts for anticipated increases in school bus fuel costs. Subsection F directs the state budget division of the Department of Finance and Administration to reduce all appropriations under the other state funds, internal service/interagency transfers and federal fund columns to reflect the general fund reduced appropriations.

Section 2 addresses Budget Adjustment Authority (BAR) for state agencies allowing movement of funds within program from one category to another. Currently, agencies may request transfers into personal services and employee benefits and may request transfers out of personal services and employee benefits if the cumulative effect of the transfer plus all previous transfers out of personal services and employee benefits does not exceed two percent of the total appropriations to that category.

Section 3 reduces appropriations contained in Laws 2008, Chapter 3, Section 5 that are no longer needed or will not be expended in FY09.

Section 4 reduces all general fund appropriations by $901.8 million or 2.5 percent. Language is included to clarify that agencies shall use other funding sources to provide salary increases as appropriated by the legislature in that section.

Ms. Dannette Burch, State Budget Director, Department of Finance and Administration added that agencies were asked to provide 5 percent reduction plans; exemptions to the reductions are recommended. Health and human service agencies could not provide a 5 percent reduction without cutting services.

Director Burch provided a list of proposed bills that require amendments and include HB1, HB 2, and SB 165. Because appropriations in SB 165 are named individually they are set up in the budgetary system as individual operating budgets. Some appropriations have been fully expended, therefore imposing a 2.5 percent reduction against those individual projects means they are over-expended. A list of SB 165 appropriations with actual expenditures and encumbrances to date will be provided to assist with deliberations.

Director Burch said there are concerns with budget reductions and the anticipated events that could occur after the session and the bill has passed. More budget flexibility is needed for transfers between programs and increased budget authority. In 1996, the Legislature addressed this issue by re-enacting Section 4 with lump sum appropriations.

Mr. Moser said recommendations for the Executive and the LFC are similar. The LFC is proposing a 1.5 percent average reduction versus 1.7 percent for the Executive. Vice-Chairman Varela asked when reduction of allotments begins. Director Burch said there have been initial conversations about how this bill will be implemented. Currently, allotments are done at the beginning of each month and it is recommended to recalculate what monthly allotments should be through the end of the year and lowering them so that allotments to state agencies are equal split. Monies have already been allotted for SB 165 and other special appropriations. Vice-Chairman Varela asked if there will be enough time to reduce the budget as well as the allotments. Director Burch said schedules of allotments are approved by the State Budget Division. The Financial Control Division carries out the actual allotment.

Senator Beffort said she requested a list of the 400 hires made after the hiring freeze and recommended they be considered as part of the reduction. Director Burch responded that all hires and expenses for those employees are contained within 5 percent plans. With the reductions that are recommended from both branches, agencies will still be able to balance budgets. Some of the hires were not general fund and are being paid out of other funds and some positions are essential. Senator Beffort asked if there was discussion of selected reductions of unauthorized hires. Director Burch responded that the Executive reduction plan represents reductions proposed by the agencies. Senator Beffort said there has been a budget increase from \$3 billion to \$6 billion consisting of more directors and deputy directors. Mr. Moser said staff has taken an aggressive approach in reviewing unauthorized exempt and exempt positions and will be addressing it in budget recommendations. Vice-Chairman Varela suggested the Personnel Act be reviewed because the hiring authority and the evaluation agreement have become decentralized. Legislation needs to be developed to address the personnel system for all branches of government.

Chairman Smith asked about the reduction of the Gila water appropriation. Director Burch said the administration is not proposing to cut the appropriation. A plan is in place to spend the entire amount on different studies that are needed. Chairman Smith requested time tables on the plan before action is taken. Director Abbey added that part of the LFC recommendation stemmed from an announcement that the executive was not going to pursue construction of the dam on the Gila.

Discussion of Legislation to Reauthorize Capital Outlay Appropriations. Linda Kehoe, Principal Analyst, Legislative Finance Committee reported on the proposed solvency solution. Ms. Kehoe indicated that in October 2008, the Governor outlined a plan to address the general fund gap including reauthorization of \$200 to \$300 million in stalled capital projects, and the LFC directed staff to identify \$150 million in stalled capital projects for consideration in addressing the solvency issue. Staff developed criteria to identify proposed projects and the majority of projects reviewed were taken from the \$1 million or greater list. Criteria included: inadequate planning or funding to move the project forward, funds sitting idle for two to three years, a lack of funding at the local level to support operational and maintenance costs, federal funding needed for the project that didn't materialize, third-party agreements not in place, projects that could not meet contingencies, funding declined by the grantee, or unused balances for projects already completed. Representatives were contacted at both the local and state level to derive information regarding the status of projects. When staff obtained copies of Requests for Proposals, construction contracts, time tables, award letters, and other information needed to validate, sometimes there were no valid third party obligations. As of this date, 89 projects were identified totaling \$163.3 million for potential reauthorization. The proposal voids 56 general fund projects totaling $136.8 million and 24 severance tax bond projects totaling $26.6 million. Of the voided severance tax bond projects, $26.5 million would be used to swap and continue ten viable general fund projects. The major dollar amount includes $58.4 million from public school capital outlay award balances, $23.3 million for the Equestrian facility, $16.6 million for film initiatives, and $8.4 million from New Mexico Finance Authority water and wastewater and Smart Money program unexpended balances. LFC has not received all executive proposed projects, but has worked with the Local Government Division to review projects funded from the $1 million or greater and other state agency unexpended balances.

Robert Apodaca, Director, Local Government Division, reported that DFA and LFC have been working to concur on a number of projects. DFA has taken a different approach with respect to identifying capital outlay appropriations for solvency. Correspondence was sent out to local governments and to state agencies requesting them to assist in identifying potential projects that were stagnant, stalled, or underfunded. General fund appropriations in the amount of $228 million have been identified for potential de-authorization including balances from the $58.4 million for public school capital outlay. Agencies have identified $100 million severance tax projects and $31 million in potential swaps or reauthorizations from the general fund to severance tax bonds. Vice-Chairman Varela suggested redirecting projects rather than cancelling them. Representative Saavedra requested a copy of the correspondence that was sent out to local governments. Mr. Apodaca indicated since the letter that was sent out to local entities, an average of 115 invoices have been received each month.

Representative Sandoval inquired about funds not being released due to anti-donation issues and asked when it would be resolved. Director Apodaca responded DFA, in compliance with the anti-donation clause, is requiring an exchange of services must be equal to the value of state capital funding, and that DFA legal counsel is working with local governments to quantify projects and not violate constitutional issues.

In response to questions regarding non-profits, Mr. Rick Martinez, Deputy Director, Department of Finance and Administration suggested a statute or rule-making authority be established so that when funds are appropriated to a non-profit there is enough time to get agreements in place that are required by constitution. Representative Bratton added that funds are requested for local communities and cannot be authorized to non-profits. Funds are distributed to state agencies, county or local governments that have a responsibility to make sure paper work is in place before funds are utilized for any organization providing services.

Chairman Smith said he will recommend to the leadership on the Senate side that the entire solvency plan be proposed as a whole. In the event there are delays, it will be recommended that no bills be submitted until there is consensus with the Executive branch.

Discussion of Proposed Legislation to Ensure Long Term Solvency of Retirement Funds.
Michelle Aubel, Senior Fiscal Analyst -- Legislative Finance Committee, reported on the long-term solvency for state retirement plans. Both pension plans are defined benefit plans, creating obligations or liabilities to pay certain retirement benefits based on salary and the length of service. The percent of liability funded indicates fund solvency. As of June 30, 2007, the Educational Retirement Board (ERB) was 70 percent funded and the Public Employees

Retirement Association (PERA) was 93 percent funded; the standard is 80 percent. Funding occurs by contributions made by employers and employees; money going out paying pensions is more than the contributions coming in. The gap is filled by earnings on the investments and both plans assume a long-term 8 percent return. The ability to achieve that performance over the long-term is in question. Since the last actuarial evaluation on June 30, 2008, both funds have significantly declined, increasing the unfunded liabilities. PERA reports a 30 percent decline for FY09 as of December 2008, and ERB reports a 25 percent decline. Benefits for both plans are in the top tier of public plans in the United States. The current plans allow employees to retire at a relatively young age enjoying Retiree Health Care Authority long before becoming Medicare eligible.

David Archuleta, Senior Fiscal Analyst, Legislative Finance Committee, reported the Retiree Health Care Authority (RHCA) is facing a number of significant issues. According to their most recent actuarial evaluation as of on June 30, 2008, the RHCA is projected to become insolvent by 2019, meaning expenditures will exceed all combined revenue sources including long-term assets. The assumptions used to develop the report appear to be optimistic as it incorporates a near 8 percent return on investment complimented by a 2.5 percent increase in payroll for FY09 and FY10 with a four percent growth thereafter. Currently, the RHCA does not receive contributions for return to work employees or for the purchase of service credit. In addition, RHCA does not receive a higher contribution for employees in the enhanced retirement plans, even though those retiring from these plans will receive benefits for a longer period of time.

Ms. Aubel continued with an explanation of a drafted bill and said it creates a second tier under PERA and ERB coverage plans to increase retirement age and service credit requirements for members who first become members on or after July 1, 2009. In general, eligibility would increase from 25 years of service to 30 years of service and age 55. ERB's combination of age and service increases from the "rule of 75" to the "rule of 80." PERA's service requirements increase for those over 61 by two years. It also amends PERA's return to work provision by increasing the separation of service requirement from 90 days to 12 months and reinstates the stipulation that the return to work employee pays the employer portion of the PERA contribution. It provides for a different and more restrictive calculation of final average salary for the purposes of calculating retiree pensions.

Mr. Archuleta indicted that the proposed legislation includes conditions for the purchase of service credit for ERB and PERA on the payment of the associated statutory contributions to RHCA. The proposed legislation would also increase employer and employee contributions to RHCA for the enhanced and 20 year plans and require financial training for ERB and PERA board members.

Ms. Aubel ended by pointing out the primary policy issue as summarized by the Pew Center on the States: "the need to intelligently control and manage the costs of post-retirement benefits in order to meet competing needs such as adequate roads, water infrastructure, and high quality public education while ensuring that qualified individuals continue to be attracted to careers in public service." The decisions that the Legislature makes in the upcoming session regarding retirement benefits will impact the decisions that will be made regarding other state appropriations in future sessions.

Wayne Propst, Executive Director, New Mexico Retiree Health Care Authority (RHCA) reported that the board has not had an opportunity to take a position on the proposed legislation. RHCA's investments for the month of December were up by $5 million resulting in a 10 percent increase that was lost in the first quarter of the year. Mr. Propst stated that currently, if a member has 5 years of service they are eligible for a subsidy of 6.5 percent gradually increasing until an employee with 20 years of service is eligible for the full subsidy. The board understands very clearly that given the financial condition, nothing can be off the table including review of age and service requirements to determine whether or not that needs to be increased. It is anticipated that the board will consider a rule making to change years of service requirements. However, changing years of service for employees who are hired after July 1, 2009, will not impact solvency.

Jan Goodwin, Executive Director, Educational Retirement Board (ERB), compared the proposed bill to endorsed legislation from the board, which includes the effective date for employees who begin employment as educators after July 1, 2010. The board's proposed legislation does not require a 55 age minimum. Most retirees average 56 years of age and have 28.6 years of service; the median year of service is 28. An annual 2-day retreat is provided for board members and includes investment education, changes in laws, fiduciary duties, and an educational section for asset allocations. Proposed legislation will be provided to the board for review on February 13, 2009.

Terry Slattery, Executive Director, Public Education Retirement Association (PERA), reported that it has been a difficult time investment-wise for PERA. However, the board decided it would prefer to work with the actuaries to develop a comprehensive study to review replacement ratios, benefit structures and comparable state funds before making any changes. The average age of retirement is 58 and has been consistent over the past few years. The average active member is 44 years old with 8.5 years of service. The state police active member average is 38 years with 12 years of service and state corrections is 37 years old with 9 years of service. The board has adopted a funding policy and may have to consider increasing contributions.

Vice-Chairman Varela said the effective date needs to be consistent for the retirement funds. Mr. Pepin, Administrative Office of the Courts (AOC), noted that the report by PERA on the two judiciary retirement accounts – the Judicial Retirement Fund (JRF) that covers metropolitan district court of appeals judges and justices of the Supreme Court and the Magistrate Retirement Fund (MRF) that covers magistrates -- repeats what the PERA has been saying for many years. The most critical things to address with these two retirement accounts is that fact they are 50 percent funded from docket fees; funding should be tied to salary. There are a number of other issues with the retirement accounts, particularly the magistrate retirement plan, which is not meeting current costs. Before any issues can be addressed, the relationship between docket fees and funding of retirement has to be severed. Legislation will be proposed to move docket fees into the general fund. The general fund would then pay 19.39 percent in addition to 12 percent to the judicial retirement account. If legislation is effective in 2010, the general fund would see no impact. At some point, there is a divergence between funding by the general fund and how much is being contributed by the docket fees. It is proposed that the AOC provide an addendum to the report submitted by Judicial Compensation Commission on an annual basis showing how much money is put into the general fund from the docket fees. Over time, the percentage contributed by the general fund would increase. Judges contribute more that state employees; however, it would be the Legislature's determination as the costs for funding increased, whether there should be additional contributions from the judges. Vice-Chairman Varela suggested that the board come up with a recommendation on how much more employees and employers should contribute to the funds. Chairman Varela said he is concerned with benefits, time of service, and return to work.

Senator Beffort said it would be responsible to place a sunset on the return-to-work program in the bill. Mr. Slattery responded that other systems, along with what is good for membership, need to be reviewed. Director Goodwin said the ERB has endorsed legislation dealing with the return-to-work program. Currently, the board was due to sunset 2011 and requested to put that date out ten years. It is also requested that contributions from the employee returning to work be made into ERB by their employer. Senator Beffort said the employee should be asked to make a contribution as well. Representative Stewart requested information on the percentage of retirees using the rule of 75 and the percentage of retirees returning to work. Director Goodwin responded that the percent of retirees under the current rule of 75 is 32 percent with an average age of 60.4 years and an average of 18.4 years of service. There are 1,300 employees on the return to work program and 65,000 active members. Director Slattery said there are 52,000 active members, 21,500 retirees and 2,015 are using the back to work program. The average age of retirement is 58. Representative Stewart suggested eliminating the sunset on return to work or pushing it back.

PERA actuaries testified that changes need to be approached with caution for a lasting change. As of June 30th, the retiree liability is just under \$8 billion, meaning that all benefits can be covered to the current retirees expected to be paid out over their entire life time. PERA is not running out of money. Currently, \$100 million less is collected than what is paid out of the fund. As of June 30, 2008, PERA was 93 percent funded and the magistrate plan was 100 percent funded. However, contributions for the magistrate plan are not covering current costs. Vice-Chairman Varela asked if contributions should cover payments to retirees. PERA actuaries said not always. When a retirement plan first starts pre-funding, it has to cover more than benefit payments to retirees. If contributions are more than what is paid out, there is no reason to put funds away. The purpose of putting money in the fund and earning interest is so the ultimate contribution is less than the ultimate pay out from the fund, with the difference made up by the investment income earned from the market. What needs to be determined is the level of benefits for employees and if the current plan is meeting or exceeding that cost--and make adjustments accordingly. Representative Heaton said there is opportunity to bring parity between PERA, ERB and the judges' system. PERA actuaries responded that when the next evaluation is complete in June 2009, the experience up to that point will be incorporated going forward.

In response to a request from Representative Heaton, Ms. Aubel reported as of June 30th, assuming a negative 20 percent return for FY09 and rebounding of 8 percent in subsequent years, ERB's actuaries projected a funded ratio of 51 percent and an unfunded actuarial liability increase to \$8.2 billion from the current \$3.7 billion by FY13.

Chairman Smith asked if ERB had dealings with Vanderbilt. Director Goodwin said the ERB made a $40 million investment with Vanderbilt in May 2006. A statement will be placed on the ERB website to further explain the situation. ERB has "written down" the investment to zero and has been investigating possible avenues of action. Chairman Smith asked whose decision it was to make the investment. Director Goodwin said the investment was discussed at two separate investment committee meetings, in April and May 2006, and was voted on by the board at the May 12, 2006 board meeting. The board members present at that meeting were Chairman Bruce Malott, the State Treasurer, the Honorable Doug Brown, Secretary Veronica Garcia, PED, Gary Bland, State Investment Officer, Delman Shirley and Dr. Pauline Turner. The vote was 4-2 with descending votes from Dr. Turner and Mr. Shirley. Mr. Dan White, Economist, Legislative Finance Committee, added that $50 million with the State Investment Council was also written down to zero. There were some interest earnings; therefore it was not a complete loss. Chairman Smith asked what staff members from ERB were present at the May meeting. Director Goodwin said staff present was Mr. Robert Shulman, Staff Attorney, Dr. Evalynne Hunemuller, Executive Director, Jeff Riggs, Deputy Director, Frank Foy, Chief Investment Officer, and Sherry Lacomb, Executive Administrative Assistant. Representative Larranaga asked what the staff recommendation was to the board. Director Goodwin said at the State Investment Council meeting, Mr. Foy said the investment division recommended to invest between a minimum of $20 million and a maximum of $40 million. The investment committee meets once a month and the entire board meets every other month. The investment committee takes major investments and investments with different managers to the full board; the full board then votes on the decision.

Representative Bratton said CDOs have been an issue brought before the Committee for over a year with the possible exposure to losses. The fund that was written down to zero is only a fraction of the total money put into CDOs by the state. Representative Bratton asked how many other CDO investment funds have been written down to zero. Director Goodwin said Vanderbilt was ERB's only CDO investment. Mr. White said there were various products similar to CDOs that have had significant write downs. Representative Bratton said there should be scrutiny as to why those investments were made as well. Chairman Smith asked how many investment committee meetings there were where this fund was discussed. Director Goodwin said the investment was discussed at two separate committee meetings. Chairman Smith asked what the issue was that was not resolved at the first meeting. Director Goodwin said the committee began preliminary discussions largely because of how ERB would classify the investment. They decided to defer until more information was received from the investment consultant and had further discussion with the State Investment Council.

Senator Griego asked how often is an investment of that magnitude made without the director being present. Director Goodwin responded that the director was present for all votes. Senator Griego asked if a firm is studied when making an investment to them. Director Goodwin responded that ERB's investment consultant worked on the investment. Staff also conducted research on the company and at the time it was a highly regarded firm.

Representative Larranaga asked how many of the members that voted for the investment are still on the board. Director Goodwin said neither of the two board members that dissented on the vote is on the board. Senator Papen asked if the selection of Vanderbilt was a sole selection or if there were several people that applied for the monies. Director Goodwin said staff had become aware of the Vanderbilt investment and after due diligence they brought forward a recommendation to invest. There are times where an RFP is issued with many firms replying. Managers are selected to compare their investment results, statistics, and investment strategies before making a decision. Ms. Goodwin indicted that the investment staff led by Mr. Foy conducted extensive due diligence and worked with the consultant and strongly recommended the investment. (STAFF NOTE: New England Pension Consultants provided an analysis that listed both the strengths of the Vanderbilt and the negative risks of the investment in an April 16, 2006 letter, which cannot be characterized as "strongly recommending" the investment.)

Chairman Smith said the board may need to be restructured and removed from executive appointment.

Vice-Chairman Varela requested a list from PERA and ERB of employees who have returned to work with a salary over $40 thousand. Director Slattery said by definition, if they are a retiree in the back-to-work program, they are receiving their pension. If they suspend their pension, they are no longer considered a retiree and have to pay a contribution. Director Goodwin said the average earnings for return to work members is $39 thousand. Vice-Chairman Varela asked how many return-to-work members contribute to the Retiree Health Care Authority. Director Propst said it is the Department of Finance and Administration's (DFA) interpretation that return to work members should not pay the Retiree Health Care portion. Vice-Chairman Varela suggested that all elements that can be implemented administratively and statutorily be reviewed. There is a sunset on the income tax provision to be considered for removal, allowing it to be continued revenue for RHCA.

Standards Based Assessment, Public Education Department. Craig Johnson, Program Evaluator, Legislative Finance Committee provided a review of the Public Education Department (PED) assessment program. Mr. Johnson said New Mexico could develop an effective assessment at a lower cost and PED's management of contracts could be improved. No child left behind requires annual assessments in math and reading and is administered to all students in grades 3 through 8 and a grade level in high school. Assessments in science are required once in elementary school, once in middle school, and once in high school. The purpose of the state's assessment and accountability act is to comply with no child left behind and requires an assessment system aligned to the state standards. The New Mexico Standards Based Assessment (NMSBA) is the cornerstone to the state's assessment program; other assessments include the high school competency exam, the New Mexico alternate performance assessment (NMAPA), and the English language performance assessment (NMELPA). Types of assessments include formative and summative; formative assessments are commonly referred to as short cycles targeting individual students and can be used to modify day-to-day classroom behavior and summative assessments are used to identify state wide, district wide or school wide strengths and weaknesses. It is important to distinguish between the types of questions used on these assessments; they can be multiple choice or constructed response. Constructed response includes fill in the blank, short answer, and extended response questions.

Over the past few years, New Mexico has invested heavily in implementing several education reforms and the assessment program is critical to measuring the impact of these reforms on improving student achievement. The key accountability measure, adequate yearly progress (AYP) is based largely on NMSBA results. The current contract for the NMSBA expires in June 2009. This review was meant to coincide with PED releasing the RFP for the new assessment contract.

The NMSBA is a rigorous assessment and there are opportunities to lower costs by using a different mix of question types. This finding integrates three important aspects of an assessment; the cost, the reporting of results, and the rigor. PED reported that according to the contractor, extended response or essay questions compromised 40 to 50 percent of the total costs of the NMSBA. These costs are related to the hand scoring of those questions. In 2003, Congress asked the Government Accountability Office (GAO) to conduct a study on what states are spending for no child left behind assessments. That report identified extended response as a primary cost driver.

The NMSBA is 70 percent multiple choice and 30 percent constructed response in all content areas and in all grades. Other states are more selective in their use of constructed response. Constructed response costs much more than multiple choice because the scoring process is labor intensive. These questions are hand scored by individuals and often rescored to check for inter-rater reliability. Timeliness of results is one of the most important aspects of the assessment and many districts have expressed dissatisfaction with the timeliness of results. Constructive response questions increase the time needed to get results. The current contract for the NMSBA requires results be returned within 60 days of the contractor receiving test materials from all districts. The NMSBA comingles multiple choice and constructive response with the various competencies that are measured and it is impossible to report those results separately.

The LFC's Rio Rancho public school review raised the issue of a test window being so early in the school year indicating there was not sufficient instructional time prior to the test being given. As a result, PED has changed the test window. Secretary Garcia noted that while the test window has been moved to later in the school year, PED does not expect results to be delayed but rather they anticipate receiving results at about the same time that results were received this year. Rigor has provided a more accurate picture of what students have learned. In general, constructed response increases rigor; however this evaluation found several examples of states using comparatively less constructed response and still achieving the same or more rigor. By bringing costs, results, and rigor together the evaluation found opportunities to lower the costs of state tests, getting results back sooner without an unacceptable loss of rigor by reducing constructive response. This recommendation is not to eliminate constructed response, just reduce it. It is recommended that PED develop the RFP for the next NMSBA to direct bidders to submit various levels of constructed response in their proposal and associated time frames. It is also recommended developing assessment contracts with the requirement that results from constructed response questions be available to districts in the desired format before the next school year and the results from the multiple choice assessment available in the year the test is administered enabling end-of-year adjustments.

A substantial amount of tax payer dollars, both state and federal, are spent for assessment and assessment related expenses. From FY06 through FY09, PED expenses for the main assessments were $28.5 million or just over 75 percent of the amount of funding. The remaining

25 percent is spent on alignment studies and other contracts. It is recommended that PED provide a report on expenditures to include any remaining documentation necessary. It is also recommended to move funds for assessment out of the SEG and provide them as a categorical appropriation. Two issues with the current arrangement include administrative efficiency and equity. Efficiency is compromised in the sense that the contractor bills and collects from each district separately rather than sending one bill to PED. Equity is compromised since some districts receive more for assessment and some receive less even though the cost per assessment is a flat fee.

PED's management of contracts needs further improvement. PED's inadequate contract management has cost the state money. There has been several procurement code violations often related to PED requesting services outside the scope of work of the contract. The NMSBA, the NMAPA, and the NMELPA are covered with three different contracts; all three have procurement violations. A PED, Office of Inspector General (OIG) report regarding the NMAPA shows issues with the selection of the contractor occurred. The report found that PED selected AIR even though their bid was twice as high as the lowest bid. PED staff described AIR's performance as disappointing. The report also noted that AIR over billed PED and did not provide all deliverables. PED recently amended the NMSBA contract amounting to $425 thousand in additional FY09 costs. The report recognizes that PED has made improvements in recent contract amendments. PED must improve their ability to effectively administer these contracts. Specific recommendations include tracking all deliverables in contracts and developing a contract abstract outlining the scope of work to be used as a reference document. PED should maintain additional documents reflective of contractor performance and agency and contractor responsibilities should be more clearly delineated in the contracts and planning documents. The contractor should also be able to provide records of incurred costs for major deliverables.

The LFC activity report notes that New Mexico is third in the nation in improving teacher salaries over the last ten years. The next step to this project is to determine the impact of the three tier licensure system on improving student test scores.

Veronica Garcia, Secretary, Public Education Department, reported that PED agrees with the overall finding of cost effectiveness in assessment contracts. The LFC and PED have worked together to collect organized detail, program financial, and management information about the statewide assessment program. Cost information was provided to LFC staff on all assessment contracts from FY06 to FY09 and included the Standard Base Assessment, the High School Standards Assessment, the English Language Deficiency Assessment, the High School Competency Exam, and the Alternate Performance Assessment. The goal was to provide a picture of the state's assessment program and to assist with staff in their evaluation. The timing of this evaluation is good and PED is currently working on new contracts for several assessments. The evaluation affords an opportunity to consider cost savings and other changes as new contracts are entered into.

Constructive response items particularly extended response items have clearly added to the cost of assessments. Over the four year life of the Standard Base Assessment contract, constructed response items accounted for 40 to 50 percent of the assessment development administration cost. The largest investment was made early on to develop rigorous items; PED now owns these items limiting the costs of hand scoring and ongoing item refreshment. Significant savings could be seen from a reduction in constructed response items and Secretary Garcia noted that PED is considering a reduction in constructed response items by requiring bidders in the RFP for the new NMSBA to submit varying levels of constructed response. Hand scoring and constructive response takes time and impacts ability to get quick results. New methods of scoring like distributive scoring reduce processing time for the state.

Most, but not all of the assessment's costs are specified in contracts and contract amendments. The PED is required to conduct test development and professional development activities that are not included in the assessment contracts.

The LFC evaluation raises concerns about the PED's management of its assessment contracts. Some of the deliverables listed in the evaluation were provided last year. One was modified, two were not needed, and one was not a deliverable. Staff monitors contract performance and issues are being addressed immediately. When needed, a cure notice is sent seeking an immediate remedy from the contractor. Beyond that, contractors provide remedies satisfying PED and school district requirements. Most importantly, PED and contractors are building trust and will assess penalties when contractors do not provide a satisfactory remedy.

Measures have been put in place in regards to procurement violations and no violations have occurred with assessment contracts since the summer of 2007. The procurement violations covered a variety of cases of which were not due to negligence and the monitoring of deliverables. In many instances planning was inadequate and additional deliverables were needed to meet timelines and changes in federal requirements.

Dr. Tom Dauphinee, Deputy Director, Assessment and Accountability has been trained by the General Services Department, Contract Management Bureau and has studied numerous materials on contracts. Concerted effort has recently been devoted to providing detailed specifications for contract deliverables and many other vital areas. Deliverables are very detailed and include language for fiscal penalties and have been an important undertaking for the assessment staff.

The contract amendment to the Standard Base Assessment was in preparation for a number of months before the economic downturn and was signed in September 2008. The amendment authorized the contractor to complete the development of the Grade 11 Spanish Based Assessment in Science as required by NCLB.

New Mexico was under a timeline waiver from the U.S. Department of Education to implement an alternative assessment for students with significant cognitive disabilities that met NCLB technical requirements. If not complied with, the federal government could have withheld a significant portion of Title I administrative funding from PED. In order to maximize the probability of selecting a successful contractor and receiving USDE approval of the assessment, the RFP evaluation committee emphasized the importance of a strong management component and a strong project plan in the evaluation. Of the three offers, the committee determined that the corporate experience, the corporate reference, staff experience, and individual references for AIR were superior with respect to expertise and understanding of how to assess students with significant cognitive disabilities, New Mexico's desired test design, and to have high probability that the plan would be approved by the federal government. It was also determined that AIR proposed a test design that was most relevant and appropriate for New Mexico's population of students with significant cognitive disabilities. The committee believed that AIR proposed the most feasible test design for a one-year implementation schedule. Based on the evaluation of criteria and scoring system AIR was awarded the highest overall score.

Miscellaneous Committee Business.

Approval of LFC Minutes – November/December 2008. **Senator Cisneros moved to adopt the Legislative Finance Committee meeting minutes of November 2008, seconded by Senator Leavell. Motion carried.** Chairman Smith asked that Representative Wallace be designated to review and adopt the Legislative Finance Committee meeting minutes of December 2008.

Tax Policy Guidelines in LFC Fiscal Impact Reports. Director Abbey reported that staff recommends adopting the tax policy guidelines contained in the LFC fiscal impact reports (FIR). Principals will be included in every FIR tax bill as a reminder of criteria that will be recommended to the Legislature. **Senator Cisneros moved to approve the recommendation, seconded by Senator Papen. Motion carried.**

IT Program Evaluation of SHARE payroll deductions, retirement, contribution transfers, and follow-up of previous reports. Ms. Aurora Sanchez, IT Program Evaluation Manager, Legislative Finance Committee reported that this review of statewide human resources, accounting and management reporting system (SHARE) was to provide an update on the timeliness and accuracy of payroll deductions and of data transfer to retirement benefit systems, external assessments, and all remaining issues from the two previous SHARE reports. Payroll deductions from employee paychecks and transfers to third-party beneficiaries are timely and accurate. Issues of concern with payroll deductions are: (1) one Department of Finance and Administration (DFA) employee has total control over all payroll documents and therefore presents a single point of failure, and (2) the Retiree Healthcare Association's Retiree Healthcare Fund has lost $495.7 thousand from January 2007 through October 2008 because employers do not contribute to the fund from 537 return-to-work retirees. PERA has experienced issues with data downloaded from SHARE. As of July 31, 2008, $10.2 million in retirement contributions had not been posted to the proper member accounts for 5,747 state employees. DFA and PERA are working together to resolve the data issues and the errors are down 50 percent.

Findings from the 2007 and 2008 reports have not been resolved. The most significant issue is the establishment of a governance structure that will allow the enterprise to achieve its goals. The Department of Information Technology and DFA have agreed to develop and implement a governance structure that will allow for good technical support. The Federal Highway Administration is extremely upset about the accounting for federal transportation aid and is threatening to cut off funding if governance structure is not implemented and the changes to SHARE are not in production by July 1, 2009. The access to SHARE reports continues to be intermittent and limited. Director Abbey suggested that if there is incremental funding for SHARE, it be contingent on ensuring access for staff. Deputy Director Patel said that a recommendation will be made to the House Appropriations and Finance Committee and the

Senate Finance Committee that no funding be appropriated unless necessary access is granted to staff.

Performance Evaluation Work Plan 2009. Deputy Director Patel said staff is focusing on the PED early childhood program, impact of the three tier teacher salary initiative, the State Transportation improvement plan and resource allocation, and alterative energy tax incentive grants. Review of additional school districts is also considered. Representative Saavedra requested that the review of additional school districts be included in the 2009 work plan.

Status Report on Federal Fiscal Year Relief. Director Abbey reported that staff will recommend adjustments to appropriations when federal funds are received.

November Cash Balance Report. Director Abbey reported that the report consists of accounts in the treasury that are borrowed to cover the shortfall in the general fund.

December BAR Report. Information

December LFC Budget Status Report. Information

January 16, 2009

The following members were present on Thursday, January 15th: Chairman John Arthur Smith, Vice-Chairman Luciano "Lucky" Varela, Representatives Donald E. Bratton, Rhonda King, Don Tripp (for Brian K. Moore), Edward C. Sandoval, Jeanette O. Wallace, Nick L. Salazar, Henry "Kiki" Saavedra; and Senators Carlos R. Cisneros, Sue Wilson Beffort, Carroll H. Leavell (for Leonard Lee Rawson), Stuart Ingle, Phil A. Griego, Mary Kay Papen, and Pete Campos. Representatives Larry Larranaga, John A. Heaton, Mimi Stewart, and Senators Cisco McSorley, and Bernadette M. Sanchez attended as guests.

Review of Selected Capital Outlay Projects. Manu Patel, Deputy Director, Legislative Finance Committee introduced Donna Hill-Todd, Program Evaluation Manager, Brenda Fresquez, Evaluator, Lawrence Davis, Evaluator, and John Ketchens, Evaluator. Mr. Patel reported that in September 2008, the capital outlay subcommittee asked that a presentation be given on how capital projects are audited. A separate audit of major capital outlay projects had not been done in the past and the committee determined that there is a need to conduct audits for compliance on a selected basis. The subcommittee requested to review three or four projects to determine key steps to be followed for projects that are audited.

Ms. Hill-Todd began with the Tri-Services Laboratory and said the original state laboratory was constructed in the 1970s and houses the Department of Agriculture Veterinary Diagnostics Services, the Department of Health's Scientific Laboratory Division, and the Office of the Medical Investigator. With the increase in New Mexico's population the demand for services provided by these organizations increased. The Infrastructure Capital Improvement Plan indicated that in this building, construction materials and degrading heating, cooling and ventilation systems interfered with specimen analysis causing contamination and exposed employees to risk from airborne and chemical hazards. In addition, changes in federal and state laws, the new and re-emerging infectious diseases, and mounting concerns about the use of biological and chemical weaponry necessitated the proposal to construct a new facility. It was not deemed cost effective to remodel the existing complex.

The inception of the Tri-Services Laboratory project occurred between 1999 and 2000. Since then, the project has gone through two administrations and several GSD cabinet secretaries. Five acres of land were purchased from UNM on which Tri-Services Laboratory is being constructed. The planned complex will be approximately 201 thousand square feet which will increase the space of each occupant by 60 percent and will contain general analytical laboratory space, specialized areas to perform molecular diagnosis, human and animal autopsy, and office and conference areas.

The Property Control Division of the General Services Department is overseeing the general construction, the design and architectural planning are under the oversight of Studio Southwest Architects, Inc., and the general construction contractor is Jaynes Corporation. The construction component is 20 percent complete and ahead of schedule and the anticipated completion date is March 2010. Over a ten year period, this project has cost the state $86 million.

Ms. Hill-Todd reviewed the team's key observations and said project management formed a group of reliable and competent onsite and internal project team members. Project partners and team members demonstrated cooperation with project leadership as well as maintaining timely and ongoing construction meetings, change order reviews and status reports. The Office of the Medical Investigator is concerned about whether funds will be available to adequately equip and furnish the laboratory after the construction is complete especially if the $7 million budget request for Fy10 is not approved for the Department of Health. There is a need for legislation to require all capital outlay projects under the jurisdiction of the Property Control Division to submit a maintenance plan and an annual maintenance report similar to the master planning, maintenance and utilization model implemented by the public school facility administration. Piecemeal funding of planning and construction monies resulted in lost savings and expertise for the state. The Tri-Services Laboratory's cumbersome project development can also be attributed to state gubernatorial and UNM presidential administration changes, as well as attitudes about the worthiness of the project.

Ms. Hill-Todd proceeded with the Belen Multipurpose Community Center project and said in 1993, the city of Belen first sought assistance from the state legislature to fund land acquisition, design and construction of a multi-purpose community center. With a 1993 state legislature appropriation of $100 thousand, and a city contribution of $163 thousand, the city purchased 47 acres of vacant land within the city limits. The site is located immediately north of Belen High School, between Interstate 25 and the Belen Highline Canal. The project continues funding through the legislature and U.S. Department of Housing and Urban Development. It appears that the city has accounted for and spent the majority of more than $4 million in appropriated funding except for a remaining balance of $277.3 thousand which is related to final completion of the gymnasium, equipment and park amenities.

Molzen-Corbin and Associates served as the project manager for the project and served in the role of architect/engineer of record. Pre-construction and field meetings were held on a regular basis with documented meeting minutes maintained in the records. The project was advertised, bids were received, and a selection process was exercised with the approval of the city council. Overall, the project was efficiently monitored and managed throughout the construction and close-out phases.

In August 2006, flood waters from heavy rains extensively damaged the park by eroding and enlarging the unprotected drainage channel, undermining the concrete slabs around the recreational facilities, and washing out sidewalks and depositing siltation in the construction retention basin. The flood damage site was evaluated by the Federal Emergency Management Agency (FEMA) for possible funding of the Hazard Mitigation project. FEMA paid $192.8 thousand for the multi-purpose park drainage restoration portion of the project. The city was responsible for the remaining balance. The Construction Industries Division of the Regulation and Licensing Department (RLD) conducted an inspection to determine causal factors of the settlement and cracking that occurred in the west and north building walls and north courtyard wall of the Belen Multi-Purpose Community Center which was constructed in 2004. The report was dated July 2008 and determined that the drainage was a factor in that the water was not adequately diverted away from the building, but apparently diverted the runoff into the building. The soil type in the area does not allow ditches to hold their shape. Soils below the structural fill collapsed and shifted causing building movement due to the sheer amount of water which ran onto the site.

The review team's key observations were that the Belen Multipurpose Community Center project along with surrounding recreational parks and roads have received multiple appropriations and grants dating back to 1993 through 2008. The project was monitored consistently and the project manager was readily available to the city of Belen personnel. Maintenance of the drainage area around the center was not conducted consistently and as a contributing factor, flooding in 2006 caused structural damage to the facility. The drainage plan for the center has been drafted, but not finalized and approved by the city council.

Ms. Hill-Todd continued with the Eagle Nest Dam repairs project and said it is a 140 foot high, concrete arch structure that was constructed between 1916 and 1918. The dam is located in Colfax County 2.4 miles southeast of Eagle Nest at the headwaters of the Cimarron River in north central New Mexico. The dam stores water in Eagle Nest Lake and regulates stream flow for downstream irrigation and municipal water supplies. With the state's purchase of the dam in 2002, the state Game and Fish Commission owns Eagle Nest Dam and the Department of Game and Fish administers the Dam. The project is managed by the Office of the State Engineer's Interstate Stream Commission based on an October 2003 joint powers agreement (JPA). The Interstate Stream Commission has the financial responsibility for the oversight, management, and maintenance of the Dam. The Commission is also responsible for procuring the services of a qualified professional engineer to study and report on the condition of the Dam and provide engineering cost estimates for refurbishing.

During the 2003 legislative session, $3 million was appropriated from the game protection fund to the Department of Game and Fish for expenditure in fiscal years 2003 through 2008, to refurbish and repair the Dam. During the 2008 legislative session the appropriation of $1.7 million was reauthorized through fiscal year 2010. The original cost estimate of $6.2 million for repairs was prepared prior to the state purchase in 2002. Neither the Interstate Stream Commission or the Department of Game and Fish could provide a revised cost estimate detailing the planned use of the $3 million appropriation.

The Interstate Stream Commission was responsible for procuring engineering services for the project and managing contractors based on issued work orders. Each work order identified a commission project manager. During initial meetings with the Department of Game and Fish as well as the commission, it was noted that the commission had turnover in the project manager position at least four times averaging one per year. With the changes in project managers, the information was not current or complete. Since the department does not have an engineer with dam expertise on staff they have to rely on commission expertise. The department's project management was limited to reviewing contractor invoices, project meetings, and e-mail correspondence from the commission.

The Dam Safety Bureau of the Office of the State Engineer inspected the Eagle Nest Dam prior to the state's purchase in 2002. The past four inspection reports classified the dam as in "fair condition" which was based on uncertainties regarding the performance of the dam during extreme flood events. Since 2005, the inspection reports have consistently recommended repair of the concrete joints and hairline cracks in the dam crest. These repairs have not been made, cost estimates have not been obtained and repairs were deferred to be part of the overall dam rehabilitation strategy. Other than normal maintenance, the recommendations have included pursuing the rehabilitation of outlet gates, completion of access road improvements, resolving spillway capacity issues and completion of an emergency action plan and operation and maintenance manual. The Department of Game and Fish director has indicated that dam safety is a priority and will move forward with these documents as soon as the agency is able to meet and prioritize the 16 state Game Commission owned dams.

The review team's key observations were that after five years, spending $1.3 million and receiving the results from the engineering reports and analysis, the Department of Game and Fish still has not made a decision on the path forward or determined the cost to repair the dam. The change in the agency director and the lack of dam expertise at the department has contributed to the delayed, decision making process regarding the project. The agency has encumbered and expended the appropriation according to the statutory intent, however the contractor invoices do not reconcile between the Department of Game and Fish and the Interstate Stream Commission. The remaining appropriation of $1.7 million may be overstated by approximately $55 thousand. There was turnover in project management at the Interstate Stream Commission and as a result they did not maintain current project data and documentation efficiently. The turnover also may have contributed to the limited documentation made available to the review team.

Mr. Patel continued with the Water Innovation Fund project and said during the last three to four years $25 million has been appropriated for projects. Of that, the Department of Finance and Administration (DFA) has awarded 49 grants totaling $17 million with a remaining balance of $8 million. Mr. Patel discussed projects that were selected and began with the Albuquerque Bernalillo County Water Utility Authority. The total amount of the grant was $577 thousand and is a successful project. Based on the 52 water leaks they identified, it is estimated that over a one year period it could save 457.3 million gallons of water. This project is currently being used and DFA is in the process of taking it out to other counties and municipalities.

The second project reviewed was for the Marine Environmental Partners with a total cost of $545 thousand. DFA considers this project successful and 100 percent complete, however the system has not been used since late 2005. Equipment needs to be moved from the Milagro Dairy in Clovis to the New Mexico State University (NMSU) Agriculture Science Center in Clovis so that parts could be used for other projects; DFA has not provided legal authority to transfer the equipment.

The third project is a pilot study on the Pecos River called the N.A. Water System. This system is supposed to purify the blackist water to be reused. The contractor did not submit all the bi-monthly progress reports and the final report indicated it is possible to produce water, however this project is discontinued and DFA cannot provide inventory details showing where equipment is located and how it will be utilized in the future.

The Santa Fe County Lagoon water project is located at the State Penitentiary. According to the proposal, this project was supposed to filter 140 thousand gallons of water per day to be reused and resold at $2.00 per one thousand gallons. It was expected that the filtration system would have a life expectancy of 15 years. The New Mexico Environment Department's (NMED) technical staff had reservations regarding the system. The final report from New Mexico Tech indicates that the system would produce 45 thousand gallons of water per day at a cost of $2.27 per one thousand gallons and does not meet all NMED requirements. DFA indicates the system is operational; however LFC staff visited the site and determined the project has not been used since day one. The main pump is pulled out and lying on the ground. The New Mexico Corrections Department also indicated that the project is not cost effective and do not plan on using it.

The Subsurface Technology project totaling $826 thousand is located at the San Antonio Mutual Domestic Water Consumers Association. The contractor complied with submitted all reports, however the final report indicates that it had unsatisfactory performance. The system is currently not being utilized and there is not an inventory of equipment at DFA.

Other projects include: New Mexico Tech and the city of Rio Rancho. These two projects are currently in progress and staff will follow up on them once they are complete.

Key issues with the Water Innovation Fund are a lack of information from DFA hampering the LFC's oversight efforts. Information was requested, however in some cases DFA claimed an executive privilege and did not provide documentation to analyze all the projects. Documentation is insufficient and cannot be verified to determine if project selection and the grant award process is in accordance with procurement code regulations. DFA has not developed a tracking system to measure the project performance and outcome and determine if similar systems have been used at other locations.

It is recommended that since the Water Innovation Fund has not been established by the Legislature, legislation to establish the Water Innovations Fund Act be considered to provide necessary program guidance, requirements, limitations, and oversight responsibility. It is recommended that DFA create water innovation fund guidelines to ensure proper oversight, fiscal responsibility, and project management. It is also recommended that DFA create centralized project documentation guidelines, establish a tracking system to measure project performance and outcomes, complete funding reconciliations to ensure the balances in the SHARE system reconcile with capital outlay evaluations, and ensure that all funds received adhere to the contract deliverable. It is also recommended that DFA compile the inventory of the equipment purchases, location of the equipment, custodian, and current use of the equipment and transfer unused equipment to other water projects that could benefit from such transfers.

Arturo Jaramillo, Cabinet Secretary, General Services Department commented on the audit of the Tri-Services Laboratory building and indicated this is the fourth audit in a three year period. The project is 20 percent complete and is three to four weeks ahead of schedule. Annual maintenance plans and reports are not managed by the Building Maintenance Division and have to be relied upon by agencies. A new rule has been developed requiring agencies to provide the General Services Department with an annual building maintenance plan that includes deferred maintenance of buildings.

Todd Stevenson, Director, Department of Game and Fish, responded to the audit and said the project has been a struggle. There has been good partnership between the Department of Game and Fish and the Interstate Stream Commission along with interaction from the State Engineer's Office. Currently, the biggest issue is with the assessment from the engineering firm and what are the most cost effective measures to be able to move forward. Director Stevenson pointed out that there has been oversight by both the Department of Game and Fish and the Interstate Stream Commission from the beginning. There has been a priority shift since the previous administration in the importance of dam safety and how it is addressed. Significant steps will be taken to get into compliance with the Office of Engineer's Dam's Safety Board requirements and rules as far as emergency management action plans and operational plans on all dams. The department is also currently working with the U.S. Fish and Wildlife Service. The dam is not anywhere close to a point where there are significant problems with the dam itself or the operation of the dam and the ability to provide water to the downstream users.

The Interstate Stream Commission has established protocols to assure there is continuity in accurate record keeping. Steps have been taken to establish contract management protocols to keep better track of work orders, invoices, and contracts.

Vice-Chairman Varela said it is his understanding that no repairs have been done to the dam. Director Stevenson said that was correct. Dam safety issues include cracking in the cement on the outside of the dam surface. The Department of Game and Fish has been in interaction with the Dam Safety Bureau and have agreed that is something that should be dealt with along with other modifications, however, they do not contribute to an "at risk" for that dam facility at this time. Chairman Smith asked if this project was considered to be submitted as part of the Stimulus Package for infrastructure. Director Stevenson said no, however it is something that could be suggested.

Rick Martinez, Deputy Cabinet Secretary, Department of Finance and Administration responded to the water innovation fund and said it was intended for research to look for technologies to conserve water. DFA considers those projects that were noted unsuccessful, to be successful. Equipment located at the State Penitentiary will be transferred to New Mexico Tech and will be enhanced to move forward. DFA is also working with universities to transfer other equipment. Work is being done with the Environment Department to target areas where research can be moved to smaller communities. DFA is also working on getting reports out on a timely basis.

Robert Apodaca, Deputy Director, Department of Finance and Administration, also provided testimony regarding the water innovation fund and said unexpended funds will go out to bid. Deputy Director Apodaca added that there are over 40 projects that have been funded and a number of successes that were not reported.

Chairman Smith asked where in statute it is indicated that the water innovation fund could be used for research. Deputy Cabinet Secretary Martinez said there is nothing in statute that discusses research. Chairman Smith said it is a breach of legislative responsibilities and the legislature should take full responsibility for this inaction.

Vice-Chairman Varela inquired about documentation that was denied throughout the evaluation. Mr. Patel said documentation was requested specifically for the Gordon Construction Company project. A memorandum was generated from the Environment Department indicating the project should not move forward. The final report indicates the system is not functional and did not meet requirements. The department claimed executive privilege to documentation. LFC staff met with the Attorney General's Office who recommended requesting assistance to obtain documentation. Deputy Cabinet Secretary Martinez responded that the department considers executive privilege between two executive agencies. Vice-Chairman Varela asked if a copy of the memorandum was received from either agency. Mr. Patel said no. Vice-Chairman Varela said the LFC may need to consider evoking subpoena powers. Chairman Smith added that the Executive Branch has a responsibility to report the source of funds being expended and when there is connotation of not releasing information there is an appearance of a cover up. Deputy Cabinet Secretary Martinez said the state of New Mexico needs a statewide comprehensive capital outlay plan to encompass all types of projects. Mr. Patel concluded by saying both the Legislative and Executive branches of government have improved accountability for capital outlay appropriations, however much more needs to be done. It is recommended that the Legislature consider including requirements in the Capital Appropriations Act for the State Auditor and the LFC to conduct special agreed upon procedure audits of the major capital outlay projects. It is also recommended that the Committee require staff to include capital outlay project audits on an annual basis. A checklist has been developed to be used by staff and DFA in monitoring future projects.

<u>LFC Sponsored Legislation/Catch-Up/Clean-Up.</u>

<u>Solvency Bills.</u>

Reductions to Laws 2008, Chapter 3, General Appropriations Act. Director Abbey reported that the proposed bill reduces FY09 general funds, operating budget recommendations. LFC staff presented a range of recommendations that was a net of minus 1 percent for public schools and Medicaid and 2.5 percent for all other agencies. LFC continues to be concerned about the ability of small agencies half way through the year to take a 5 percent reduction. DFA recommended reductions deeper than 2.5 percent for larger agencies; LFC reviewed them and adopted them in part or in whole. The total reduction from FY09 averages 1.5 percent or $89 million. The LFC recommendation for FY09 Specials includes $750 thousand to DFA with Board of Finance approval to allocate to agencies that are in trouble. The proposed bill also recommends expanded BAR authority allowing transfers among programs. **Senator Cisneros moved to adopt the Reductions to Laws 2008, Chapter 3, General Appropriations Act proposed bill, seconded by Representative Saavedra. Motion carried.**

Reductions to Laws 2008, Chapter 1 and Chapter 6, Fund Transfers; Other State Fund Transfers and Appropriations. Director Abbey reported on transfers, appropriations and delays. Transfers and appropriations include: an increase in the Fire Protection Fund distributions, a transfer of $20 million from the College Affordability Act, $8 million from the Telecommunications Access Fund which is in excess of current spending, adding $1 million to the recommendation for the Workers' Compensation Fund to reflect the DFA recommendation of $1 million higher, an adjustment of the Higher Education Endowment Fund to $600 thousand reflecting better information and $5 million for the SB9 Public Infrastructure. The Higher Education performance (special appropriation from 2007) is not recommended to be included in the financial summary because it does not require legislative action. In section six of the bill, LFC recommended deauthorizing $22.5 of the special session appropriation. The revised staff recommendation leaves $4 million for DD and $1.5 million for behavioral health. It is believed there is $20 million of TANF funds available that HSD needs to apply for and could be used for expanding coverage of children in Medicaid, behavioral health, and developmentally disabled. It is also believed Congress will pass significant expansions of the S-Chip program that will also allow the state to cover more children with federal appropriation. **Senator Cisneros moved to adopt the Reductions to Laws 2008, Chapter 1 and Chapter 6, Fund Transfers: Other State Transfers and Appropriations proposed bill, seconded by Senator Papen. Motion carried.**

Corporate Income Tax Quarterly Payments. Director Abbey reported on the Transfer of funds to General Funds and said revenue from DFA has been incorporated and includes the Enforced Motor Vehicle Statute. The Taxation and Revenue Department is trying to obtain fair accounting of automobiles for resale with a tax estimate of $5.9 million. Alternatives include splitting the amount into March and June brining money in this fiscal year and allowing a two phase payment. It is also suggested to require an eighth quarterly estimated payment rather than a quarter in FY09 and the other eighth quarterly estimated payment in FY10 reducing FY09 to half. **Representative Saavedra moved to adopt the Corporate Income Tax Quarterly Payments proposed bill to take before the House Appropriations Finance Committee and the Senate Finance Committee as one of the pieces to take care of the Solvency, seconded by Representative Sandoval. Senator Beffort voted in the negative.**

Capital Outlay Reauthorizations. Director Abbey reported that LFC recommendations remain valid and cautioned that in some cases it appears there may have been a rush to spend funds to avoid the reach of the Legislature. It is recommended to pursue staff recommendations and present the proposed list to the full Legislature. All bills are going to need thorough hearings in House Taxation and Revenue, House Appropriations and Finance, Senate Finance, as well as joint hearings. Representative Saavedra added that work would also be done with the administration. **Senator Cisneros moved to approve the Capital Outlay Reauthorization proposed bill, seconded by Representative Saavedra. Motion carried.**

Pension and Benefit Solvency. Director Abbey reported that there are no adjustments recommended to what was previously submitted and concurrence has been received from benefit administrators. **Senator Beffort moved to approve the proposed Pension and Benefit Solvency bill, seconded by Representative Saavedra. Motion carried.**

Director Abbey reported that Vice-Chairman Varela urged him to draft a bill establishing a capital projects review process. The proposed bill creates a capital outlay division at DFA that is a companion to the budget division directing establishment of timelines and guidelines for agencies. It also creates a capital outlay review committee of the legislature and would review requests submitted September 1st providing recommendations for both the executive and the legislature. It would also provide auditing on a sample basis by the State Auditor and the LFC, an independent group from the executive branch. Senator Beffort asked if statute was being considered. Director Abbey said it is an amendment to the DFA statute 6-4, as well as an amendment to the legislative statute to set up budget processes. Senator Beffort suggested having a deadline cutoff in front of the final bill so projects could not be legally put in after that deadline. Director Abbey said the capital outlay review committee and the DFA capital division could not recommend projects that are not submitted by September 1. **Senator Cisneros moved to adopt the proposed bill, seconded by Senator Griego. Motion carried.**

Director Abbey reported the final bill recommendation is part of the Solvency for FY09 and FY10 and delays the enactment of the hospital gross receipts tax until FY11 and raised $3.4 million for FY10. **Senator Cisneros moved to adopt the proposed bill, seconded by Senator Beffort. Motion carried.**

Director Abbey said three additional bills are recommended for individual sponsorship. Solvency bills are recommended to be introduced on both sides of the legislature.

Sunset Subcommittee Recommendations.

Osteopathic Medicine (Bi-Annual Renewal); Dental Health Care (Scope of Practice); Dental Health Care (Licensure Requirements); Dental Health Care (Temporary Licensure); Professional Psychologist Act (Reciprocity); Professional Psychologist Act (Licensure Requirements); Board Repeal Dates; Office of Military Base Planning Repeal Date

Director Abbey reported that the Sunset Sub-Committee met in September and October and adopted a package of bills and the full committee adopted the Sunset Sub-Committee report and action is recommended to adopt committee legislation. **Senator Leavell moved to adopt the sub-committees recommendations, seconded by Senator Griego. Motion carried.**

With no further business, the Committee adjourned at approximately 11:40 a.m.

[signature]
Chairman

5/18/09
Date