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Sherry C. Diel, Director

Sam Brownback, Governor

To: Senate Appropriations Committee
From: Sherry C. Diel, Executive Director
Date: January 24, 2011
Subject: **SB 16**—Opposition to Section 7 Proposing a 10% Shrinkage Rate and Reduction from Kansas Real Estate Commission's FY 2011 Budget

Chairperson McGinn and members of the Senate Ways and Means Committee, thank you for the opportunity to share the Commission's concern regarding the impact the proposed application of a 10% shrinkage and budget reduction will have on the Commission's ability to adequately regulate the industry and protect the public.

What Happened to the Commission's Cash Balance

The Commission understands and appreciates the difficult position the Legislature is facing this year due to the continuing tough economy and the elimination of federal stimulus monies for State General Fund programs. Even though the Commission is 100% fee funded, its budget has likewise suffered significantly from the sharp decline in the real estate market. The Commission has been hit by the "perfect storm" caused by the following: (1) since FY 2005, over $700,000 has been swept from the Commission's fee fund; (2) licensee counts have decreased by approximately 3,000 since FY 2007; and (3) the number of requests for hearings and severity of the cases have more than doubled since the housing market began to decline. The proposed budget only hampers the Commission's ability to realign staffing to address the over one-year backlog of disciplinary orders waiting to be drafted and hearing requests waiting to go through the hearing process. Possibly most important to the Committee members, the proposed shrinkage and budget reduction will not benefit the State General Fund budget because the Commission is not a SGF agency and the 10% shrinkage will remain in the Commission's fee fund.

The Budget Realities

The Commission respectfully takes exception to the statement in this year's Governor's Budget Report that states that the Commission needs to be more aware of its fee fund balance and reduce its expenses to a level that the receipts support operations without depleting the agency's fee fund balance. In FY 2005, $508,438 was swept from the Commission's fee fund. In FY 2009, another $195,671 of Kansas Savings Incentive Plan (KSIP) monies that the Commission had saved for updating its licensure system was swept from the fee fund and transferred to the State General Fund when the KSIP program was terminated. Ironically, the Division of Budget had also recommended that another $550,000 be swept from a combination of the Commission's recovery fund and fee fund in FY 2009, but fortunately that measure was defeated late in the Session.

In addition to the fee fund sweeps, the Commission transfers 20% of fees received from licensees up to a maximum of $200,000 per year for "indirect costs" for accounting, legal and other centralized services. However, the Commission is also direct billed for those services by the Department of Administration. In FY 2009, the direct bills received from the Department of

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Administration exceeded $50,000. Consequently, in FY 2009, approximately $450,000 was transferred to the State General Fund.

In many agencies when licensee counts are drastically reduced, the workload of staff is also reduced and a shrinkage rate would make sense. However, the opposite is true in the Commission's case. The number and severity of the complaints increase and the licensees are less receptive of disciplinary action. In addition, because a tough economy can bring out the worst in people, there are more long-term suspensions and revocations in a tough economy. When the real estate market steadily declines like has occurred over the past three years, licensees often times will not accept disciplinary action taken against their license and have a tendency to request a hearing regardless of whether a fine is imposed or a more severe penalty is imposed. The strain of the increased workload on the staff is enormous and this situation has created a substantial backlog of agency orders waiting to be drafted and hearings to be held. However, due to the complexity of the workload involved and the skills needed to address the backlog, there are two positions in Enforcement—a Special Investigator I and an Office Assistant—which are purposely kept vacant and the funding otherwise used to hire or contract with temporary paralegals because these two FTE positions are not properly classified to handle the complexity of the work that is required. However, an attorney is needed to truly address the backlog that exists and the backlog will continue to grow until the proper staffing mix is obtained. The backlog for complaint orders that do not involve a danger to the public currently exceeds one year and the backlog of audit orders is currently around 8-9 months. It takes on average 15 months to have the hearing process initiated once a hearing is requested due to the number of hearing requests in the pipeline. Application of a shrinkage rate and reduction of the budget will only cause the backlog to increase. This hampers the Commission's ability to fulfill its mission to protect the public and it's not fair to licensees who find they must defend themselves after a substantial period of time has passed after the complaint was received.

The Commission is not going to spend money it doesn't have. It has not spent money foolishly. If the Commission's proposals for revenue enhancements are not approved, the Commission will out of necessity have to adjust what services it provides and possibly what bills it pays. If revenue enhancements are approved, the Commission should then be allowed to manage its staffing resources in the manner it deems appropriate to best address the backlogs because the Commission's expenditures have no impact on the SGF.

The Commission's Proposed Solution for FY 2011—FY 2013

Because the Commission's fee fund balance would be depleted by FY 2013 unless revenue was enhanced, a carefully crafted proposed budget consisting of a fund transfer, revenue enhancement and expenditure enhancement for staffing reorganization was proposed by the Commission for FY 2011—FY 2013 to provide increased revenues and provide the Commission with the tools to manage its backlog.

For FY 2011, the Commission proposed **transferring $200,000 from the Commission's recovery fund (claims fund) to the fee fund.** The recovery fund was initially funded by a transfer from the fee fund derived from fees paid by licensees. By statute, licensees are assessed only if the recovery fund balance falls below $100,000. Approximately $250,000 would remain in the recovery fund after the proposed transfer. The recovery fund balance appears to be sufficient because claims are statutorily limited to a maximum payout of $15,000 per claim.

The Commission proposed a revenue enhancement by **requesting an increase of the statutory cap on original and renewal fees for salespersons and brokers**. Renewal fees have remained at the statutory cap since 1998 and the statutory cap has not been raised since

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1993. The Commission proposed requesting a statutory increase on original and renewal license fees for brokers from $150 to $250 and would set the broker license fees by regulation at $175. The Commission proposed requesting a statutory increase on original and renewal license fees for salespersons from $100 to $150 and would set the salesperson license fees by regulation at $120.

The Executive Director has been trying to handle the work of both the director of the agency and an attorney for almost three years. To address the backlog properly, a staff attorney and paralegal are necessary, but the funding available from the two vacant Enforcement FTEs that have purposely not been filled because they are not classified properly to handle the complexity of the work is not sufficient to cover the salaries of an attorney and paralegal. The attorney would draft orders and function as disciplinary counsel for the Commission. The paralegal would could draft simple orders, draft correspondence and assist with litigation. The Commission proposed **upgrading a vacant Special Investigator I position to an unclassified Attorney position**. The Commission proposed **upgrading a vacant Administrative Assistant position to a classified Legal Assistant position**. The Commission believes the proposed reorganization of Enforcement staff to include an Attorney and a Legal Assistant would accomplish three purposes: (1) reduce the backlog of agency orders; (2) ultimately reduce attorney fees; and (3) enable the Executive Director to balance staff's workload.

Summary of the Commission's Request for FY 2011

Despite the Commission's request for adequate funding to address the problem of the growing backlog, the proposed budget recommends a 10% shrinkage rate (and in FY 2012 eliminates 2 FTEs). The purpose of the shrinkage is to reduce expenditures and increase the fee fund balance. The Commission is capable of managing its expenditures without the necessity of a shrinkage and budget reduction. The Division of Budget recommendation deletes the funding the Commission is using from the two improperly classified Enforcement FTEs to hire or contract for temporary workers to assist with the backlog. This will only make a very bad situation worse. The Division of Budget's recommendation will require the Commission to either determine it can no longer enforce most types of violations—a message the Commission does not want to send to licensees when the Commission's purpose is to protect the public—or the Commission will soon be forced to determine its priorities and will accordingly reexamine what bills it can and cannot afford to pay. Either scenario is not the best choice when the Commission has offered other viable alternatives—and the Commission's budget does not impact the SGF budget.

The Commission believes that auditing brokerages, investigating complaints, issuing reasonably timely orders, and being able to take necessary disciplinary action are core services of the agency that are necessary to help ensure the integrity of the industry and to protect the public. **The Commission respectfully requests that the following revenue and expenditure proposals be approved for FY 2011—none of which will have an impact on SGF**:

(1) transfer $200,000 from the Commission's recovery fund to the Commission's fee fund;

(2) reverse the recommendation to apply a 10% shrinkage rate and reinstate funding in the amount of $82,164; and

(3) approve an increase of the statutory cap for original and renewal broker's license fees from $150 to $250 ($175 by regulation) and an increase for original and renewal salesperson's license fees from $100 to $150 ($120 by regulation.)

Thank you for your consideration of this matter of substantial importance to the Commission.

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