

MINUTES

Interim Joint Committee on Appropriations



Senator Larry Tidemann, Lead Co-Chair
Representative David Anderson, Co-Chair

**Third Meeting, 2017 Interim
Wednesday, July 26, 2017**

**Northern State University
Aberdeen, South Dakota**

The third meeting of the Interim Joint Committee on Appropriations for 2017 was called to order by **Lead Co-Chair Larry Tidemann** at 9:00 AM in the Centennial Room of the Student Center at Northern State University, Aberdeen.

A quorum was determined with the following members answering the roll call: Senator Larry Tidemann, Lead Co-Chair; Representative David Anderson, Co-Chair; Senators Justin Cronin, Terri Haverly, Reynold Nesiba, Jeffrey Partridge (via telephone), Deb Peters (via telephone), Billie Sutton (via telephone), Jim White, and John Wiik; Representatives Dan Ahlers, Lance Carson, Jean Hunhoff, Chris Karr, and Sue Peterson (via telephone). Excused: Representatives Hugh Bartels, Taffy Howard, and John Lake.

Staff members present included Annie Mehlhaff, Chief Fiscal Analyst; Jason Simmons, Principal Fiscal Analyst; Jeff Mehlhaff, Fiscal Analyst, and Lucas Martin, Fiscal Analyst.

***NOTE:** For purpose of continuity, the following minutes are not necessarily in chronological order. Also, all referenced documents distributed at the meeting are attached to the original minutes on file in the Legislative Research Council office. This meeting was web cast live. The archived web cast is available at the LRC web site at <http://sdlegislature.gov>.*

Approval of Minutes

A MOTION WAS MADE BY SENATOR NESIBA, SECONDED BY SENATOR WHITE, TO APPROVE THE MINUTES OF THE JUNE 8, 2017, INTERIM JOINT COMMITTEE ON APPROPRIATIONS MEETING. The motion prevailed on a voice vote.

Co-Chair's Opening Remarks

Lead Co-Chair Tidemann and **Co-Chair David Anderson** thanked Dr. Downs, President, Northern State University, for hosting the committee and providing a tour of the campus.

FY2017 Year-End Report

Ms. Liza Clark, Commissioner, Bureau of Finance and Management, gave a review of the fiscal year end for FY17 ([Document #1 – FY2017 Year End Summary](#)).

Mr. Jim Terwilliger, Deputy Commissioner and Economist, Bureau of Finance and Management, provided a revenue update. Mr. Terwilliger said although the February and March receipts were down, the tax collections in April, May and June recovered some of those losses. At year end, the revenues received were lower than the adopted estimate by \$7.623 million. There was a cash surplus of just under \$8 million at the end of FY17, which flowed into the budget reserve fund per state law.

Senator Justin Cronin asked about the one-time revenue sources. Mr. Terwilliger replied the one-time revenue sources include unclaimed property from stock sales and overpayment of a bank franchise tax, as well as

unexpended carryovers and special appropriations. Mr. Terwilliger explained unclaimed property is an unpredictable source of funding and claims were about \$20 million in FY16 and \$27 million in FY17.

Senator Jeffrey Partridge requested a detailed analysis of the insurance premium tax the state collects. Mr. Terwilliger explained some of the changes in the insurance tax payments and said he will send more detailed information to the committee members. Insurance companies report by calendar year, not fiscal year. The insurance companies remit their payments quarterly based on estimates, and then "true up" when they have their actual numbers, and that payment is normally more than the other payments. However, insurance has been softer this year and the "true up" payment was less than usual. The main reason the numbers are down is really the timing of the "true up" payment.

Representative Anderson said the change in the federal fiduciary rule is a reason revenue from annuity sales is down substantially; and premiums on crop insurance were lower because crop prices were lower meaning ag prices are bringing those revenues down.

Mr. Terwilliger said annuities are about 3% of the total premiums, which is a small part of the \$7.4 million decrease in insurance premium tax.

Senator Cronin asked for more detailed information on crop insurance premiums. Representative Anderson explained that crop insurance premiums are based on the spring price. The USDA establishes the price for crops during the month of February on which the premium is based, and the volatility factor is built into that spring price. The overall trend of crop prices being lower over the last few years does impact these premium prices.

Ms. Clark presented the Agency Budgeted Reversions which totaled \$15,566,622. A breakdown of the reversions by agency can be found on page 6 of the *FY2017 Year End Summary*.

Ms. Clark said the agencies did a variety of things to find money to revert, such as keeping vacant positions open longer and waiting on some expenditures until the next fiscal year. Upon requests from the committee, Ms. Clark said she will provide them with more detailed information on the agency reversions following the meeting.

Senator Tidemann said there are some questions regarding how agencies are using transfers. Ms. Clark explained there are two types of budget transfers. There is a one-time transfer which may be used for an unexpected payment. These are mostly used at year end for cleaning up the budgets. The other is the ongoing transfer which is used for realigning things once more information is received. These are base transfers.

Ms. Clark said in 2017, BFM did 39 transfers, in 2016 there were 48 transfers, in 2010 there were 68 transfers. There are not a lot of transfers but they are used to assist the state in managing large budgets over a fiscal year.

Representative Jean Hunhoff said there seems to be a lot of transfers from operating expenses to personal services and asked what is happening to cause the money to move in that direction. Ms. Clark explained there are times when agencies contract for staff and later hire staff instead of having to use the contract process. Contract payments come from operating expenses, while salaries are paid from personal services. Representative Hunhoff asked that the agencies communicate the reason more clearly when making these transfers.

Senator Tidemann said transfers have been a concern for many years, but the process has been enhanced and the descriptions of the transfers are more clear. Transfers are a management tool when used properly and applies to about one-half of one percent of the budget.

Update on FY2018 Revenue Projection

Mr. Jim Terwilliger, Deputy Commissioner and State Economist, Bureau of Finance and Management, gave the [Revenue Forecasts](#) Report ([Document #2 – BFM Updated Revenue Forecasts](#)). Mr. Terwilliger said this report is required in statute, SDCL 4-8A-16. The revenue projection presented in February has been revised down about \$11.4 million, or .72%, which does not meet the threshold requiring further action as outlined in statute.

Mr. Terwilliger reviewed the report explaining the changes made to the forecast amounts. One impact on the numbers is that the farm economy was expected to see some improvement in 2018 but the drought has changed that thinking.

Representative Lance Carson asked why there is an upward trend in the tobacco tax collection. Mr. Terwilliger said the cigarette tax is a declining revenue source because we see fewer people smoking. However, South Dakota will see some increase in sales because of the high cigarette tax in Minnesota, and the decrease in gas prices provides more disposable income allowing for more purchases of tobacco products.

Representative Chris Karr asked Mr. Terwilliger about his comfort level in predicting a 4% growth in sales tax collections. Mr. Terwilliger responded that taxable sales in 2017 decreased about 2%. There was decreased spending in 2017 within the ag economy, especially when tracking machinery sales. The drought does cause concern in predicting an increase in farm spending. The increase in overall spending the last couple of months does create the comfort that the predicted 4% growth will be met.

Mr. Jeff Mehlhaff, Fiscal Analyst, LRC, gave the Legislative Research Council's FY18 Revenue Projection Update ([Document #3 – LRC Update Revenue Forecasts](#)). Mr. Mehlhaff explained the process he used in updating the FY18 revenue projections. Mr. Mehlhaff detailed the changes to the projections and why those changes were made. The updated projection shows a \$12.1 million decrease in the projection made in February.

Certify the Proration of FY2017 Interest Earnings

Commissioner Liza Clark, Bureau of Finance and Management, presented the proration of FY17 interest report for approval ([Document #4](#)).

A MOTION WAS MADE BY SENATOR WIIK, SECONDED BY SENATOR CRONIN, TO APPROVE AND CERTIFY THE RECOMMENDED INTEREST PRORATION DESIGNATIONS AS PARTICIPATING AND NONPARTICIPATING AS PRESENTED BY THE BUREAU OF FINANCE AND MANAGEMENT. The motion prevailed on a roll call vote with 14 AYES and 4 EXCUSED. Those voting AYE: Senators Cronin, Haverly, Nesiba, Partridge, Peters, White, Wiik, and Tidemann; Representatives Ahlers, Carson, Hunhoff, Karr, Sue Peterson, and Anderson. Excused: Representatives Bartels, Howard, Lake, and Senator Sutton.

Board of Regents Report on Efficiencies

Dr. Mike Rush, Executive Director, Board of Regents, introduced Board of Regents' staff members Dr. Paul Turman, Chief Academic Officer; Ms. Leah Ahartz; and Mr. Monte Kramer, Chief Fiscal Officer. Dr. Rush said the Board of Regents spends a lot of time on efficiencies and continues to do so, and presented the Board of Regents Efficiency Report ([Document #5](#)).

Dr. Rush said one of the four goals adopted by the Board of Regents is to try to maintain affordability for students served. South Dakota Universities' cost per student remains lower than cost per student in other states, in fact this past year saw South Dakota's cost per student decrease while the rest of the nation saw increases in the cost

per student. While the overall cost per degree is lower in South Dakota than in other states, the amount received from the South Dakota general fund per degree is significantly lower than in other states, and that increases the individual student costs.

Senator Cronin asked for the data to be compiled from 1998 through today regarding the amount of general fund dollars per student and that information be provided to the JCA members.

Representative Karr asked what is included in the cost per degree. Dr. Turman said included is the direct educational costs and mandatory fees; housing and food are not included.

Program productivity and reducing complexity:

Dr. Rush said one of the most significant revisions to the transfer of credits policies this year was the implementation of general education block transfer for students, internal and external to the regental system. This will considerably reduce the need for students to take unnecessary courses as they transfer among campuses. South Dakota is working with 12 other states to improve methods for accepting academic credit for military experiences, training, and occupations.

Senator Terri Haverly asked if the Board of Regents is working with Midwest Higher Education Compact (MHEC) on the military credits. Mr. Rush said this is a specific project South Dakota is working on with MHEC, which significantly reduces the cost to the state for collecting the basic information.

Dr. Rush said another strategy to improve the general education transferability was to remove institutional graduate requirements and a much more collaborative program is now in place.

Dr. Rush said there has been a reduction in the required number of credit hours which has resulted in a savings of about \$1,800 per graduate. The JCA members did share some concerns regarding the reduction in required credit hours, and Dr. Turman explained that the decrease in hours was from the electives and not from the major requirements.

Dr. Rush said three regental institutions have implemented the exploratory studies program for students who are undecided on their majors. This program allows the courses to add up to a major once the student has declared.

By implementing all of these programs, the students can save up to \$5,000 on their tuition.

Representative Hunhoff asked if these efficiency programs are currently in place and Dr. Rush said the programs are in place, but the BOR continues working with faculty to get more open source textbooks, which was also discussed as an efficiency in the higher education system.

Senator Reynold Nesiba said he is concerned about affordability, especially with low to moderate income students. Dr. Rush replied that South Dakota's students do not tend to have higher average loan debt but more of our students have loans than in other states, and that is a result of a lack of need-based scholarship programs in South Dakota. We are the only state in our surrounding area that does not have a need-based scholarship program. Senator Nesiba asked for a written report regarding the comparisons of South Dakota to other states and the need-based scholarship programs.

Strategic planning, mission alignment, and structural review:

Dr. Rush said the general education re-design seeks to improve student transferability, and better align system requirements through the elimination of unique graduation requirements.

Dr. Rush explained the changes to the regental library consortium, instructor and lecturer ranks, multi-measure placement, remediation, advising and student interventions, dual credit enrollment, and the common course catalog.

Effective and efficient operation:

Dr. Rush said the 4/7/10 policy for section size has had a significant impact on controlling the costs. The Board of Regents also strives to implement centralized enterprise resource planning systems. Centralized electronic student billing saves \$750,000 annually in postage, supplies, and credit card fees. The Board of Regents is responsible for the oversight of the State Authorization Reciprocity Agreement (SARA). The SARA consortium provides considerable savings in time and cost for the BOR.

The Board of Regents has a set interactive dashboards that are critical to making improvements to the regental system. The dashboards allow the BOR to understand where performance efficiencies and inefficiencies lie. Dr. Rush said he believes the South Dakota BOR has the most efficient higher education dashboard system in the country.

Dr. Rush presented information on the University Centers which are tailored to each community's learning needs. The University Centers are located in Rapid City, Pierre, and Sioux Falls. The committee members had several questions regarding the funding of the University Centers. Dr. Rush said enrollment at the centers needs to increase and if that does not happen something significantly different will need to be done.

Dr. Rush said the USD Law School is examining the various factors that impact their efficiency and have created a special task force to look at the delivery of legal education in South Dakota and that task force is chaired by Representative Mark Mickelson.

Several courses are shared between universities through the collaborative academic programs and Dr. Rush listed those courses. The shared resources create a significant cost savings. Dr. Rush said the Board of Regents has done a lot to consolidate services, but has also learned that consolidations do not always work.

Dr. Rush concluded by pointing out that South Dakota has a unique system that contributes to the fiber of an incredibly great state and was the first university system to be created in the United States.

Representative Sue Peterson asked for a report on the long-term vision of the Board of Regents and what can be done now to prepare for realizing that vision.

Update on State Facility Maintenance and Repair Projects

Mr. Scott Bollinger, Commissioner, Bureau of Administration, said the Bureau is responsible for maintenance and repair projects for multiple agencies. Each spring, the State Engineer requests a current project list from all facilities that receive statewide maintenance and repair funds. A rating scale is applied which uses seven criteria including: life safety, health and safety, age of the building, functionality, occupancy of the building, and the risk factors involved with the project. Projects can earn up to 103 maximum points on the scale; five additional points can be earned for energy conservation.

Mr. Bollinger reported that the State Engineer's Office reviews the projects, including ratings, cost, and how extensive the project is, to compile a final list. If the top projects are all at the same institution, the agency is asked if they can handle simultaneous projects at the facility without disrupting agency operations. Institutions are notified by July 1 as to what projects will be on the final list.

Mr. Bollinger then compared the construction process to the budget process. Deferred maintenance is a two-year appropriation because some projects take multiple years to complete and the time period during which the funds become available for use doesn't always coincide with the construction cycle. Depending on the estimated cost of the project, the process to interview and retain an architectural engineering firm before work can begin can add weeks or months to a project timeline. Mr. Bollinger said the target is to get the architectural engineering studies done by mid-December at the latest so bids can be issued before firms are committed to other projects.

Mr. Bollinger stated there are eight engineers in the State Engineer's office that are assigned to the various campuses to work with them on projects, each handling between 20 and 40 projects at a time. There are currently about 300 projects on the books with a value of more than \$500 million and 137 projects in play valued at just over \$37 million. He advised that an issue to watch for in the upcoming legislative session would be possible maintenance and repair needs for the newly created South Dakota Board of Technical Education.

Representative Hunhoff asked how architectural firms are selected and whether there have been situations in which the firm has changed midway through the project. Mr. Bollinger said once the needs of the project are determined, the information is sent to engineering firms and a firm is chosen from among those responding to the bid. **Ms. Kristi Honeywell, Deputy Commissioner and State Engineer, Bureau of Administration,** said in her ten years with the office, there have been two or three occasions in which the selected firm has struggled with a project and a new direction had to be taken.

Ms. Honeywell also responded to Representative Hunhoff's question about projects in litigation or dispute by saying less than a dozen projects are in liquidated damages involving delays, incompleteness, etc.

Senator Nesiba inquired whether the Bureau of Administration maintains a record of unfunded projects. Mr. Bollinger said in addition to his agency's overall deferred maintenance list, agencies also keep their own unfunded projects lists. The Bureau of Administration's deferred maintenance list has decreased in recent years from about \$90 million to \$52 million.

Mr. Monte Kramer, Vice President of Finance and Administration, Board of Regents, reported on the process for determining maintenance and repair needs on university campuses. The board compiles a 10-year maintenance and repair list based on the needs lists provided by the campuses; the current overall list is valued at \$468 million. About \$25 million is invested annually in maintenance and repair at the facilities.

Mr. Kramer told committee members that the board approves all the campus projects on the overall list. Institutions are allowed to shift funds from one project to another if needed, as long as both projects have been approved by the board. If they want to add another project due to an emergency, they must come back to the board for approval. Funds cannot be used to build new facilities but only to maintain existing facilities. Residence halls do not receive maintenance and repair funding and must generate their own money to maintain those facilities.

Other Fund Authority

Mr. Steven Kohler, Director of the Executive Management Finance Office, Bureau of Finance and Management, discussed cost allocation which is the cost for services incurred by the bureaus that is allocated to state agencies who use those services. This provides for centralization of services among state agencies and allows the state to leverage the federal awards it receives. Costs are allocated based on guidelines from the Federal Office of Management and Budget via the Super Circular (comprehensive guidance document for federal grant awards).

Five factors are considered in determining costs: type of costs, forecast of estimated expenses, when to account for those expenses, any over or under recovery, and what is a proper and reasonable allocation method. The goal

is to have revenues equal expenses. If the "zero" goal is not reached, the federal government can ask for a cash refund, request the individual program be credited, or seek an adjustment in future billings.

Mr. Kohler identified nine primary internal service funds at the Bureau of Administration, created to fund specific services offered to agencies and designed to be self-sustaining. The Bureau of Information and Telecommunications has two primary internal service funds – Data Processing and Telecommunications.

Mr. Kohler concluded by reiterating that the Super Circular dictates the standards and principals that must be followed and the Department of Legislative Audit audits the Bureau of Finance and Management annually to ensure they are following them.

Mr. Jeff Mehlhaff, Fiscal Analyst, Legislative Research Council, presented data regarding the Bureau of Information and Telecommunications' (BIT) internal service funds. The data trend indicates the agency over recovered for their expenditures in FY12, FY13 and FY16 and under recovered in FY14 and FY17, causing the funds to balance out over the course of several years. \$11.1 million from the General Fund was spent on BIT.

Representative Hunhoff asked if there is an over recovery and BIT collects more than it needs, what happens to the extra dollars. Mr. Mehlhaff responded that the money stays in the internal services fund to be used in the next year when BIT will under recover.

Mr. Lucas Martin, Fiscal Analyst, Legislative Research Council, explained the internal service funds for the Bureau of Administration. Four budget units feed into internal services: Administrative Services, Central Services, State Engineer, and Risk Management. When the data shows an over recovery, there may be a corresponding decrease in the rate the following year.

Selection Process for Construction Projects

Mr. Darin Bergquist, Secretary, Department of Transportation (DOT), reviewed the process used by the department to determine road construction projects. Decisions regarding what construction projects need to be completed are based on three main criteria: condition of the particular asset, safety, and capacity. Data that is constantly collected on the condition of the state's assets is electronically fed into the Pavement Management System which estimates the life of the road and recommends an effective treatment. A similar system is used for bridges. Traffic volume, current and projected for the next 20 to 35 years, is also analyzed as are accident records to ensure safety issues are addressed.

Mr. Bergquist said once the data is collected and prioritized, the Project Development Office works with field staff to compile a list of construction projects which becomes a tentative STIP that is first discussed by all impacted internal parties and then taken to the Transportation Commission for initial review. A public hearing process follows after which a final STIP is presented to the Commission for approval.

Responding to what impact Senate Bill 1 has had on the process, Mr. Bergquist replied that the benefit of the additional revenue means the department can get more done in a timely manner and defer less work to future years. The department received about \$89 million more after the passage of Senate Bill 1 with the funds being used for highway and bridge construction, the creation of the bridge fund, and the local buyout of federal funds which provides more flexibility in the use of general funds.

Mr. Bergquist noted that the majority of construction projects are managed by DOT staff but in situations where there's not enough staff available, consultant engineers are used. The department oversees project inspection and materials testing.

Project engineers monitor the day to day operations to see how much work is being done and the amount of materials being used. Every two weeks, a pay estimate is submitted based on the monitoring results; contractors receive progress payments every two weeks. A summary is submitted at the end of the project to determine the final amount to be paid.

Mr. Bergquist said changes are almost always made to the contract during the course of the project to account for the actual work, materials, etc. vs the estimates used for the initial contract. South Dakota compares favorably to other states in terms of the construction change orders issued.

In concluding his comments, Mr. Bergquist fielded questions on a bridge replacement that was delayed in Dell Rapids; construction work on Interstate 29 between Colman and Sioux Falls; and rest area closings.

Future Meeting Dates and Sites

The Joint Committee on Appropriations will tour West River State Facilities October 23-25, 2017. The Governor's Budget Address will be December 5, 2017.

Adjourn

A MOTION WAS MADE BY REPRESENTATIVE AHLERS, SECONDED BY REPRESENTATIVE ANDERSON, THAT THE INTERIM JOINT COMMITTEE ON APPROPRIATIONS MEETING BE ADJOURNED. The motion prevailed on a voice vote.

The Committee adjourned at 3:30 p.m.