GOVERNOR KATE BROWN

PERS UAL TASK FORCE

Meeting 3: Deliverables and Resource Requirements

September 8, 2017

2:00 – 5:00 pm

PSU Board Room, Academic and Student Recreation Center

1.	Call to Order	*Don*	2:00 – 2:05
2.	Report on Public Comments	*Elana*	2:05 – 2:15
3.	Review of Governor's Charge	Nik	2:15 – 2:25
4.	Introduction to Discussion	*Don*	2:25 – 2:40
5.	Options and Execution Plans	*Task Force Members*	2:40 – 4:10

Task force members will lead a discussion of the areas for which they have responsibility, identifying the options they intend to discuss with the group at the October 13 meeting, discussing the depth of analysis they expect to deliver and the resources they require to achieve those outcomes.

6.	Wrap-up / Next Steps	*Don*	4:10 – 4:25
7.	Close of Public Session	*Don*	4:25 – 4:30
8.	Executive Session	*Don*	4:30 – 5:00

PERS UAL Reduction Task Force **DRAFT FOR ILLUSTRATION ONLY**

Option Name: Enhanced Debt Collection for Cities

Public Entities Affected: Cities (maybe counties?)

Option Description: Cities have property tax and other liens that have been imposed against properties within their boundaries that are not routinely collected in a timely manner. Reasons for non-collection are varied, and include political concerns about impacts of lien collections on property owners (particularly low income) and it is time consuming and a drawn out process to actually get to foreclosure and the collection of liens. The state can help streamline the notice and collection process timeline that is embedded in state law. The state could limit use of the streamlined process to paying down the PERS UAL. This would provide cities with discretion of when to use the streamlined process (in order to make sure they don't evict 85-year old grandmothers) they could target appropriate properties for its use. To help manage and control collection costs cities could allow private companies to collect liens on their behalf, or sell off the receivable.

Another form of debt collection has to do with municipal court fines. Oregon's cities do have the ability transfer debts to the Oregon Department of Revenue for collections but the state will not utilize its full suite of collection options to collect local government debt as its own. This is a policy choice designed to protect the private debt collection interests. This limitation does not serve Oregon's cities or the criminal justice system well and should be amended to treat all government debt identically.

	Biennia			
	2017 – 19	**2019 – 2021**	**2021 – 2031**	**All Years**
Gross Capital Opp (foreclosure)	$10M - $100M	<$10M	<$10M	$30M - $100M
Cost to Implement	< $5M	-	-	< $5M
Net PERS UAL reduction	$5-$95M	-	-	$25M - $95M
Impact on other public budgets	-	-	-	-
Impact on non-public entities	-	-	-	-

	Biennia			
	2017 – 19	**2019 – 2021**	**2021 – 2031**	**All Years**
Gross Capital Opp (muni court)	$10M - $100M	$10M - $100M	$10M - $100M	$30M - $300M
Cost to Implement	< $5M	< $5M	< $5M	< $15M
Net PERS UAL reduction	$5-$95M	$5-$95M	$5-$95M	$15M - $285M

Impact on other public budgets	-	-	-	-
Impact on non-public entities	-	-	-	-

<u>Other Considerations</u>

- Foreclosing on properties has difficult optics. Local discretion is important. Portland recently completed its first foreclosure sale in almost 50 years so this is clearly an opportunity to realize one time resources where we are not currently expecting to receive anything.
- More aggressive collection of unpaid tax/fee liens will not be well received by subordinate lien holders (i.e., banks and mortgagors). Because government liens are superior to other property liens, foreclosure sales could impact them if net sale proceeds are insufficient to pay off all underlying property obligations.

PERS UAL Reduction Task Force

Policy Option: Agency Reserve Funds

Entities Impacted: Agencies that have built up ending balances or reserves, fee payers whose fees have gone into those reserves, and programs supported by the fees.

Description of Policy Option: Many state agencies, particularly those dependent on revenue from sources other than the state's General Fund, maintain reserves from the funds they collect. These funds are often statutorily dedicated for specific purposes. The size of reserves needed will vary depending on circumstances. If fees collected by regulatory agencies to support their operations come in unevenly throughout the year (due to annual license renewals, for example), reserves will vary throughout the year based on the cash flow cycle. If fee revenue is highly variable or unpredictable, reserves may be needed to smooth out inconsistencies and cushion against shortfalls. In some cases, revenue may be hard to predict and a reserve fund may build up to a higher level than anticipated or needed. Some agencies maintain formal policies governing the levels of reserves needed; others do not.

Over the past several biennia, the Legislature has "swept" funds from selected agency reserves to support the biennial budget. This practice has increased significantly over the past two biennia. Fund sweeps budgeted for the 2017-19 biennium (scheduled to occur in May 2019) total just over $111 million, as follows:

• Alternative Fuel Vehicle Revolving Fund	$3.0 million
• Insurance Fund	$33.3 million
• Department of Administrative Services Operating Fund	$18.5 million
• State Information Technology Operating Fund	$10.5 million
• Department of Justice Protection and Education Revolving Account	$46.0 million

Rather than using fund sweeps sporadically to balance the biennial budget, the state could develop consistent policies for determining the appropriate size of agency reserves, based on the nature of the program, the revenue associated with the reserve, and other relevant factors. Reserve funds in excess of the amounts needed could be transferred to reduce the UAL on an annual or biennial basis.

Financial Opportunity: $10M-$100M per year

Key Considerations:

- Legal analysis would be needed to determine whether there are constraints on redirecting amounts from these reserve funds. If so, it is unknown whether these restrictions could be addressed by setting up a side account dedicating these funds to the UAL associated with the restricted use.

- If federal funds have been paid into an account that is swept, there may be consequences if it is determined by the federal government that the sweeps were an unallowable use of federal funds.

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Policy Option: Capital Gains Taxes

Entities Impacted: Other programs receiving General Fund revenue.

Description of Policy Option: The state's receipt of tax revenue from capital gains taxes is highly variable, because it is largely dependent on the decisions of high-net-worth individuals regarding when to sell capital assets. These decisions may be based on individual circumstances and may be driven by changes (or the anticipation of changes) in the federal tax code – circumstances outside the state's control, and which cannot be predicted. The result can be large spikes in the state's receipt of capital gains taxes, particularly in times of economic growth. Biennial capital gains revenue has exceeded estimates by an average of about $350 million for the last three biennia. The previous two biennia (post-recession), capital gains revenue fell significantly short of estimates.

Due to its uncertain nature, spikes in capital gains tax revenues (i.e. revenues exceeding projections, or revenues exceeding a rolling multi-year average) could be treated as windfall income and used to reduce the UAL.

Financial Opportunity: $100M-$500M per year during times of economic growth; zero during economic downturns

Key Considerations: Capital gains taxes currently flow to the General Fund. Although they are projected separately, currently these revenues are not treated differently from other tax revenues. A mechanism for segregating excess capital gains revenues might be the sale of tax credits late in the biennium, if revenues are anticipated to exceed projections, with the sales proceeds flowing directly to the UAL. It is undetermined whether or how this would affect kicker calculations.

PERS UAL Reduction Task Force

Policy Option: Common School Fund - State Lands, Unclaimed Property

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Entities Impacted: School districts receiving funding from the Common School Fund; lessees and other users of state lands; owners of unclaimed property.

Description of Policy Option: The state owns and manages about 2.8 million acres of land for the benefit of the Common School Fund established by the Oregon Constitution. This includes about 740,000 acres of uplands (primarily rangeland and forests); 770,000 acres of sub-surface resources (minerals and energy); and about 1.3 million acres of waterways (territorial sea, tidelands, and navigable rivers).

Timber revenues, traditionally the largest revenue source for Common School Fund, have declined steadily in recent years primarily due to issues related to species protection, to the point where management costs exceeded revenue. After much discussion surrounding the largest timber asset (the Elliot State Forest), the 2017 legislature authorized $100 million in bond funding to enable the transfer of the Elliot State Forest out of the Common School Fund. This should enable the Common School Fund to obtain a higher return.

The Common School Fund currently earns less than $1 per acre, on average, for the rangelands it holds. Many of its land holdings are viewed by the Department of State Lands as having limited revenue potential and limited marketability. Total revenues from real estate management totaled $6.8 million in FY 2015. The Department has not updated its real estate asset management plan since 2012.

In addition to revenue from land management and leasing, the Common School Fund receives revenue from several other sources. The assets of persons who die intestate (without a will) "escheat" to the state and become part of the Common School Fund if no heirs are found after ten years. In addition, unclaimed funds such as bank accounts and insurance proceeds are held in trust by the state, and the earnings on these unclaimed funds become part of the Common School Fund. However, ownership of the unclaimed funds never transfers to the state – the funds can be claimed by their owners even many years later. These unclaimed funds currently total around $600 million, approximately $200 million of which has been unclaimed for more than ten years.

The Oregon Constitution provides that income from the Common School Fund must be "applied to the support of primary and secondary education as prescribed by law." The Common School Fund expects annual distributions to schools equal to 4% of assets. Since 2000, distributions have ranged from a low of $13 million in 2004 to a high of $70 million in 2017.

Options relating to the Common School Fund could include:

- Increase revenues to the Common School Fund through investment of proceeds from the Elliot State Forest and update of real estate management strategies; dedicate any increases in revenue to the UAL.

- Sell additional Common School Fund land assets and transfer proceeds to the UAL.

- Provide that unclaimed property becomes property of the state and transfers to the UAL if not claimed after ten years.

Consistent with constitutional restraints, funds transferred to the UAL would need to be applied to the support of schools, which could be accomplished through the use of side accounts for the benefit of school districts.

Financial Opportunity: $100-$500M

Key Considerations: A key question would be whether transfer of funds from the Common School Fund to the UAL would financially benefit schools. An analysis of this question would need to include a comparison of the earnings potential of the funds and implications for the short and long term.

PERS UAL Reduction Task Force

Policy Option: Estate Taxes

Entities Impacted: Other programs receiving General Fund revenue

Description of Policy Option: The state's receipt of estate tax revenue is highly variable. The state imposes taxes on only a small percentage of decedents' estates – those valued at over $1 million – and the timing is of course inherently unpredictable. Due to its uncertain nature, spikes in estate tax revenue (i.e. amounts over a multi-year median) could be treated as windfall income and used to reduce the UAL.

Financial Opportunity: $10M-$50M per year

Key Considerations: Estate tax revenues currently flow to the General Fund. It is undetermined whether or how this proposal would affect kicker calculations

PERS UAL Reduction Task Force

Policy Option: Fire Suppression Costs

Entities Impacted: Private forest land owners (both industrial and small woodland owners).

Description of Policy Option: The costs of fighting major forest fires in Oregon are shared by the state, private and public landowners, and some federal reimbursement. In high-expense years, a portion of the cost is met by commercial insurance. The formulas for cost-sharing are complex, and vary depending on whether the costs are for the pre-season deployment of resources; the initial attack; large fire costs; or insurance premiums. However, private landowners' share of costs is capped and the state General Fund picks up the excess if the caps are exceeded. A larger share of fire suppression costs could be shifted from the state General Fund to private landowners based on acreage assessments.

Financial Opportunity: $10-$50M per year; $100M-$500M over ten years

Key Considerations: Fire suppression financing is a complex structure involving many parties. More than half of the revenue in the Oregon Forest Land Protection Fund (which provides the private landowner share) is received from small woodland owners.

PERS UAL Reduction Task Force

Policy Option: Increased Lottery Revenue

Entities Impacted: Other programs receiving non-dedicated lottery funds

Description of Policy Option: The Oregon Lottery is considering several options to expand the types of gaming it offers. Some options may offer existing games on new platforms (e.g. mobile devices) while others would offer new games that could be expected to appeal to different audiences and potentially different retailers. The Lottery Commission is expected to vote on a strategic direction in October of this year, and new options would be offered as soon as fall of 2018.

Revenue from these new options could be directed toward the UAL in any of several ways:

- Reallocate revenue from specific new lottery games
- Reallocate all lottery revenue increases above a baseline (for example, all amounts over current revenue trend line, or above current revenue plus inflation, or above forecast)
- Reallocate a specific percentage of total lottery revenue

Financial Opportunity: $10-$50M per year initially, increasing over time; $100M-$1B over ten years.

Key Considerations: Under the Oregon Constitution, lottery proceeds must be used for the purposes of "creating jobs, furthering economic development, financing public education in Oregon or restoring and protecting Oregon's parks, beaches, watersheds and native fish and wildlife." Specific percentage allocations must be made to the Educational Stability Fund; to parks and fish and wildlife; and to veterans' programs. The remainder (65.5% of net lottery proceeds) may be allocated by the legislature consistent with the general constitutional categories specified above. Any transfers to the UAL would likely have to come from this remainder, and would have to be consistent with the constitutional purposes – for example, reducing the UAL for schools would likely be permissible as "financing public education."

PERS UAL Reduction Task Force

Policy Option: Interest on Agency Funds

Entities Impacted: State agencies that currently retain the interest accrued on their funds, and the programs and beneficiaries supported by the funds in those accounts.

Description of Policy Option: The State Treasury currently holds a number of specialized accounts with balances over $100 million, the interest on which accrues to those accounts. Interest on those accounts could instead be directed to the UAL.

For the fiscal year ending July 2017, accounts over $100 million that retain their own interest earnings are:

- Education Stability Fund (Average Balance of $340 M)
- Common School Fund (Average Balance of $585 M)
- Safe Drinking Water Program (Average Balance of $95 M)
- Veteran's Loan Program Non-Operating Fund (Average Balance of $5,895 M)
- DEQ State Revolving Loan Fund (Average Balance of $235 M)
- Public Employees Benefit Board Self Insurance Statewide Fund (Average Balance of $180 M)
- Public Employees Benefit Board Stabilization Fund (Average Balance of $145 M)
- ODOT Highway Fund (Average Balance of $250 M)
- Capital Construction/Improvement Fund (Average Balance of $110 M)

The first two accounts – the Educational Stability Fund (one of the state's two rainy day funds) and the Common School Fund – are addressed in separate concept papers. The total annual interest on all of the listed funds is approximately $82.5 million. The total without these two funds is approximately $72.8 million.

Financial Opportunity: $50M-$100M per year

Key Considerations:

- Legal analysis would be needed to determine whether there are constraints on redirecting the interest from these accounts. If so, it is unknown whether these restrictions could be addressed by setting up a side account dedicating these funds to the UAL associated with the restricted use.
- Redirecting the interest away from these accounts means less revenue will be available for the programs supported by the accounts.

PERS UAL Reduction Task Force

Policy Option: Portland State Office Building

Entities Impacted: Agencies which currently have offices in the Portland State Office Building (PSOB), located on Portland's east side in the Lloyd District.

Description of Policy Option: The PSOB contains 290,000 square feet of office space and 28,000 square feet of basement space. Agencies occupying space in the PSOB currently pay a "full service" rate of $17.40 per square foot per year, which includes insurance, maintenance, utilities, custodial services, etc. Since this is a State-owned property, it is exempt from property taxes.

The state could sell the PSOB and either lease back the space, relocate to another leased facility, or construct one or more new facilities in a less expensive area. Sale proceeds are estimated at about $120 million.

Office rents on Portland's close-in east side for comparable Class B office space average about $26.33/SF (triple net or modified gross rates), with total tenant costs averaging $30-$32/SF. Very little Class B office space larger than 5,000 square feet is currently available outside the Portland core. A total of five such properties were located in Beaverton and Tigard, averaging $22.74/SF triple net, or about $27/SF total cost. Three were found in Gresham and East Portland, averaging $19.83/SF triple net or modified gross, or about $24/SF total cost.

For leased space, tenant improvement costs are estimated at $80/SF, or $23 million. Moving costs (either to leased space or new construction) are estimated at $100/SF, or $29 million. With a sale/leaseback, moving and tenant improvement costs are avoided but costs to tenant agencies could be expected to increase $6-7 million/year due to property taxes and market-based lease rates.

Constructing two new 2-story facilities (east side and west side) would be estimated to cost $87 million and should result in lower operating costs. If construction and moving costs were paid out of sale proceeds, net gain would be small. Alternatively, construction could be debt financed with financing costs met through operating cost savings and adjustment of agency rates closer to market, allowing transfer of some or all of the sale proceeds to the UAL.

Financial Opportunity: $10M-$100M in three to five years.

Key Considerations: Relocating to private leased space would likely be to high-cost locations, as existing rental space of the size needed is not available in lower-cost metro locations. New construction could be in transit-friendly lower-cost location with surface parking and would allow more efficient space utilization.

PERS UAL Reduction Task Force

Policy Option: State Data Center

Entities Impacted: The majority of state agencies use the State Data Center located in Salem, and might experience service disruptions if IT services are either moved back to the originating agency or moved to a cloud service provider. If there are service disruptions to agencies, Oregonians using state services or systems could be affected as well.

Description of Policy Option: A detailed analysis would be needed to determine whether it would be cost-effective to sell the State Data Center and either move IT infrastructure to cloud/contracted services or move IT infrastructure back to the agencies. Several factors would need to be analyzed to determine the potential market value of the facility, including:

- Marketability – Private sector organizations are building data centers in eastern Oregon. Locations such as Bend, Boardman and Prineville are chosen due to the lower cost of power, favorable climate and distance from all fault zones. Due to these factors, Salem may be a less desirable location.
- Load Capacity – The current facility has the infrastructure to support 67 kW of IT load capacity. The majority of the data centers built today are built with an infrastructure to support 2000 kW of IT capacity.
- Resilience – The current facility is located in a flood plain and in the direct flight path of the Salem Airport.

Financial Opportunity: Unknown. As noted, a detailed analysis would be required to determine the potential value of the existing State Data Center and the cost and service implications of to other options.

Key Considerations:

- There are good reasons to consider cloud storage and/or contracted (hosted) data services for certain state data applications; however, there are applications that work well in a cloud environment and those that do not. Applications that do not function well in the cloud could be moved to a hosted provider, but this has historically been more expensive than hosting the same system at the State Data Center. A case-by-case determination would be needed.
- The relocation of computing and storage from the State Data Center to agencies or to cloud providers would take approximately 18-24 months, as agencies plan and coordinate the relocation of the technology and systems are decoupled from the shared environment.

PERS UAL Task Force

<u>Summary of Expected Options for Presentation – Don Blair</u>

1. SAIF
    a. Transfer a portion of existing SAIF capital surplus to PERS UAL. *Analyzed Option*
    b. Back SAIF with the full faith and credit of the State of Oregon; transfer more of existing SAIF capital surplus to PERS UAL. *Analyzed Option*
    c. Direct some or all future dividends to PERS UAL. *Analyzed Option*
    d. Monetize SAIF real estate assets (TBD). *Analyzed Option*
    e. Manage SAIF to deliver financial returns to the citizens of Oregon (PERS UAL), as well as provide quality WC coverage to workers and employers at a reasonable price. *Analyzed Option / Option to be Evaluated by Staff*
    f. Monetize "going concern" value of SAIF through sale, IPO or mutualization. *Analyzed Option / Option to be Evaluated by Staff*

2. OLCC
    a. Adopt business best practices to maximize profitability of OLCC liquor distribution operation; dedicate increased profitability to PERS UAL. Consider spin-off to a public corporation to accelerate implementation. *Analyzed Option / Option to be Evaluated by Staff*
    b. Implement selective or across the board surcharges (e.g., price increases) on liquor sales as an interim step. *Analyzed Option*
    c. Monetize OLCC real estate assets. *Analyzed Option*
    d. Increase excise taxes on beer and wine. *Analyzed Option*

3. PERS UAL Resolution Incentive Program *Framework developed by the Task Force, specific provisions to be evaluated by the Staff.*
    a. Objective: With assistance from the State, PERS employers evaluate and implement options to use their own assets and resources to

address their PERS UAL / manage the impact of potential PERS cost increases on budgets and services.

b. Potential Incentives, e.g.,
    i. Some of the capital raised through implementation of task force options is used to fund a partial State match of capital raised by local entities to reduce their PERS UAL.
    ii. State relaxes some restrictions on local taxing authority.
c. Potential Penalties
d. Other Provisions, e.g.,
    i. Cooperating PERS employers commit to undertake specific evaluations of potential sources of capital (e.g., inventory, and evaluate options to monetize, redundant assets; identify and sweep budget upsides; assess fund balances).
    ii. Cooperating PERS employers develop specific plans to manage the impact of PERS cost increases on future budgets and service delivery. State provides training and implementation assistance.
    iii. Cooperating PERS employers commit to future fiscal guardrails to ensure benefit of lower PERS costs used to protect services.