Department of Administrative Services FY'18
Internal Service Fund Rate Review Committee Meeting

September 6, 2016
State Capitol Building, Room 445
350 North State Street, Salt Lake City, UT 84114

Committee Members:

Barry Conover, – Board Chair, Executive Director, Tax Commission
LuAnn Adams – Executive Director, Commissioner of Agriculture & Food
Becky Bradshaw – Comptroller, Department of Transportation (joined the meeting late)
Mark Brasher – Deputy Director, Department of Human Services
Joseph Brown – Division Director, Department of Public Safety
Matthew Lund – Budget and Policy Economist, Governor's Office of Management and Budget
Sal Petilos – Executive Director, Department of Alcoholic Beverage Control

Note: An audio recording of the meeting can be found on the Public Notice Website.

1. Committee Business:

a. Welcome - Ken Hansen, Interim Executive Director, Department of Administrative Services (DAS).

Ken Hansen welcomed everyone to the hearing and introduced the committee members.

b. Selection of a Committee chairperson.

Mr. Hansen opened nominations for the selection of a chair. Sal Petilos nominated Barry Conover for the committee chair. Mark Brasher seconded the motion. There was no discussion about the nomination. Mr. Hansen called for a vote for selection of Barry Conover as chair. The vote passed unanimously. Mr. Hansen turned the meeting over to Chairperson Conover.

c. Open and Public Meetings Act Training – Paul Tonks

Chairperson Conover recognized Paul Tonks, Assistant Attorney General, to provide Open and Public Meetings Act Training. (Power point presentation of the training, is available on the Public Notice Website.)

Mr. Tonks explained that the DAS Rate Committee is subject to the Open and Public Meetings Act. The statute requires annual training of the Open and Public Meetings Act for Boards and Committees. He briefly reviewed the training. The power point training will be available for the committee if they would like it sent to them. They may contact Barbara Sutherland to receive the power point OPMA training presentation.

d. Approval of minutes of September 1, 2015 meeting.

The committee members reviewed the minutes from the meeting held on September 1, 2015. Mr. Petilos moved to approve the minutes, Mr. Brasher seconded the motion, and the motion passed unanimously.

e. Overview of Rate Committee Responsibilities

Chairperson Conover recognized Mr. Hansen. Mr. Hansen reviewed updates to the rate packet previously distributed. He explained that packets sent to the agencies contained different pagination.

Mr. Hansen reviewed the committee's responsibilities and changes made by SB 52. The membership and duties of the committee are found at Utah Code Section 63A-1-114.

2. <u>Presentation by DAS Internal Service Funds</u>

Mr. Hansen, reviewed the DAS mission, vision, values, and goals. He described the DAS organization.

a. Department of Facilities Construction and Management – Ken Hansen, DAS Executive Director and Eric Tholen, Division Director

With consent of the chair, Mr. Hansen invited Eric Tholen, Director of the Division of Facilities Construction and Management, to provide information about DFCM rates. DFCM operates its building management service as an internal service fund (ISF)

Mr. Tholen explained that DFCM provides maintenance and management services to over 180 state-owned and leased buildings. The FY'17 revenues are estimated at $30M. DFCM is authorized to employ 134 full-time equivalent positions, and currently operates with 112 of those positions filled. DFCM manages over 7 million square feet of space throughout the state.

DFCM focuses on providing an efficient building operation to the agencies. The average operations cost is 25% below local private sector costs, and 48% below the national average. The cost per square foot for FY'16was $4.74, and the proposed cost for FY'18 is $4.85 per square foot.

Joe Brown asked if state buildings get benefits for being a state building.

Bruce Whittington, DFCM Assistant Director, explained that, generally, state buildings do not get extra benefits for maintenance. One exception is that buildings on Capitol Hill receive free water.

Mr. Brasher asked if state buildings are getting the proper oversite to maintain the buildings.

Mr. Whittington stated that the rates and costs listed cover the cost for facilities the state maintains. It is not for all the facilities. The State Building Board audits maintenance performance of all state-owned facilities.

Mr. Tholen stated that of the over 180 programs, DFCM is recommending rate adjustments for 15 programs. DFCM reviews each program on an annual basis and recommends adjustments as needed. Mr. Tholen highlighted several rate adjustments.

Mr. Petilos asked about the reductions, and the net earnings as portrayed on the graph presented.

Mr. Whittington explained that the program, as a whole, has positive retained earnings. DFCM accounts at the building or program level. Each of the 15 programs for which adjustments have been recommended are carrying a deficit in their retained earnings. DFCM reviews the rates annually and tries to limit rate adjustments to every three to five years. Rates typically go up as buildings age. DFCM establish the rates to take care of the current expenses.

Mr. Petilos asked if the Department of Alcoholic Beverage Control (DABC) is being charged the same rate as other facilities.

Mr. Whittington responded that DFCM cannot charge a uniform rate because each building is different. DFCM accounts for its costs at building level so it knows how much each facility costs to maintain.

Mr. Petilos asked to see the math on the rates for the deficit reduction on the DABC retail store facilities.

Mr. Whittington indicated that he would provide that information. He indicated that the last rate adjustment for the DABC retail stores occurred seven years ago, and it was a rate reduction.

Commission LuAnn Adams asked why the cost was going up at the Fairpark DMV.

Mr. Whittington responded that the Fairpark DMV had been operating off of positive retained earnings. There had not been adjustments on that building in five years. As the building ages, DFCM must make adjustments.

Mr. Conover asked DFCM to correct the label from Fairpark DMV to the Fairpark Driver's License Division on the list of rates. DFCM said it would make the correction.

Mr. Brown said the facilities and maintenance retain earnings it trending upwards. He asked what level of retained earnings is appropriate to manage DFCM.

Mr. Whittington said DFCM tries to maintain 10 to 20 days of operating expenses in its retained earnings. In FY'17 and FY'18 it is expected to go up to approximately 31 days.

Mr. Tholen said that until FY'13 net income was negative. DFCM attempts to set rates that allow it to operate in the black.

Mr. Petilos asked if there is any provision in the FY'18 proposed rates to make up for the FY'17 unfunded rates.

Mr. Whittington acknowledged that the rates were not funded for FY'17, but all the agencies paid the FY'17 rates with the exception of some DABC properties.

Mr. Brasher asked what would happen if the Legislature did not fund the rates for another year.

Mr. Whittington said if DFCM was in a position where the rates were unfunded again, they would discuss with each agency potential changes to service levels in the short termed to save costs. However, if buildings are neglected short term, the cost of maintenance will go up in the long term.

Mr. Tholen stated that many of the increases in the FY'17 rates were for utilities and other things outside of DFCM's control. The plan is to get the operating capital in place.

Mr. Hansen described the departments plan to help legislators understand the internal service funds rate process and ensure that the rate bill is properly vetted. This includes discussing rates with Infrastructure and General Government Appropriations Subcommittee at its next interim meeting. In addition, the Legislative Fiscal Analyst (LFA) prepared an issue brief on internal service funds, and presented it to the Executive Appropriation Committee (EAC) this summer. DAS anticipates that the ISF and rate discussion will continue at the Executive Appropriations committee meeting in November. Mr. Hansen said that DAS will make the rates part of its budget preparations during the upcoming session.

Mr. Conover asked Matt Lund how the Governor's Office of Management and Budget (GOMB) was looking at rates.

Mr. Lund stated that the Governor's budget recommended funding the rate adjustments last year. He stated that he anticipated the same this year, and GOMB is working with LFA to resolve some of these issues for the agencies.

Mr. Brown ask how DFCM determines when a rate increase is necessary.

Mr. Whittington stated that DFCM never automatically increases rates immediately when expenses are higher than revenue at a facility. DFCM works with facility managers to see what efficiencies can be achieved. DFCM usually waits to see if the cycle continues to determine if the rates will need to increased.

Mr. Tholen continued with the presentation, and explained that thirteen programs are new or are affected by scope changes. He also presented the garage rates which are billing rates for personnel that are providing services separate from those covered by service level agreements. These rate are based on actual costs.

Mr. Tholen reviewed the retained earnings chart. He explained that DFCM has been working since 2013 to get the income up to where it matched expenses.

DFCM recommended the committee's approval of the rate adjustment for 15 programs, 13 new programs or scope changes, the labor (garage) rate adjustments, and all other existing rates.

There were no other comments from the committee or public.

Mr. Brown indicated that he had received some additional information from DAS on administrative salary increases and incentives. He asked the committee if they would want to see the information before taking action. Mr. Petilos indicated his desire to see the additional information.

Mr. Petilos move to defer the motion to vote on DFCM's rates until the next meeting scheduled for September 13, 2016, to enable the committee to review the additional information on compensation.

Commissioner LuAnn Adams seconded the motion, a vote was taken, and passed unanimously.

b. Fleet Operations – Ken Hansen, DAS Interim Executive Director and Jeff Mottishaw, Division Director

Jeff Mottishaw, Director of the Division of Fleet Operations, explained that Fleet Operations has three programs that operate as ISFs: Motor Pool, Fuel Network, and the State Travel Office.

Motor Pool

Within the Motor Pool program, the state fleet consists of 7,864 vehicles, 4,750 are Fleet Operations vehicles, the rest are higher education and agency-owned vehicles. Fleet Operations maintain 340 private vendor network maintenance facilities. It also manages an on-demand motor pool partnership with Enterprise Rent-A-Car, and is rolling out an electric bicycle program.

The Motor Pool monthly lease rate is made up of the 2013 contract price for a vehicle, minus the salvage value, over the lifecycle of the vehicle. The current rate also includes fees that are added on to the rate: an administrative fee, a Management Information System (MIS) fee, and Alternative Fuel Vehicle (AFV) fee. The salvage level varies based on the class of the vehicle.

Mr. Petilos asked about the standard lifecycle of sedans.

Mr. Mottishaw indicated that the average lifecycle of sedans, is approximately six to seven years.

Mr. Mottishaw explained the proposed rate changes for the Motor Pool lease rates. Fleet Operations is currently approved to charge the 2013 contract price, but has been charging the 2013 price for the least expensive vehicle in the class. He explained one class of vehicles includes the Toyota Prius, and the Ford Focus. Fleet has been charging the rate for this class based on the lowest cost vehicle of class. Fleet Operations propose starting in FY'18 that it charge the rate as it has been approved. This is not a rate change but may impact some agencies. The total estimated impact would be approximately $79,600. Fleet Operations has also recommended removing the alternative fuel fee. That would reduce rates by $255,000. Fleet Operations also recommends the elimination of the premium fuel use fee, and the operator incentive alternative fuel use fee. Removing these fees would reduce rates by about $37,000.

Mr. Brown asked if Fleet Operations would track for agencies what kind of fuel operators are using, other than regular fuel.

Mr. Mottishaw said Fleet Operations would soon release an agency dashboard based on the IBM Cognos platform which will enable agencies to track the kind of fuel used, down to the transaction level.

Mr. Conover asked if the agencies were being reimbursed for fuel tax.

Mr. Mottishaw indicated that the excise tax is reimbursed to the agency.

Mr. Mottishaw wanted the committee to be aware that the Motor Pool has been working to reduce its debt to the general fund. The debt is now $31M. Fleet Operations is continuing work to reduce that debt.

Mr. Mottishaw explained the Motor Pool retained earnings. In FY'15, a decision was made to delay replacement of certain vehicles for a year, to increase the net income and retained earnings. In FY'16, Fleet Operations replace more vehicles, but not to the level that it should have. In FY'16, there is an increase in the retained earnings and a decrease in net income as they reduce their debt to the general fund. Over time the net income will be going down, but they will pass the 60 day retained earnings.

Mr. Petilos asked about keeping vehicles longer than they are useful, or keeping them longer than the salvageable life.

Mr. Mottishaw stated, in FY'15 a decision was made to push the replacement from 105,000 miles on gasoline engines to 120,000 miles. This resulted in $7.5M in vehicles that were scheduled to be replaced and were not. As vehicles age, they cannot be sold for as much, there are more repairs, etc. The plan moving forward is to catch up on replacing vehicles, and then reduce the life cycle of those vehicles.

Fleet Operations has contracted with a private vendor, Wheels, Inc. Starting in FY'17, Fleet Operations will lease a portion of its fleet from Wheels, and purchase the remainder. This will allow Fleet Operations to acquire more vehicles, without borrowing from the general fund.

Fleet Operations continues to expand its On-Demand Motor Pool. Enterprise will rent vehicles to agencies to help reduce underutilized vehicles. There are 20 agencies across the state that are using the On-Demand Motor Pool.

Mr. Brasher stated that Human Services is participating in the On-Demand Motor Pool and feels that this needs to be managed differently than the traditional fleet.

Mr. Petilos asked what the saving are from Fleet owning the vehicle, to agencies leasing vehicles from Wheels, Inc.

Mr. Mottishaw responded that there will not be a significant difference in cost for the customer. Fleet Operations will work with customers to decide if it would be best for them to lease the vehicle, or purchase it.

Mr. Petilos asked what the lease rates will be, and the length of the lease.

Mr. Mottishaw stated that Fleet Operations' contract allows for open ended leases. This will allow Fleet Operations to sell the vehicle when the lease is up, through Surplus Property, and give it flexibility with the terms, and miles, when selling the vehicle.

Mr. Brasher stated that he participated in the Request for Proposals (RFP) that resulted in the contract with Wheels, Inc. He explained that the fleet would be smaller, but consistent in use. It will help with the management of the fleet.

Fuel Network

Mr. Mottishaw explained the Fuel Network rates. There are 40,000 vehicles that participate in the Fuel Network. The network dispenses 18M gallons of gas. The fuel network maintains over 450 tanks state-wide, 130 sites with card readers, and 7 Compressed Natural Gas (CNG) fuel sites. These sites are compliant with federal and state regulations.

Fleet Operations is proposing an increase to its rate associated with low volume sites from $0.065 to $0.105. This will bring in approximately $82,000. This will bring the revenue in line with the expenses of maintaining low volume sites.

Mr. Mottishaw reviewed the fuel network retained earnings, and stated that Fleet Operations anticipates the program will break even by FY'18.

Mr. Petilos asked why Fleet Operations maintains a state fuel network, and how competitive the rates are.

Mr. Mottishaw explained that the network consists of state-owned sites, local private sites, and backup generators. Around the valley, most fuel is dispensed from private sites. In rural areas, Fleet Operations maintains fueling locations for schools and agencies like the Department of Transportation.

Jeff Done, program manager for the Fuel Network, explained that Fleet Operations is approximately $0.05 per gallon less than the commercial sites for gasoline, and $0.16 less per gallon for diesel. This saved state customers almost $900,000. Fleet Operations removed seven underground tanks this last year.

Mr. Conover said that it is important to maintain these fuel sites, in case of a disaster. Mr. Done is on the State's response team, and they have identified Tier 1 fuel sites, and keep 50% volume in these tanks at all times.

<u>State Travel Office</u>

Mr. Mottishaw gave an overview of State Travel. State Travel booked 5,642 car reservations, 7.675 hotel reservations, and 19,225 airline reservations, last year.

Fleet Operations is recommending changes to some of the funding mechanisms in the program to offset costs. These includes the rates charged to customers, the administrative fee on rental vehicle contracts, and the rebate from the travel card.

Mr. Mottishaw explained that it needs to reduce the administrative changes on rental cars to comply with changes to the procurement code. In addition, Fleet Operations is implementing a new travel card based on the purchasing card (P-Card) contract. There will be a rebate that is a little higher on the P-Card. There will still be about a $20,000 gap that State Travel will need to recoup.

Therefore, Fleet Operations is proposing to increase the Travel Agency service fee by $1 for each category. That will raise approximately $19,225, if bookings are similar to last year. Fleet Operations is asking the committee to allow State Travel to receive some of the administrative fees from State Purchasing for contract management services as well.

Mr. Brown asked if Fleet Operations is required by federal rules to keep the various programs separate as far as costs, and revenues in the ISF programs.

Mr. Mottishaw said yes, Fleet Operations is obligated by federal rules to keep the programs separate.

Mr. Petilos asked why the $1 was consistent for every category of customers.

Mr. Mottishaw explained that while the cost of travel agents has gone up consistently, they have tried to absorb additional service fees costs, but can no longer do it.

There were no other questions from the committee, or the public.

Mr. Petilos moved to approve the Division of Fleet Operations rates. Commissioner Adams seconded the motion. A vote was taken, and the motion passed unanimously.

c. Purchasing and General Services – Ken Hansen, DAS Interim Executive Director and Kent Beers, Division Director

Kent Beers, director of the Division of Purchasing and General Services, introduced the four ISFs in Purchasing and General Services, specifically: Cooperative Contracts; State/Federal Surplus Property; Print Services; and State Mail.

Cooperative Contracts

The State has over 750 Cooperative Contracts, and there is $1.9B total sales on the state contracts. The contracts are used by counties, cities, state agencies, school districts, higher education, and special service districts. State agencies are required to use the contracts, while others voluntarily do so. The vendors under contract pay a small fee. User agencies pay nothing. The current rate structure allows for Purchasing to charge an administrative contract fee up to 1.0%. Purchasing is not proposing a change to the rate. The current average fee is 0.39%.

Utah is a member of a national purchasing cooperative. State Purchasing manages 55 contracts as part of this cooperative. On these contracts, all 50 states come together to combine their buying power. A legislative audit looked at the cooperative contract program. The audit concluded that the National Association of State Purchasing Officials (NASPO) ValuePoint contracts have lower fees than other purchasing cooperatives. Administrative fees these contracts are three times lower than other purchasing contracts. State Purchasing saves money by using NASPO ValuePoint contracts.

The current cooperative contracts retained earnings balance is about $2.7M. The higher than normal retained earnings balance is needed to keep the cooperative contracting program functioning in the event of an economic downturn. Because so many entities rely on the use of the contracts, sufficient reserves must be maintained.

Purchasing will use a portion of the retained earnings to implement a program where Purchasing Contract Analysts are put into state agencies that do not have a sufficient contracting staff.

Mr. Petilos asked about the retained earnings being higher, and the Federal ISF rules.

Mr. Beers explained that Purchasing is required to pay the federal government a certain percentage of any retained earnings above the 60-day limit.

There was a slight loss in revenue in FY'16, and Purchasing is expecting the loss to be greater in FY'18 as Purchasing continues to reduce rates on individual contracts. Purchasing must adjust rates over time as contracts expire and new contracts are let.

Mr. Petilos stated that at some time the rates will have to change to remove the negative earnings.

Mr. Beers explained that the program started in 2012, so there is not a lot of history on moving the fees up and down on the contracts. The program requires fine tuning year to year.

State/Federal Surplus

The Surplus Property program saved Utah law enforcement agencies $95,950 through the Federal 1033 program. The Surplus program also saved governmental agencies $1,870,099 through the Federal Donation Program. Surplus uses the NADA Guide to determine value of surplus vehicles. It uses a variety of means to surplus vehicles. Outside vendor sales received 94% of the NADA resale values, and Surplus Property received 115% of the NADA resale values.

Mr. Petilos asked how close is the salvage on the fleet vehicles to NADA.

Mr. Mottishaw said surplus is doing a fantastic job on selling vehicles. Surplus Property is close to what NADA says the vehicle is worth. After Surplus takes its fee for doing all the work on selling the vehicle, the salvage value to Fleet Operations is 17 to 21%, depending on the condition of the vehicle. Mr. Mottishaw discussed a study of the surplus vehicle program that was conducted several years ago.

Mr. Beers said there have been many different studies done on the disposal of state vehicles. The studies show that the direct sales conducted through Surplus Property receive a higher value.

Surplus Property is proposing no changes to the rates in Surplus Property.

Mr. Beers reviewed the State Surplus retained earnings. The revenue goes up and down as the Surplus program sells what agencies surplus. He recommends higher retained earnings for Surplus Property. When Fleet extended the time period for which cars are disposed, there was $1M less in vehicles salvaged in one year. Surplus Property is also located at the prison. When the prison is relocated, Surplus will be required to move, and it will need some of these retained earnings to make that move.

There is negative retained earnings in the Federal Surplus program. Surplus will discuss this with the Federal agencies to determine if there should be a slight increase in the rates in the future.

Print Services

Mr. Beers gave a general introduction to Print Services and its service levels. He explained changes in volume associated with the shift of some services from Print Services to Utah Corrections Industries (UCI)

Print Services is not proposing any rate changes to their current rates.

Mr. Brown asked how Print Services maintains the system with the print jobs going down without a rate increase.

Mr. Beers responded that they have a contract with Xerox to do all the copying and printing. The only expense with the program is managing the contract.

Mr. Petilos asked if Print Services leases all the machines from Xerox.

Mr. Beers said that is what they do. The program is outsourced.

State Mail

Brian Jensen, the Program Manager for State Mail and Distribution Services, joined Mr. Beers.

Mr. Beers explained challenges related to the State Mail program. Volumes have been declining. The three services which contribute the most income have seen a decline in volumes from 2% to 10%. Mail and Distribution Services expects this trend to continue. The impact of the volume started in FY'15, and has been significant in FY'16 as well.

The net income and retained earnings balances are negative for FY'16. State Mail and Distribution Services asked an independent internal auditor look at the program. The auditor found that many courier routes did not cover costs.

Mr. Brasher asked why the state would continue with State Mail, and not use the US Postal Service. He asked if State Mail and Distribution Services had looked at anything that would be an alternative to State Mail.

Mr. Beers indicated that the program still provides savings, but that it will continue to monitor this. When the lifecycle of existing equipment ends, it will need to determine the most cost-effective options for the state including contracting services to the private sector. The Program is still viable, but in decline. State Mail and Distribution Services needs to develop a plan to address the demise of this industry. It will be a gradual plan as pieces of equipment lifecycles expire, and they decide whether to buy new equipment or outsource the work.

Mr. Brasher said his department may utilize these services and it may not be necessary, where there are services that would cost them less. He feels there should be some direction to help agencies understand the possibilities of using other resources for mail.

Mr. Jensen and his staff are available to help agencies with any particular mail job, or the overall management of mail.

Mr. Jensen discussed problems with the current rates. He explained solutions the audit helped State Mail and Distribution Services identify. Proposed rates, separated into a courier rate and a production rate, are more transparent so that each agency can assess its need and the associated cost, and then make an informed decision as to the best way to achieve the agency's needs.

The audit identified problems in the current courier system. It found that 70% of the time routes did not collect enough mail to generate revenue necessary to cover the costs of running those routes.

State Mail and Distribution Services conducted a customer survey to determine how many times agencies needed to have mail picked up. The results showed the majority of agencies needed mail picked up once a day or less. Approximately 5% of customers said that it was essential to have mail picked up more than one time per day.

Reducing the number of stops will allow reductions in routes, couriers, and the number of vans used to deliver the mail. By reducing the stops, the routes would be reduced from 16 to 10 routes, and the result would be a savings of $302,400 per year.

Mr. Brown asked why they could not begin reducing routes right now, and if they need the committee's approval.

Mr. Jensen said he plans to start implementing these changes in FY'17.

Mr. Hansen asked that this be made part of the motion at the end of the presentation.

Mr. Beers stated that State Mail and Distribution Services could have gone forward with the route reduction, but the wanted to have the new rate structure ready for the committee's approval. Under the current rate structure State Mail and Distribution Services can start eliminating routes. The new rate structure would not take effect until FY'18.

Mr. Petilos asked if the agencies are willing to not have multiple mail pick-ups each day, and if they have talked with their customers.

Mr. Beers said that DAS wants to provide great customer service. State Mail used to be able subsidize the multiple mail pick-ups, but with declining volume, it can no longer subsidize unprofitable routes. Every service an agency wants needs to have an appropriate rate, so agencies can decide what they need. With the new rate structure, customers can decide what they need by location.

Mr. Jensen said his office has spoken with the major agencies using mail services. This will be a process that will take several months. If an agency no longer wants the services, State Mail will help these agencies identify alternatives. He noted that the state had contracts with both UPS and FedEx, and some agencies already use them.

Mr. Conover said that the Tax Commission will be cutting back on some of the courier stops. He expressed some concern on the method used to establish the courier rate. He thanked State Mail for sending the Tax Commission the detail behind the rate structure from the auditor. He thinks it would be helpful for all agencies to see it. The committee will be sent the analysis on the rates.

Mr. Conover said their services are needed, for the state as a whole, because it is still more cost-effective than relying on the US Post Office and other vendors.

The new courier rate structure is based on 12 different zones. For each zone, State Mail and Distribution services calculated mileage and average minutes from state mail to the different stops as well as every stop within the zones. The proposed rate for each zone covers the cost of the van, and its maintenance, and the courier's salary and benefits.

State Mail and Distribution Services recommends that agencies residing in the same building work together to provide a single mail drop-off and pick-up location. This would allow all of the agencies in a building to share the stop rate. Otherwise, agencies will be charged a stop rate for each office to which mail is delivered.

Mr. Brasher expressed concerned about mail that needs to be secured area.

Mr. Jensen said that every centralized mail location is required to be secured.

Mr. Petilos asked if State Mail would see more revenue, or would the agencies see more savings.

Mr. Jensen explained that the agencies will see more savings, but State Mail will not see more revenue from the stop, but it will allow them to see cost reductions from eliminating stops. State Mail will need fewer couriers.

Mr. Conover said there is an issue of safety with mail. It is safer to have a centralized mail drop, because of the chance of dangerous substances being sent through the mail. Agencies may need to have staff to handle the mail.

Mr. Jensen indicated that State Mail is proposing to eliminate the existing distribution fees and the task distribution fees. These rates generated $1,689,343 in FY'16. The new courier rate will cover the cost of these two fees.

The new production rate schedule will cover the services agencies are requesting and are structured so that the agency can clearly see the cost associated with each service.

Mr. Conover asked if agencies would be notified about any changes in advance to make adjustments with bar coding etc.

Mr. Jensen said State Mail will work with agencies to address needs. He addressed how changes will cover costs, and will net around $100,000 per year, with the new rate structure. He discussed the cost of processing a piece of mail. If an agency chooses to process its own mail the cost for sending a one-ounce envelope will be $0.47 for postage. That does not include what it costs the agency to have the letter prepared to be sent, such as folding, metering, inserting, etc. The cost through the post office, for a two-ounce envelope is $0.68, and does not include fees associated with preparing the envelope. The State Mail rate is still lower than other mail services.

Mr. Brown asked about the increase for "other" on the rate impact summary for FY'18.

Mr. Jensen said there are other agencies that are not state agencies that use State Mail services. Those are reflected in the "other" category.

There were no other questions from the committee.

Mr. Conover asked if there were any comments from the public.

Michael Jones, Finance Director for the Department of Financial Institutions, understands State Mail is in a tough situation with the decline in mail, and State Mail need to make a change in their service model. The mail is important and cannot be sitting in an office waiting to accumulate enough mail to make the pick-up cost effective.

He expressed concern with the courier service changes being proposed. He said State Mail is taking a variable rate service and applying a fixed rate cost to it. The new rate being proposed is

$0.475 per letter. This does not include the cost of the courier service. He said his office could save $5 per day by taking mail directly to the Post Office.

Mr. Jones is also concerned that if his office drops the courier service, it will also lose inter-departmental mail service. He said mail will continue to decline and State Mail cannot keep increasing the costs of the courier service. He encourages the committee to take a hard look at the proposal.

Mr. Beers agrees it does not make sense to have mail services for five letters a day. That is why it will be left up to each agency to decide if it wants to use State Mail services. Eventually, as mail declines, the service will only make sense for agencies like Tax Commission that have large mail volumes.

Commission Adams asked how an agency will opt out of using state mail.

Mr. Jensen indicated that State Mail will work with each agency and provide transition services to use the U.S. Postal Service.

Mr. Brown said that agencies need to understand that inter-office mail will be discontinued if the agency discontinues courier service.

Mr. Petilos said that many agencies are not aware of the changes and how it will affect them operationally. He asked if leaving rates at current levels would make sense.

Mr. Beers asked John Reidhead, Director of the Division of Finance, to comment. Mr. Reidhead referred to the proforma financial statement for the mail program. FY'16 shows a $734,000 loss, and for FY'17 losses are projected at $416,000 at current mail volumes. In total, negative retained earnings are projected to be over $1M at the conclusion of FY'17. Mr. Reidhead stated that in his opinion, action must be taken now to stop the losses and also to reduce the negative retained earnings. He said that state law expects an ISF to operate on a break even basis. Borrowing from the General Fund is limited to 90% of the program's capital assets. State Mail will likely be out of compliance with state law if changes are not made. Also, the federal cost negotiators look unfavorably on negative retained earnings and will not allow the state to continue in a negative position indefinitely without consequence.

Mr. Hansen said there may be incidents where agencies would be better off to use the U.S. Postal Service. State Mail will put together a packet to help agencies work with the post office. State Mail must make changes, but will work with its customers to minimize the impact of the changes.

Mr. Brown referred to the proforma statement. The services are declining, and the expenses are not declining.

Mr. Jensen said that State Mail is looking at the decrease in the amount of manpower needed to run the facility. As the volumes decline the same manpower to process the volume of mail is not required. State Mail is looking at restructuring the production floor, job sharing and reducing the number of couriers and vans.

Mr. Beers said they will eliminate six employees and the cost of six vans within the next year. Going forward the expenses will be reduced.

Mr. Brasher indicated that other alternatives should also be considered. The state is mailing material that may make more sense to send electronically. State Mail needs to reach out to the departments and divisions, to see what they are using the service for, and what the alternatives might address needs.

There were no other questions or comments from the committee or public.

Mr. Conover asked state mail to get the details about the courier changes and rates out to the agencies. He asked the committee for a motion.

Commissioner Adams suggested that State Mail go through the SUCCESS Framework program.

Commissioner Adams made a motion to approve the production rate structure as presented for the FY'18 rates, and the existing rates that were presented. Becky Bradshaw seconded the motion.

Mr. Brown made a substitute motion to defer action until September 13, 2016. This motion failed for lack of a second.

Chairperson Conover asked for a vote on the first motion, to accept rates, current rates, and the new rates. A vote was taken.

Becky Bradshaw voted yes
LuAnn Adams voted yes
Barry Conover voted yes
Sal Petilos voted yes
Matt Lund voted no
Joseph Brown voted no
Mark Brasher voted no

The motion carries to accept the rates as presented.

d. <u>Risk Management</u> – Ken Hansen, DAS Interim Executive Director and Tani Downing, Division Director

Tani Downing, director of the Division of Risk Management, presented Risk Managements rates. She described the four ISF programs operated by Risk Management: Liability, Property, Auto, and Workers Compensation.

<u>Insurance</u>

Ms. Downing explained similarities and differences between Risk Management and traditional insurance providers. Similarities include premiums, the insurer determining what's being insured, the general liability exclusions from coverage, and an actuary determines premium based on loss experience.

In some ways Risk Management is different. Its coverage is broader that what individuals can buy on the market. Risk Management cover things that home owner's policies do not cover. Agencies covered by Risk Management are part of a pool that shares the impact of losses. The pool distributes the impact of a catastrophic loss. Rates are affected by an agency's loss history, losses of other members of the pool, and insurance market changes.

Ms. Downing explained the excess insurance coverage Risk Management purchases on behalf of covered entities. This year one of the three insurers large enough to cover the state dropped out of the market. As a result, excess coverage costs jumped, and less coverage is available.

Liability premiums will increase $75,000, for the whole pool. Within the pool, individual entities premiums will go up and down, based on loss history and risk exposure. Risk Management passes to the agencies what the actuary says each agency should be charged based experience and their portion of the pool. Charter school rates will increase from $8 to $9 per student.

The insurance retained earnings go up and down depending on the claims' cost.

<u>Property</u>

The Risk Management fund insures over $34 billion of State Assets.

Risk Management commissioned an independent rate audit from Flatiron Risk Advisors. Flatiron looked at the liability, auto, and property rates, how the actuary determined the rates and found that the rates followed industry standards. Flatirons shopped randomly selected properties covered by Risk Management against the market. They found Risk Management's property premium to be 38% to 90% less expensive than the market.

Risk Management is not recommending any rate increases, but overall the premiums will go up by around $123,000.

Risk Management is below its 60-day retained earnings for property. Risk Management will issue an RFP to hire an appraisal company to appraise all buildings over $1M.

<u>Auto</u>

Ms. Downing reviewed the current premium rates for vehicles Risk Management insures. Auto accidents continue go up. Last year, the rate committee authorized the deductible to go up to $1,500. Risk Management is not ready to implement that yet. There are minimal retained earnings in the auto insurance program.

Risk Management is not recommending any auto rate changes this year.

<u>Workers Compensation</u>

Last year, Risk Management recommended the reduction of workers compensation rates because Risk Management was collecting too much money. Ms. Downing reviewed the reduction for the agencies which will continue for this fiscal year.

Risk Management does not recommend any changes to the workers compensation rates for FY'18.

With the excess retained earnings in the Workers Compensation account, Risk Management plans to implement a safety grant. Agency will be able to apply for safety equipment and resources that will help the agency decrease its workers compensation claims.

Ms. Downing requested that the committee take action to approve liability premium changes, the charter school rate increase, and to approve all other existing rates.

There were no questions from the committee or the public.

Mr. Lund moved to approve Risk Management rates as presented. Mr. Brasher seconded the motion. A vote was taken and the motion passed unanimously.

Chairperson Conover indicated that the committee had come to the end of its allotted meeting time. He asked the Division of Finance to present its rates at the next meeting on September 13, 2016.

Mr. Petilos made a motion to adjourn. The vote was unanimous. The meeting adjourned at 12:01 p.m.