Approved: February 3, 2009
Date

MINUTES OF THE HOUSE GOVERNMENT EFFICIENCY AND FISCAL OVERSIGHT COMMITTEE

The meeting was called to order by Chairman Jim Morrison at 3:30 p.m. on January 28, 2009, in Room 535-N of the Capitol.

All members were present except:
Representative Tom Sloan- excused

Committee staff present:
Renae Jefferies, Office of the Revisor of Statutes
Daniel Yoza, Office of the Revisor of Statutes
Hank Avila, Kansas Legislative Research Department
Mary Galligan, Kansas Legislative Research Department
Gary Deeter, Committee Assistant

Conferees appearing before the committee:
Representative Jeff King
Senator Chris Steineger

Others attending:
See attached list.

The minutes for the January 20, 2009, meeting were approved. (Motion by Representative Neufeld; seconded by Representative Landwehr)

Representative King requested that the Committee sponsor a bill creating a zero-sum budgeting process for state agencies. He said the proposed bill will establish a six-year rotation so that an agency need not create a new budget every year. A motion was made (Representative Burgess), seconded (Representative Neufeld), and passed to sponsor the bill.

Representative Burgess noted four bill requests which he made at the January 20 meeting, adding a further request for new legislation to adopt standards for electronic committee processes and archiving of legislative bills. Representative Burgess made a motion, seconded by Representative Spalding, to introduce the bill as a committee bill. The motion passed.

Senator Chris Steineger, commenting on the state's economic crisis, recommended that the Committee consider selling the University of Kansas Hospital (Attachment 1). Tracing the background of the hospital, he noted that the Kansas University Hospital Authority was created to be separate from the Kansas University Medical Center; he noted that the former is now a quasi-private entity. He referenced **SB 372** from the 2007 session which would have, had it passed, sold the hospital. He observed that the value of the hospital included not only the physical assets, but the brand and the good reputation of the hospital. Members discussed whether or not state ownership was needed to receive Medicare and Medicaid reimbursements. Answering a question, Senator Steineger said the pending designation of the hospital as a cancer center should not be

affected by its sale, since the designation depends more on the amount of research and the quality of medical services than on ownership. Members raised the possibility of unintended adverse consequences to the Graduate Medical Education program if the hospital were to be sold.

The Chairman requested that the work groups report their findings and make appropriate requests for bill introductions.

Representative Burgess reported that a bill is presently being drafted to create a stabilization fund to put funds in reserve during good years to provide a funding bridge during lean economic years. He reported that the Performance Measurement Management Commission has developed a draft report of their work, which can be incorporated into a bill to create a pilot project. He stated that a pricing flexibility bill is also being drafted.

Representative Trimmer reported that a bill is being drafted to modify the waiver in the state-use law that requires school districts to show purchasing preference for certain state vendors. According to the proposed legislation, a school district will be permitted to purchase locally if the price of an item is at least 10% less than the price in the state catalogue. He noted that modification in the state-use law will save school districts thousands of dollars in the purchase of toner cartridges alone.

The Chair reported on the proposal to sell unused state assets and property. Members noted the difficulty of obtaining accurate information about what property is owned by the state. A member recommended a magazine article addressing this issue (Attachment 2). Members agreed that a general-concept bill might be an initial course of action.

Representative Burgess made a motion, seconded by Representative Vickrey, to introduce as Committee bills the proposed legislation mentioned above and the ones introduced by Representative Burgess on January 20. The motion passed.

Representative Neufeld reported that a bill was being drafted to restore to the state budget items that were taken off budget in 2002. Referencing the budget shortfalls and the fact that state employees might be furloughed, he recommended creation of a policy addressing the issue. Answering a question, he said revenue transfers would also be included in the first bill. Representative Neufeld made a motion, seconded by Representative Landwehr, to introduce the two bills above as Committee bills. The motion passed.

Representative Vickrey reviewed the Kansas Whistle Blower statute, saying that it was weak in providing confidentiality to individuals who report deficiencies in the workplace and noting that Kansas was ranked 29th nationally by the Public Employees for Environmental Responsibility. Staff Renae Jeffries commented that Connecticut has a whistle-blower statute similar to Kansas with a stronger employee protection component. After some discussion, Representative Vickrey made, and Representative McCray-Miller seconded, a motion to introduce a bill that would amend the Whistle Blower Act to extend its protections to more employees. In drafting the bill, staff was instructed to look at the Connecticut law and to work with Representative Vickrey on specific provisions. After some discussion to assure that the bill would include temporary employees as

well as full-time employees, the motion passed. Representative Roth voted no.

Representative Spalding thanked members of her work group and staff for their efforts and offered details regarding their findings:

- Statute books provided to legislators cost $90,000 annually to be printed. The Committee may want to recommend legislators opt in to receive the books rather than opt out.
- A complete set of regulations is published every three years at a cost of $250,000.
- The recommendation to replace state vehicles with hybrids does not have enough data to warrant any action at this time.
- Energy conservation measures such as lighting currently have no state standards by which to judge a knowledgeable course of action.
- No creditable study has been made to ascertain the number and location of state-owned properties. Post Audit and the Department of Administration have attempted to gather such information, but currently no database exists to provide this information.

A motion was made, seconded, and passed to draft a bill creating a dababase reflecting state property ownership. Using the Property Valuation Division of the Kansas Department of Revenue, counties can report state property to the Department of Administration, which will create the dababase as a part of the state transparency website KANView. (Motion, Representative Spalding; second, Representative Neufeld.)

The Chair announced that further reporting from the work group will continue at tomorrow's meeting; he adjourned the meeting at 5:17 p.m. The next meeting is scheduled for January 29, 2009.

HOUSE GOVERNMENT EFFICIENCY AND FISCAL OVERSIGHT COMMITTEE

GUEST LIST

DATE: JANUARY 28 2009

NAME	REPRESENTING
Wil Leiker	KS. AFL-CIO
Joe Mosimann	Hein Law Firm
Tom Krek	KASB
Lindsay Holwick	KBA
Juan Luengo	FARMERS INSURANCE
Jane Carter	KOSE

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SENATE CHAMBER

An outline to sell KU Hospital

Companion to SB 372 – From 2007 Session

1. Most big city hospitals are owned by private industry or non profit groups like the Sister Servants of Mary. Very few big city hospitals are owned by state government.

   KU Hospital was semi privatized in 1998 when the Legislature spun it off into the KU Hospital Authority with its own separate management, board of directors, budget, personnel department, etc.

2. I suggest the following conditions apply to any sale.

3. The minimum price will be $800 million. The minimum price of $800 million was arrived at through two different EBITDA (Earnings Before Interest Taxes Depreciation and Amortization) analyses and does not include the intangible value of being co-located with a major medical training and life sciences research facility.

4. One-half of sale proceeds, ($400 million) will go to fund KPERS liability which saves $1.26 BILLION over next 25 years. The other half to the State General Fund.

5. KU Medical Center shall remain owned and operated by the State of Kansas and be renamed the Kansas Life Sciences Research Center.

6. The new owner of the hospital will pay full property taxes.

7. The sale contract should include specifications about maintaining charitable care.

Attachment 1
GEFO 1-28-09

February 17, 2009 –
2:00 PM EST | 11:00 AM PST
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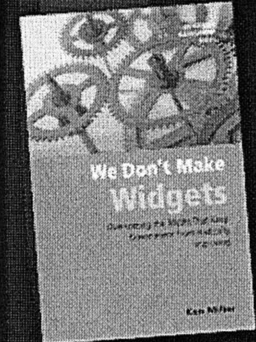

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– Michael Lawson
Director, ICMA Center for Performance Measurement

From *Governing*'s January 2007 issue
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MANAGEMENT/FINANCE

Unloading Assets

Cities and states are selling off bits and pieces of infrastructure. Is it a sweet deal or a mistake?

By CHRISTOPHER SWOPE

Richard M. Daley might say, with a wink and a nod, that he's got a bridge he'd like to sell you. Except that Daley has already sold it. It's called the Chicago Skyway, and a Spanish-Australian consortium gave him $1.83 billion for it. The mayor might also like to offer you his four downtown parking garages, but as it happens, he's just recently sold those too. Morgan Stanley, the Wall Street investment bank, paid Chicago $563 million for them.

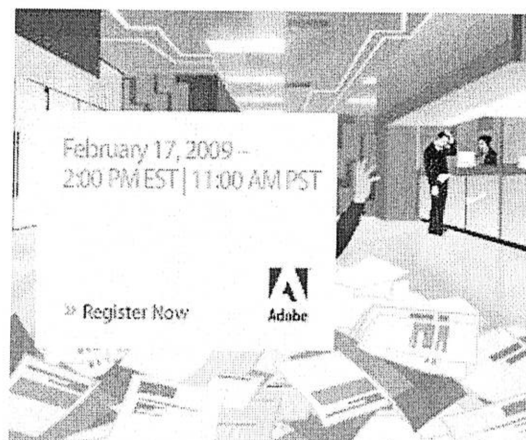
Related Links

Q&A with three experts:

- Bradley Abelow, New Jersey treasurer
- Dana Levenson, chief financial officer of Chicago
- Edwin Harrison, director of financial services, Harris County, Texas

For those who feel they've missed out on Windy City souvenirs, not to worry. Mayor Daley is putting more pieces of his city's infrastructure up for sale. Next: Midway Airport, the busy hub for Southwest Airlines. Daley wants a deal for the city-owned airport, and he wants it this year. (Buyer beware: Bring lots of cash. We're talking billions.) After that, the mayor wants to unload several recycling centers. He may also put a for-sale sign on a bunch of city-owned marinas.

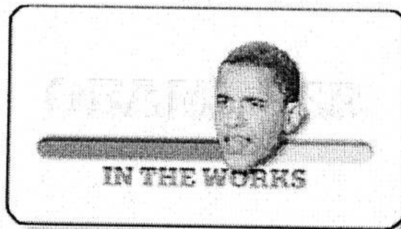
Chicago is in the midst of what's looking more and more like a liquidation sale. There may not be an "Everything Must Go" banner hanging at City Hall, but the new attitude there is that certain public assets SHOULD go if the price is right. "The city will never give up schools, police programs and parks — things we do well," says Daley's dealmaker, Chief Financial Officer Dana Levenson. "But what's the incentive to hold on to the things we don't do well when there's a market now that will pay the city lots of money for them?"



Chicago's way of thinking about infrastructure is still unusual in the United States. But ever since Daley sold the Skyway — or more accurately, leased it for 99 years — more state and local leaders have begun asking whether they, too, might unload a few hard assets. So far, toll roads are getting the most attention. In Indiana, Governor Mitch Daniels sold a 75-year lease on the Indiana Toll Road for $3.85 billion. Soon after, Virginia facilitated a 99-year lease of the 9-mile Pocahontas Parkway for $603 million. Pennsylvania's Governor Ed Rendell is

Attachment 2
GEFO 1-28-09

putting the Pennsylvania Turnpike out to ', and governors in Illinois, New York and Delaware all have expressed interest in seeing what their states' turnpikes might fetch on the world's financial markets.



"Okay, we will."

PolitiFact

More than just toll roads are in play, however. In New Jersey, Governor Jon Corzine asked the investment bank UBS to scour state government for items to consider privatizing. The study put the New Jersey Lottery and development rights around transit stations at the top of the list, right alongside the New Jersey Turnpike, Garden State Parkway and Atlantic City Expressway. Treasurer Bradley Abelow is now winnowing the list down to items the state will take bids on. "I was worried that people would view it as a fire sale," he says. "In fact, it's quite the opposite. We're starting with the presumption that we don't know what the answer is, just the questions to ask."

These kinds of deals would have been unthinkable not long ago. But in the past year or two, pension funds and other investors have decided that American infrastructure makes a good long-term investment. At first, this emerging market was dominated by companies from Australia and Europe, where private concessions for toll roads and airports are nothing new. (Macquarie Infrastructure Group, an arm of an Australian bank, and the Spanish highway manager Cintra successfully teamed up on both the Skyway and Indiana Toll Road deals.) But now U.S. firms such as Goldman Sachs and the Carlyle Group are raising their own multibillion-dollar investment funds. In total, as much as $100 billion is waiting to be invested in public assets that produce their own revenue streams from tolls or fees.

As Dana Levenson sees it, that's a seller's market. Chicago, which has been called the "Silicon Valley of infrastructure privatization," has used proceeds from its two concession agreements so far to pay down huge sums of debt and raise its credit rating. Levenson believes that governments have an obligation to at least consider selling off some of their infrastructure, even if they ultimately opt to hang on to it. "With as much money as is amassing in these funds, I can't imagine anything less intelligent than dismissing it out of hand," he says.

There are plenty of critics, however, who see Chicago-style sell-offs as a sellout. In Indiana, where public-opinion polls showed 2-to-1 opposition to leasing the toll road, the idea of paying tolls to foreign firms made many residents uneasy. The same was true in Harris County, Texas, which studied selling its network of local toll roads last year. The county council decided not to do it — despite eye-popping estimates that put the market value as high as $20 billion. "We're not leaving that money on the table, we're taking it over time," says Edwin Harrison, the county finance director. "It has to be quite obvious," Harrison adds. "If anyone comes in and gives you a billion dollars, they certainly expect to make twice or three times that. They're not doing this because they want to do a public service."

A QUESTION OF CAPITAL

When Macquarie's D.J. Gribbin makes the case for privatizing infrastructure, he likes to invoke Hernando de Soto. Quoting a Peruvian economist to an audience of state and local officials may seem an odd choice, especially since de Soto's area of expertise is third-world poverty. But Gribbin thinks de Soto's book, "The Mystery of Capital," helps explain why public infrastructure belongs in private hands.

De Soto writes that trillions of dollars of "dead capital" is locked up in the shantytowns of developing nations. This is so because inadequate systems of property law prevent people from using their primary asset — their homes — to create more wealth. In the United States, Gribbin also sees dead capital spread across the land. It's not locked up in tin roofs and mortar but rather in toll roads and other assets that government doesn't manage aggressively. "Though the state has title to the asset, it's trapped in a non-market context," Gribbin says. "As soon as you move that asset into a market context, now all of a sudden you've opened up the world to value that asset."

The Indiana Toll Road is a good example of what Gribbin is talking about. Before Governor Daniels took office, toll rates had stayed put for 20 years. For five of the past seven years, the road experienced negative cash flow. To get a handle on what the status quo

was worth to Indiana, the state's accountant projected out revenues and expenses over years, assuming that the road would continue to be managed basically as it has been the past. The accountant came up with a net present value of $1.9 billion.

By contrast, Macquarie/Cintra cut Indiana a check for $3.85 billion. In addition, the companies agreed to immediately pay for an electronic toll-collection system, widen 7 miles of congested road and not only build a new state police post but also contribute to the salaries of new state troopers. What's more, the private operators will pay for all operations and expenses, as well as any further capital improvements necessary to keep traffic moving at levels spelled out in the concession agreement.

By Gribbin's calculus, Indiana is bringing $2 billion of dead capital to life — more if you consider all the road improvements. Where does that "unlocked value" come from? First and foremost: higher tolls. After a few years, Macquarie/Cintra will be allowed to set toll rates at whatever the market will bear. As John Schmidt, a Chicago lawyer who advised Indiana on the deal, puts it, "The reality is public entities are not capable of raising tolls in an economically rational way. By shifting toll-setting power, within limits regarded as politically acceptable, you can create additional value."

Other sources contribute to that $2 billion windfall. Macquarie/Cintra thinks it can run the toll road more efficiently than Indiana did — electronic toll collection is a big first step. In addition, the concessionaire is able to depreciate the toll road on its federal taxes — a break that Indiana can't leverage since states don't pay taxes. And long-term investors seem willing to pay a premium for the sort of stable revenue stream that a proven toll road such as Indiana's can produce. Macquarie/Cintra expects to earn a return in the range of 12 percent. That beats the bond market any day, with less risk than investing in equities.

Governor Daniels and his staff couldn't be happier with the deal. Before, Indiana was looking at a $3 billion backlog in highway projects around the state and no money to pay for any of them. Now, Indiana claims to be the only state with a fully funded 10-year transportation plan. The state treasurer's Web site shows interest on the up-front lease payment piling up at a rate of $6 per second. "Nobody knows what will happen in 75 years," says Daniels' finance director, Ryan Kitchell. "There might be flying cars that don't use the Toll Road, and we'll look really smart. Nobody knows. What we do know is we have $4 billion in the bank earning interest today. And we'll put it into the ground building and maintaining roads that should throw off jobs and economic benefits that last the whole time."

THE ROAD NOT TAKEN

Daniels' critics aren't convinced. Forget the dead-capital argument, they say. This is a desperate and shortsighted play for cash. Had Indiana instead committed itself to aggressive public management of the Toll Road, it would be the taxpayers, rather than private investors, who would be enjoying those comfy long-term returns. "The fact is that the road was never intended to be a money-maker," B. Patrick Bauer, the incoming Democratic House speaker, wrote in an op-ed last year. "However, now that the governor has installed a plan that eventually will increase those tolls, why not keep control of the Toll Road in our hands?"

Similar thinking is what ultimately turned Harris County against leasing its own toll roads. "Government does not inherently have to run the thing poorly," Harrison says, noting that he believes the county does a solid job of managing its toll roads. "So why should I have my people — Americans, Texans, the people who live here in Harris County — pay tolls to somebody in Spain or Australia?"

If much of the opposition to privatization is philosophical, there are also pragmatic reasons to worry about these infrastructure deals. Most have to do with the risks inherent in leases that last for as long as 75 or 99 years. For example, how does one predict what an asset such as a toll road will be worth in 2081? Even privatization proponents admit that valuations are mostly guesswork. In other words, $3.85 billion sounds like an awful lot of money for Indiana to get for its Toll Road, but nobody can say with authority that the state shouldn't have gotten more — or less.

Another long-term risk is that expectations will change over time. In Indiana, as in Chicago, lawyers have done their best to predict what sorts of operational issues may come up over the decades. Look no further than the thickly detailed leases, specifying everything down to who's responsible for cleaning up road kill (Macquarie/Cintra is). The risk is that unseen issues may come up, or that terms agreed to in 2006 may seem like a bad deal in 2056.

Or sooner. North of the U.S. border in Toronto, it took only five years for a $3.1 billion

toll road sale to go sour over the issue of toll increases. When the concessionaire (Macquarie/ Cintra again) began raising tolls — as was its right under a 99-year lease — drivers and elected officials balked. Ontario took the concessionaire to court to stop the toll hike. The government lost, and the tolls were allowed to go up.

Toronto's lesson for U.S. officials has nothing to do with whether the government was right or wrong in its actions. Rather, the lesson is that the billion-dollar glow surrounding these deals lasts for only a little while. Once that light fades, what's left is a public-private marriage that goes on for almost a century. For better or worse, Mayor Daley and Governor Daniels have agreed to transportation and infrastructure policies that won't just outlast their administrations. Those policies will outlast the lifetimes of their own grandchildren.

HIGH FLIER

None of this fazes Dana Levenson. A former banker, Levenson came to work for Chicago at the end of 2004, just before the Skyway deal closed. Soon after, Levenson got to work on selling Chicago's parking garages. Now he's working on the Midway Airport deal. When a reporter suggests that Chicago has shown the way for other states and local governments considering infrastructure sales, Levenson replies only half-jokingly: "Yeah, they should send us a gift. We'll take the money."

In Levenson's mind, there is no doubt that the private sector runs certain operations better than government can. Take parking. Chicago's four downtown garages, beneath Grant Park and Millennium Park, were priced below-market yet still had lots of empty spaces. Levenson describes how he and other city officials would get regular e-mail reports about parking revenues. "We'd see the numbers go up and the numbers go down. The question is: Do we care? I care, because I'd like to see more people park there because that means more revenue to the city."

The way Levenson reasons, city government will never give the person monitoring the garages a performance bonus if he gets the garages to 99 percent capacity and won't fire him if it continues at 70 or 80 percent. "If the asset can be run better," Levenson concludes, "why not see what the market would bear?"

In the case of the parking garages, the market bore $563 million. In a sign that the infrastructure market is growing more competitive, 13 companies bid on the concession — compared with five on the Skyway deal. Chicago went with an offer from Morgan Stanley, which partnered with a parking manager that will run day-to-day operations at the garages. Chicago plans to use proceeds to pay off outstanding debt on the facility and create a trust fund that will generate enough interest to replace the park department's lost revenues. That will still leave $122 million to invest in capital improvements in neighborhood parks around the city.

Negotiating a deal for Midway Airport, Levenson admits, is much trickier than selling parking garages. For one thing, there are safety and homeland security concerns to contend with. But the bigger challenge is red tape. U.S. airports can be privatized only under a limited federal pilot program, so any deal Chicago strikes will require approval from the Federal Aviation Administration. Federal law also requires that most of the airlines at Midway sign off on the agreement. Historically, U.S. airlines have opposed airport privatization for fear that the landing fees they pay would inevitably increase. (Levenson declined to comment on how negotiations with Southwest and the seven other airlines that serve Midway are going.)

What's clear is that other states and cities will be watching closely. If Chicago reaps billions, expect more deals to follow — and pressure to build on Congress to open airports across the country to private management. "If Daley pulls off the Midway deal," says Robert Poole, a transportation expert at the Reason Foundation, "it will be as big an earthquake to airport privatization in this country as the Skyway deal was to toll roads."

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