

85th Legislative Session – 2010

Committee: Joint Appropriations

Wednesday, February 03, 2010

P - Present
E - Excused
A - Absent

Roll Call

P Ahlers
P Burg
E Bartling
P Dennert
P Hundstad
P Wismer
P Novstrup (Al)
P Brown
P Carson
P Deadrick
P Peters
P Wink
P Haverly
P Putnam
P Hunhoff (Jean), Chair
P Tidemann, Vice-Chair

OTHERS PRESENT: See Original Minutes

The meeting was called to order by Senator Jean Hunhoff.

February 3, 2010

South Dakota Investment Council

Mr. Matt Clark, State Investment Officer, and **Mr. Paul Livermore**, Chairman of the South Dakota Investment Council (SDIC), distributed was a handout explaining the SDIC budget. **(Document #1)**

The agency is funded primarily from the interest and investment earnings derived from the managed funds. For FY11, the Governor recommends a total budget of \$8,917,882 and 28.0 FTEs. The recommendation is an increase of \$644,845 from FY10.

Mr. Livermore stated that as of December 31, 2009, South Dakota's assets are estimated to be \$8.5 billion. The South Dakota Retirement System comprises 77% of the state's assets. The state recovered \$1 billion from the end of FY09.

Mr. Livermore briefed the members on the SDIC budget process and long-term plan. The budget is approved by the Legislative Research Council (LRC) Executive Board before presenting the budget to the Bureau of Finance and Management (BFM) and Joint Committee on Appropriations pursuant to SDCL 4-5-22. There are no general funds appropriated to the agency. Page 4 of Document #2 shows the projected budget through 2020.

In response to Representative Dennert's question, Mr. Clark stated that costs have increased because the SDIC increased that staff to have teams of two per topic. The FTEs could be cut in half, but that could damage the SDIC prospects of winning and the potential results. The increase in FTEs was phased in over time.

South Dakota internal cost for management fees are \$1.11 per \$1,000. The total cost for SDIC internal and outside manager management fees is \$3.86. South Dakota's cost is below the median of \$4.93 and the benchmark of \$6.86.

For 2008, SDIC ranked in the high value added, low cost quadrant for cost effectiveness. Research over the past 18 years has shown that there is no consistent relationship between what funds pay and the value added they achieve.

Mr. Livermore stated that additional wealth to the SDIC system can be obtained by cost advantage. Even without considering the potential for continuing superior SDIC performance, future wealth grows an extra \$1.4 billion over 30 years by keeping the SDIC costs low.

Mr. Livermore informed the members that page 8 of Document #1 is the FY09 budget summary. He noted two major areas of under-spending – personal (due to unearned incentives) and research. The committee was reminded that any unspent dollars are rolled into the next year's budget to offset the next fiscal year authorization.

Mr. Clark stated that last year was a bad year for performance and many incentives were not earned. He hopes the next fiscal year will be good in both performance and incentives earned. The Legislature gives the SDIC flexibility and the Council is careful in spending; only spend if the investment will pay dividends.

Page 10 of Document #1 is the FY11 budget request for the SDIC. The budget request is an overall increase of 9.69% from FY10. Mr. Livermore noted that the 3% across-the-board increase for all positions was removed from the original budget presented to the Executive Board in August. The 1.8% increase for all investment position was removed also. Senior investment positions, including the Investment Officer, will receive no base salary increase.

Mr. Livermore said that the investment performance incentives encourage outperformance and are only paid if earned by superior performance. The unearned funds remain part of the cash balance and are used to offset the next year's budget. Typically, the average earned incentive is 40% to 60% of the maximum.

The SDIC employee benefits were increased according to the calculations provided by the Bureau of Finance and Management.

Representative Wink asked about performance benchmarks. Mr. Livermore stated that there are three benchmarks – capital market, Mellon, and state benchmarks.

The FY11 recommended budget includes an increase of \$24,634 for contractual services in the operating budget. The major purchases in capital assets will include computer upgrades, replacement chairs, and Chartered Financial Analyst books.

Mr. Livermore stated that in FY03, the SDIC requested a \$150,000 line item to be added to the budget for consulting services. A portion of the funds were used for the Mr. Meyers consultant contract, which is being reduced to \$50,000 (\$40,000 compensation plus a cap of \$10,000 for expenses).

Mr. Livermore stated that page 13 of Document #1 is a detailed overview of the FY11 budget request. After adjustment, the request is a 7.79% increase overall.

Mr. Clark said that the return this fiscal year is good in comparison to the benchmarks. If the fiscal year ended today, the returns would be the best for the past 20 years for relative performance. The performance came from SDIC purchasing assets when items were cheap. The Council lost money during this time, but will rebound when the economy turns around.

For FY09, the total South Dakota Retirement System (SDRS) earned -\$1.478 billion. SDRS earned \$801 million over the last five years and \$1.928 billion over the last 10 years.

Health Care Trust Fund. As of December 31, 2009, the principal value was \$85,631,024, the amount adjusted for inflation was \$102,011,400, and the fair market value was \$94,480,000. The fund is \$8.8 million behind principal. Mr. Clark noted that the state will receive a 4% payout from the trust fund – an estimated distribution for F11 will be \$3.8 million.

Education Enhancement Trust Fund. As of December 31, 2009, the principal value was \$329,329,930, the amount adjusted for inflation was \$329,909,459, and the fair market value was \$346,200,000. The fund is \$16.8 million behind principal. Mr. Clark stated that there will be a 4% payout totaling \$14.8 million for FY11.

Dakota Cement Trust Fund. As of December 31, 2009, the principal value was \$238,000,000, the amount adjusted for inflation was \$290,487,885, and the fair market value was \$223,800,000. The state will receive the \$12 million payout required by the constitution.

South Dakota Retirement System

Mr. Rob Wylie, Executive Director/Administrator for the South Dakota Retirement System (SDRS); and **Justice Steve Zinter**, Vice Chair and Judicial Member of the Board of Trustees; introduced board members present at the meeting – **Mr. Darwin Longieliere**, **Ms. Laurie Gustafson**, **Mr. Eric Stroeder**, and **Mr. James Hansen**.

Distributed to the committee were two documents – summary of the priorities and budget request (**Document #2**) and a map of SDRS membership and benefits payable by county (**Document #3**).

Justice Zinter stated that the South Dakota Retirement System (SDRS) covers most public employees in the state – counties, cities, state, and districts. Over 460 employers participate in the system with over 70,000 members. The SDRS approaches its job responsibility with two prongs – fiduciary responsibility to maintain the financial stability and provide financial planning and services to members.

Mr. Wylie explained the two priorities of the SDRS:

- To provide lifetime income replacement, including primary Social Security and additional personal retirement savings, to meet the basic retirement income needs of at least 85% of a career member's final pay; and
- To provide lifetime income replacement of at least 55% of a career member's final pay from SDRS benefits.

The prior economic turmoil effected SDRS. Although a substantial reserve was created, bills were submitted this legislative session to adjust a couple programs that are causing unanticipated outflow of money.

The South Dakota Retirement System (SDRS) is funded from the SDRS Trust Fund Pool. The SDRS is allowed to expend up to 3% of the annual contributions for administrative expenses pursuant to SDCL 3-12-61. For FY11, the Governor recommends a total budget of \$3,735,876, which is an increase of \$35,622 in other fund expenditure authority from FY10, and 33.0 FTEs.

Mr. Wylie stated that regular mail is still the best method to communicate with the members. The Governor recommends an increase of \$10,000 for postage expenses. This budget has been increased in each of the last four years, but the actual expenditures continue to be higher than budget.

Rules hearings, notifications, and job announcements need to be posted in legal newspapers. The Governor recommends a budgetary increase of \$7,000 for advertising costs associated with job vacancy announcements and legal notices for rules hearings.

Mr. Wylie informed the committee that the Governor recommends an increase of \$2,800 for professional auditing services. In FY06, SDRS had an auditing budget of \$47,500. Since that time, increases of \$75,000 in FY07, \$6,020 in FY08, and \$2,000 in FY10 have been approved. The total amount approved for audit services totals \$130,520. The requested total need for auditing services in FY11 is \$107,500.

Senator Brown asked about the \$130,520 previously approved for auditing services. After discussion, Mr. Wylie stated that SDRS will provide detailed information to the committee.

Senator Ahlers asked for a budget total for postage and advertising. Mr. Wylie stated that the postage budget is \$185,000 and the advertising budget is \$61,000 (which includes dues, subscriptions, and meeting registrations).

Senator Ahlers requested a breakdown of the advertising budget. Mr. Wylie stated that advertising was budgeted at \$2,400 last year.

In response to a question posed by Senator Ahlers, Mr. Wylie stated that SDRS has an active website and all newsletters are posted. The SDRS interacts with members via the website, emails, regular mail, and telephone. The younger members are more willing to communicate on the internet. However, the 20,000 current retirees and 15,000 members nearing retirement are not as heavily connected to the internet and the only way to communicate is to send hardcopies.

Representative Wismer asked how South Dakota ranks nationally in the percentage of salary the employer contributes to the retirement plan. Mr. Wylie stated that the employer contribution matches the employee contribution, which is a-typical. The economic impact in the community is 12.5% compared to the national average of 6.5%.. Compared to other plans, SDRS ranks first in the nation.

Mr. Wylie commented on other SDRS accomplishments. Some include:

- In 2008, SDRS was recognized by the Pew Center as one of the best-funded and most stable public employee retirement systems in the nation;
- SDRS has been recognized by the CEM Benchmarking annual study as the lowest cost provider for small public employee retirement systems;

- An additional study by the USD Business Research Bureau confirms the results of the NIRS study which estimates that SDRS benefits have approximately \$336 million impact on South Dakota's economy and supports over 2,500 jobs in the state;
- SDRS was awarded the Government Finance Officer Association Certificate of Achievement for Excellence in Financial Reporting for the 14th straight year; and
- SDRS also received the Pension Coordinating Council Public Pension Standards award for the 5th straight year.

Legislative Department

The legislative budget is funded primarily from the State General Fund; only about 0.5% of the recommended budget comes from other funds. For FY11, the legislative agencies request, as approved by the LRC Executive Board, \$7,813,140 and 67.3 FTEs. The Governor recommends \$7,687,736 and 67.3 FTEs. This is an increase of \$66,862 from FY10, but a decrease of \$125,404 in the legislature's requested budget

Legislative Research Council

Mr. James Fry, Executive Director for the Legislative Research Council (LRC), distributed to the committee a handout entitled "The Priorities of the Legislative Research Council". **(Document #4)**

Mr. Fry told the committee that the FY11 budget was developed this past summer and presented to the Executive Board for review. The result was give to the Office of the Governor for recommendation.

For FY11, the LRC requested \$4,866,139 and 31.3 FTEs. The Governor recommended \$4,795,068 and 31.3 FTEs. This is increase of \$26,692 (0.6%) from FY10.

Mr. Fry said that the FY09 budget was reduced by \$160,000. The LRC managed expenses within the appropriation and reverted \$126,000 at the end of FY09.

The FY11 recommendation by the Governor was \$97,000 less than the recommendation by the Executive Board. The recommendation includes costs that the LRC was experiencing prior including pages and intern payments, social security payments, organization dues, and registration fees.

Representative Tidemann asked about the LRC having a one-line item budget. Mr. Fry responded that the LRC budget is submitted and seen in the general bill as a one-line item. The budget is loaded onto the rolling budget system and is allocated to certain items. The Governor's recommendation overfunds the LRC in the capital assets because it reflects the LRC's decision to purchase Office 2007 versus renting the system. The LRC will no longer incur a further cost for Office 2007 until a later upgrade is needed. The other miscalculation occurred in contractual

services, however, if the LRC is able to use a rolling budget as the Executive Board approved, the LRC should be fine.

Representative Tidemann asked about the leasing of laptops. Mr. Fry stated that he doesn't expect the lease payment for next fiscal year to exceed the payment for the current fiscal year. The LRC has the guarantee cost and the replacement cost if a laptop fails.

Senator Haverly asked about the additional cost to insure the laptops. Mr. Fry responded that the total cost for the insurance increases the lease payment by \$200 per laptop or a total of \$2,100 per laptop. The insurance covers the replacement of screens, hard drives, motherboards, etc. with a five day turn-around guarantee. The laptops receive tremendous use and the LRC has utilized the guarantee.

Representative Burg asked about the cost for redistricting. Mr. Fry replied that the LRC will have a substantial cost for redistricting in FY11. The cost of the redistricting committee will be borne as part of the interim committees and that cost is included in the budget. The additional cost of maps and other items are hoped to be shared with the state because the LRC will be building a system on top of the current GYS system.

Senator Ahlers asked if it would be better to purchase computers with extended warranties versus lease. Mr. Fry responded that the extended use guarantee makes the most financial sense for the LRC. The laptops are placed in surplus property after use, and no one wants them. The LRC retains the right to purchase 22 laptops that are used for the interns.

Mr. Fry stated that the LRC did not include in the budget request the increase for the employer portion of the state health insurance plan and the increase in space billing. The total increased need for FY11 is about \$96,000.

Mr. Fry agreed that it may be premature to increase the budget due to pending bills this legislative session that may change the LRC budget.

Department of Legislative Audit

Mr. Marty Guindon, State Auditor, distributed to the committee a handout listing the department's FY11 budget request. (**Document #5**) He stated that the Department of Legislative Audit (DLA) is entirely funded by the State's General Fund. The DLA returned approximately \$1.26 million to the general fund through billings to other funds of the state and local governments

For FY11, the Governor recommends a total appropriation of \$2,892,668 from the State General Fund. This is an increase of \$40,170 (1.4%) from FY10. The DLA requested \$2,947,001 from the State General Fund and 36.0 FTEs for FY11.

The Governor's recommended budget includes an increase of \$40,170 in personal services. These funds are needed to maintain the current compensation levels for the Department's employees and includes the amount (\$12,669) added by the Governor for the employer portion of the state health insurance increase.

Mr. Guindon stated that the Governor removed \$34,410 (\$30,257 salaries and \$4,153 benefits) that was requested for movement to job-worth since the Governor's recommended budget included no salary policy.

The Governor also removed \$32,592 that was requested by DLA to purchase new notebook computers for the audit staff. The Governor believed that Legislative Audit's reversion history suggested that funds would be available to purchase the notebooks without the requested increase for FY11. Based on current DLA projections of FY10 expenditures, it may be possible to purchase the laptops using the available funds.

Senator Ahlers asked about excess funds. Mr. Guindon stated that any unused funds are reverted. The recommendation from the Governor would allow the DLA to spend the same amount appropriated just in different fiscal years. Due to moving funds between fiscal years, this purchase would require Legislative approval.

Mr. Guindon informed the committee that since the submittal of the FY 11 budget request, the federal government has made changes to the Single Audit report. The federal government requires this report by March 31st. However, due to increases in audit time required to comply with additional standards for conducting Single Audits issued by both the federal government and the American Institute of Certified Public Accountant's, the DLA has not issued the Single Audit by the deadline for the last three fiscal years

The federal government has recently stopped authorizing extensions of time for the submission of Single Audit reports and the DLA believes the federal government does not intend to authorize extensions going forward. To address the issue, the DLA requests the addition of two audit staff FTEs to meet the deadline for the Single Report and additional work for the stimulus money.

Mr. Guindon stated that one additional benefit of adding two auditors would be in dealing with turnover. The timeframes for issuing the Single Audit assume that the DLA are fully staffed for the audit cycle. Although the DLA is authorized 36 FTE, the department averaged only 33.5 actual FTE for the past six years due to turnover. Increasing the FTE to 38 would allow the DLA to achieve actual FTE closer to the 36 that are currently authorized.

Mr. Guindon said that the cost of adding two additional auditors for FY11 would be \$71,616 in salaries and \$22,000 in benefits for a total of \$93,616.

Representative Putnam asked about the penalty for not complying with the federal deadline. Mr. Guindon stated that the DLA has not been told of the state penalties for noncompliance.

After lengthy committee discussion, Mr. Guindon stated the DLA reverted \$114,113 in personal services this past year because there were open positions in the department. However, the DLA has been at full capacity since May 2009 and will use all funds appropriated in personal services for FY10. An additional \$93,616 would need to be appropriated to fund the two new FTEs.

Representative Tidemann asked about contracting for additional duty pay. Mr. Guindon responded that the DLA is able to pay people for additional hours worked on a straight time basis and not traditional overtime. This is voluntary program.

Mr. Guindon explained the DLA top priorities as outlined on page 3 of Document #5.

In response to Senator Hunhoff's question, Mr. Guindon stated that the two additional FTEs will not help with the FY09 Single Audit. He hopes to have the FTEs start at the beginning of the FY11 (July 1, 2010). The new FTEs would help generate the FY10 Single Audit, which DLA estimates to have completed in April (close to the deadline).

Senator Hunhoff asked if the FTEs will be eliminated after the stimulus funds are gone. Mr. Guindon stated that the FTEs will not be eliminated initially, but the DLA will review the positions and report if the two are needed on an ongoing basis after FY12.

Department of Agriculture

William Even, Department Secretary and Chris Peterson, Finance Officer, appeared before the Committee to present the department's FY11 recommended budget. Documents 6-12 were distributed.

Secretary Even told the Committee the department's priorities for the coming year are:

- Management of invasive species inside the state of South Dakota.
- Maintaining readiness whether fire, flood or blizzard.
- Continued success and off-season diversification at the State Fair Park.
- Being effective in influencing policy decisions for the benefit of agriculture.
- Demonstrating leadership through fact based information about the important of agriculture to our economy and the hands-on working relationships with producers as they work to expand their operations.

The Committee was updated on the following department activities:

- Over 1 million pesticide containers have been recycled as part of the Pesticide Container Recycling Program first established in 1992.

- Favorable conditions for grasshopper hatching in 2010 could create an unprecedented demand for suppression of this pest at a cost of \$5 to \$6 per acre.
- The Emerald Ash Borer is expected to significantly impact the environment in South Dakota. The department estimates cities and towns have more than 274,000 ash trees and expect a mortality rate of 99%. The current cost of tree removal is \$272/tree; however this cost could rise significantly to as much as \$600/tree. The total cost for removal and replacement could reach \$200 million.
- More than \$1.6 million has been spent on Mountain Pine Beetle suppression in Custer State Park and those efforts have been successful. The Department of Agriculture spent \$503,632, the Department of Game, Fish & Parks spent \$465,161, and federal funds totaled \$715,295. Secretary Even said the money was spent primarily on labor involved in tree thinning or cutting and biological control.
- Wildland Fire Suppression Division (WFS) closed the fire equipment shop in Springfield, resulting in a savings of 1.3 FTE and \$60,000 that went back to the general fund. The WFS trained 861 firefighters in FY09 and conducted 69 training courses. Fire crews are deployed on thinning projects when not fighting fires in South Dakota or other states. The WFS received a \$252,800 grant to improve seven SEAT Bases. This will allow our Division's air assets to better deliver aerial retardant to wildfires within the state and contiguous state border areas.
- Secretary Even updated the Committee on the fire dispatch center in Rapid City (Document #7), currently located at the Rapid City Airport terminal. The lease on that facility expires in 2013. With pending changes in the dispatch center location, the department is working with BOA, BFM and the Department of Education on space in the Western Dakota Technical Institute building. This move would make it possible to have staff under one roof rather than spread all over Rapid City.
- State Fair Park – The Wisconsin 100 race, held immediately after the 2009 State Fair, was a huge success and will return in the fall of 2010. In addition, the City of Huron is exploring options for an outdoor water park. One site being considered is a 10 acre plat owned by the state and occupied by the State Fair Park.

The Department of Agriculture budget hearing will conclude on February 10, 2010.

MOTION: ADJOURN

Moved by: Haverly
 Second by: Deadrick
 Action: Prevailed by voice vote.

Barb Bjorneberg and Lisa Shafer
 Committee Secretary

Jean M. Hunhoff, Chair