MINUTES OF THE
NEW MEXICO STATE BOARD OF FINANCE

REGULAR MEETING
Santa Fe, New Mexico

March 20, 2012

A Regular Meeting of the New Mexico State Board of Finance was called to order on this date at 9:15 a.m. in the Governor’s Cabinet Room, Fourth Floor, State Capitol Building, Santa Fe, New Mexico.

1. **ROLL CALL: QUORUM NOT PRESENT**

**Members Present:**
The Hon. Susana Martinez, President [arriving 9:45 a.m.]
Mr. Michael Brasher, Public Member
Mr. John Gasparich, Public Member, Secretary
Mr. Sam Spencer, Public Member

**Members Excused:**
The Hon. John Sanchez, Lt. Governor
The Hon. James B. Lewis, State Treasurer
Mr. Robert J. Aragon, Public Member

**Legal Counsel Present:**
Mr. Zack Shandler, Attorney General’s Office

**Staff Present:**
Dr. Thomas E. Clifford, Secretary, Department of Finance & Administration
Ms. Stephanie Schardin Clarke, Director, State Board of Finance

**Others Present:**
[See sign-in sheets.]

[Because a quorum was not immediately present, the Board proceeded with non-action items.]
STATE TREASURER'S OFFICE  
Presenters: James B. Lewis, State Treasurer; Linda Montoya Roseborough, Chief  
Investment Officer; T. Spencer Wright, Lead Portfolio Manager  

Ms. Roseborough presented the January Investment Review, with the following highlights:  

-- January saw continued stability in the domestic markets, despite volatility overseas  
with the evolving European debt situation.  

-- Equity prices continued to solidify as economic numbers confirmed increased stability.  

-- January was the strongest opening month for US stocks in 15 years, according to The  
Wall Street Journal.  

-- Economic indicators have continued to show economic strength, although  
unemployment continues to be a drain on the economy.  

-- Europe continues to grapple with the issues in Greece, although European Central Bank  
activity has given some stability to the overall financial system.  

-- Oil prices have remained high, acting as a further drag on the domestic economy.  

-- In the domestic fixed-income markets, US Treasury yields moved sharply lower in  
January.  

-- Short-term LIBOR rates have continued their retreat as a result of the increased funding  
commitments of European central banks.  

-- The Fed publicly stated its intent to keep domestic short-term rates extremely low until  
2014.  

-- Over its maturity sector, STO has seen continued improvement in rate levels, with  
significant declines in the 3-5 year area.  

-- The portfolios have reported gains on a mark-to-market basis. Lower rates and a steep  
yield curve have contributed to all of the portfolios. The general fund has reported gains of $9.1  
million and the Bond Proceeds Fund at $6.2 million, while returns remain flat for the LGIP and  
Severance Tax Bonding Fund.  

-- STO has actively managed the ratio between liquidity and core portfolios within the  
general fund, aggressively moving assets into the longer term core portfolio. This has required  
additional focus on cash production to protect fund balances. The portfolios have been able to
maintain their purchase yields despite the overall lower rates seen in the domestic fixed income markets.

-- Investment earnings for the month of January are: General Funds, $1.07 million; Bond Proceeds Funds, $932,000; LGIP, $229,000; and Severance Tax Bonding Fund, $29,000.

-- During December, STO maintained average daily collected balances at the fiscal agent bank of approximately $122 million. This earned a “soft dollar” credit against processing fees assessed by the bank.

-- Domestic stock and bond markets began 2012 with renewed optimism as investors remained focused on a potential resolution to the Greek debt crisis. The general consensus is that the debt swap will go forward in the next few weeks, allowing Greece to restructure its liability portfolio. Certainly other countries are eyeing the Greek results to see if there is a potential application to their own struggles.

-- The Fed has stated its intent to potentially add additional support to the mortgage market by purchasing mortgage-backed securities if needed. This action may help the struggling real estate market.

-- Oil prices have remained stubbornly high. At this time, gas prices are expected to remain high as well. This could prove problematic in the reelection of the president.

-- STO continues to refine its cash flow modeling, allowing the portfolios to be positioned on the longer end of the maturity spectrum. STO has seen significant benefits in utilizing this strategy despite the overall lower rate environment.

-- STO also continues to look at short-term alternatives to the repurchase agreement marketplace, where appropriate. During the past month, STO has been able to move some assets into higher yielding options that provide for full collateralization and increased yield.

-- STO also looks closely at minimizing the amount held in its liquidity balances, as the differential between overnight rates and core earnings is so significant. STO continues to identify potential shifts from the liquidity portion of the general fund to the core portion, maintaining sufficient liquidity to meet the state’s cash flow needs.

GENERAL SERVICES DEPARTMENT
Presenter: Charles Gara, Director, Property Control Division


Mr. Gara reported financials for the Capitol Buildings Repair Fund, with a beginning balance as of January 1 of $17,257,841. After cash receipts and cash disbursements, the ending balance
at January 31 was $16,971,512. Subtracting encumbrances, the uncommitted cash balance as of January 31 was $1,413,514. Year to date revenues total $3,253,084

Mr. Gara stated that, of the 185 projects listed in the January Project Nothing Drops report, 95 percent are on budget and on schedule. He said the total budget for these projects exceeds $263 million, ranging from $941 to move a handicap access button to $93 million for the Tri Lab Building in Albuquerque.

Mr. Gara said there were no emergency declarations in January.

11. Property Control Division – Notification of Contract with GranCor Enterprises, Inc. for Demolition of the Old Sandia Building and the White House Building ($440,559)

Mr. Gara reported that the Property Control Division has entered into a contract with GranCor Enterprises, Inc., of Albuquerque, for the demolition of the Old Sandia Building and the White House Building at the Youth Diagnostic and Development Center in Albuquerque. Without the demolition, these buildings would continue to deteriorate and pose a safety risk for anyone in and around them.

Mr. Gara introduced Leasing Bureau Manager Tom Gurule.

EMERGENCY FUND BALANCES
Presenter: Stephanie Schardin Clarke, Director

17. Emergency Balances – March 2012

<table>
<thead>
<tr>
<th>Fund</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating Reserve Fund</td>
<td>$1,191,814.39</td>
</tr>
<tr>
<td>Emergency Water Fund</td>
<td>$118,400.00</td>
</tr>
</tbody>
</table>

Ms. Clarke reported these balances.

EMERGENCY FUNDING REQUEST

18. WITHDRAWN.
TRAINING
Presenters: Janet Fennessy, JPMorgan Executive Director/Relationship Manager;
Richard Hartzell, JPMorgan Vice President/Relationship Manager

19. Custody Banking Training Presentation

[Governor Martinez and Secretary Clifford joined the proceedings during the course of this presentation.]

Ms. Fennessy discussed the role of a custody bank and made a presentation, with the following highlights:

-- JPMorgan is one of the leading global custodians, moving $100 billion of cash daily and 1.4 million domestic trades.

-- JPMorgan is leading custodian to the world’s central banks, supranationals, Government Sponsored Enterprises and official institutions, with over 50 such relationships.

-- JPMorgan operates in 102 countries with a high degree of local market influence.

-- The company employs over 972 seasoned service professionals located in 24 regional service centers worldwide.

-- Global reach incorporates U.S. local operations hub in Dallas, global hubs in Bournemouth, Sydney and Mumbai.

-- Entrusted with US $16.9 trillion in client assets under custody, US $5.4 trillion of which are invested outside the U.S.

-- 2,734 institutional clients.

-- JPMorgan has a team dedicated to the Board of Finance. The bulk of the team is located in Dallas. Service calls are weekly and biweekly. On-site visits are made quarterly.

-- JPMorgan has worked with all of the investment managers in New Mexico’s state agencies (with the exception of STO), primarily with the global markets, so that they can now reconcile down to the penny.

-- JPMorgan sends people on site to provide training on its access system, but will also provide training online or over the phone.

-- JPMorgan also issues news flashes across all global markets.

-- JPMorgan has held two economic forums, one in Albuquerque and the second in Santa Fe.
Mr. Hartzell provided an example of a typical trade in which the State of New Mexico would be the buyer of a security.

-- An investment manager or asset manager initiates the buy transaction, which goes to a broker they have selected.

-- The broker will initiate the order on behalf of their client and passes it on to a clearing broker or clearer broker. The broker and clearing broker may be in the same firm or may be in different firms. The clearing broker, however, must have a seat on the exchange on which the security is traded.

-- The clearing broker becomes the backbone of the trade, making sure all documentation is in place, and that the trade is ultimately settled (both parties end up exactly with that they have bargained for).

-- The depository is the agency that will move the cash or asset from the buyer’s account to the seller’s account. The clearing broker makes sure this occurs appropriately.

-- The subcustodian (JPMorgan) records the buying of the asset and the sending out of cash.

A trade can “break,” or have a problem, in one of two essential ways:

-- The seller’s information on the trade doesn’t agree with the buyer’s information – they don’t “match.” The trade has to go back and be remediated with all of the parties so the trade can settle.

-- The seller is unable to deliver the agreed-upon security because the security is encumbered for one reason for another. The trade does not settle.

[The Board had achieved quorum at approximately 9:45 with the arrival of Governor Martinez. The Board proceeded with action items.]

2. APPROVAL OF AGENDA

NEXT REGULAR MEETING APRIL 17, 2012

Ms. Clarke asked Board members to prioritize certain time-sensitive action items because quorum time during this meeting would be limited; and if necessary, to postpone Items 8 and 9. She also requested that Item 20 be listed as an action item rather than an informational item.

Mr. Brasher moved for approval of the Agenda, as amended. Mr. Spencer seconded the motion, which passed 4-0 by voice vote.

New Mexico State Board of Finance: March 20, 2012
3. **APPROVAL OF MINUTES:** February 21, 2012 (Regular Meeting)

Mr. Brasher moved approval of the February 21, 2012 Minutes, as submitted. Mr. Spencer seconded the motion, which passed 4-0 by voice vote.

**STATE TREASURER’S OFFICE** (Cont’d)
Presenters: James B. Lewis, State Treasurer; Linda Montoya Roseborough, Chief Investment Officer; T. Spencer Wright, Lead Portfolio Manager

5. **Approval of State Treasurer’s Appointment of State Treasurer’s Investment Committee Private Sector Member**

Ms. Roseborough stated that Treasurer Lewis is requesting approval of his reappointment of Paul Boushelle for a two-year position on the State Treasurer’s Investment Committee (STIC) beginning in March 2012.

Mr. Spencer said he has known Mr. Boushelle for a number of years, and has a great deal of respect for his knowledge in the banking industry and in investments.

Mr. Spencer moved for approval. Governor Martinez seconded the motion, which passed 4-0 by voice vote.

6. **WITHDRAWN.**

7. **WITHDRAWN.**

**PROPERTY DISPOSITION**

12. **WITHDRAWN.**

Presenter: Anna Martinez, Deputy Director, NM Corrections Industries Division

13. **Corrections Department, Corrections Industries Division – Requests Approval of Lease of Farming Property at Central New Mexico Correctional Facility to Jones Dairy, Inc. ($185,000 annual)**

Ms. Martinez stated that Director David Bourger could not be present at today’s meeting because of a previous engagement.

Ms. Martinez stated that the Corrections Industries Division and Ron Jones Dairy, Inc. are asking approval to enter into a six-year lease, with an option to extend for two years, beginning on April 1, 2012. She said the contract would eventually expire on March 30, 2020. She stated that the lease would allow Ron Jones Dairy to farm the property, while the inmates would plant, irrigate and harvest crops, including corn, alfalfa, barley and winter wheat.
Ms. Martinez stated that Corrections Industries would be able to generate a positive cash flow while accomplishing the mission and goals of the Corrections Industries Division and the New Mexico Corrections Department. She said the lessee was selected after Corrections Industries issued an RFP through the General Services Department.

Responding to Governor Martinez, Ms. Martinez stated that Ron Jones Dairy would pay Corrections Industries to lease the property. She said the dairy would also pay for the use of inmate labor and the farm liaison’s salary and benefits, and the dairy would then be entitled to use the crops for their own use. She said a feedlot and corral is attached to the property, and in the past lessees have used it as their own feedlot, with the crops sold to area farmers.

Responding to Secretary Gasparich, Ms. Martinez said policy calls for the Corrections Department to pay the inmates directly. She said Ron Jones Dairy then reimburses those expenditures.

Ms. Martinez said this is the first year that Ron Jones Dairy will have this contract, which has been held since 1991 by Mike Mechenbier of GM Land & Cattle Company (former Four Daughters Land & Cattle Company). She stated that, while statute allows Corrections Industries to enter into contracts like this without issuing an RFP, the decision was made to start the RFP process to allow everyone an opportunity to bid. She said the exemption to the Procurement Code can be found in Section 13-1-98 NMSA.

Ms. Martinez stated that Mike Mechenbier’s lease terms were for $142,000 per year, with a 2% increase per year; in addition, he paid for the inmates that worked on the farm and at the feedlot, while Corrections Industries paid the inmates for the irrigation process. In the new lease, Ron Jones Dairy will pay $185,000 for the property lease, with a 2% increase each year, and will pay all of the inmates in both the feedlot and farming properties, as well as reimburse Corrections Industries for the farm liaison to a maximum of $65,000.

Board legal counsel Zack Shandler stated that Property Control Division, as the owners, have raised some issues with the lease in the last day or two that need to be reconciled.

Mr. Shandler asked that any Board approval of this item be continued upon (1) Board of Finance Director receipt, with review of counsel, of a final signed lease that incorporates changes required by Property Control Division; and (2) Board of Finance Director receipt of a signed resolution of the governing body (Corrections Industries Commission) evidencing approval of the lease.

Ms. Clarke said the Commission approved the resolution on March 15, but the signed copy has not yet been received in her office.

Dr. Clifford asked Property Control Division Director Charles Gara to discuss the concerns that resulted in the requested changes.
Mr. Gara responded that the questions raised by Property Control were technical and relatively minor.

Ms. Clarke added that the changes requested by PCD would only strengthen the state’s position.

Ms. Martinez stated that the contingencies were acceptable and she felt there would be no problem with the lessee accepting them.

**Governor Martinez moved for approval, with the contingencies. Mr. Brasher seconded the motion, which passed 4-0 by voice vote.**

**HIGHER EDUCATION DEPARTMENT**

Presenters: Dr. Brigette Russell, Director of Operations; Sherri Bays, CPA, Vice President of Business Affairs; Paul Cassidy, Financial Advisor; Duane Brown, Bond Counsel

14. **Western New Mexico University – Requests Approval for Issuance of System Revenue Bond Series 2012 ($13,000,000)**

15. **Western New Mexico University – Requests Approval of Student Residential Apartment Complex ($10,956,176)**

Ms. Bays requested approval of the issuance of System Revenue Bonds to finance the construction of a new student residential style complex located on the far west side of the main campus. She said this will add 192 beds and a two-bedroom resident director apartment for a total of 68,050 gross square feet. She said each unit will have two bedrooms, two bathrooms, a kitchenette and a common living area, and the project will also expand the existing laundry facility. The project will also include additional parking and resurfacing of the existing parking available to this new complex.

Ms. Bays said this will be the first new residence hall at WNMU since 1991, and the building will be LEED Silver. She said the age of WNMU’s facilities is impacting their ability to recruit and retain the students on campus, and they feel this project aligns well with the goals of New Mexico as far as increasing educational attainment at the higher education level. She said there is higher attrition out of their dorms – the students that live in student housing then become regular students.

Ms. Bays said construction is scheduled to start in June 2012, with completion expected in July 2013 and occupancy in the fall. She said the funding source will be up to $13 million in system revenue bonds, with total construction costs at $10,956,000, and total project costs at $12,635,000. She said that cost includes capitalized interest payments, reserve requirements and issuance costs.
Responding to Dr. Clifford, Ms. Bays said WNMU currently has 394 beds, of which only 300 are occupied due to the condition of the facilities.

Mr. Cassidy stated that the financing has been structured with 25-year amortizing debt and fixed rate; and the Board of Regents has accepted processing this through a loan with the New Mexico Finance Authority, the state’s bond bank. With their high double-A and triple-A ratings, WNMU can improve the interest rate by going through them and allowing them to credit-enhance the Board of Regents’ debt. He said the interest rate is expected to be about 3.75 percent, which has dropped from the 4 percent when the packet was submitted to the Board Executive Director. He said the annual debt service is anticipated at $775,000 over the 25-year period.

Mr. Cassidy said Ms. Bays and her staff have developed a student housing rental fee schedule that will allow them to amortize the debt from the housing fund rather than subsidizing it from current university funds.

Mr. Cassidy said the initial packet had an $18 million upper maximum, which has been lowered to $13 million. He stated that the Board of Regents, WNMU President Shepard and Ms. Bays determined that instead of 240 beds, they would only build 192 in this phase. In future years, it can be expected that WNMU will come back with additional financings to replace the other housing units as necessary. He said the issue size will therefore be no more than $13 million, and they will fund a reserve fund, pay costs of issuance, and pay NMFA’s fees in doing the transaction. Mr. Cassidy stated that they expect to save $300,000+ (present value basis) by going through NMFA rather than through WNMU for the financing.

Responding to Dr. Clifford, Mr. Cassidy said they anticipate the issue size at $12.6 million, with $10,956,000 to be used for project costs. They had budgeted $691,000 for the reserve fund. He said the capitalized interest is $819,000. He stated that the cost of issuance is expected to be $165,000, with $75,000 for NMFA and the remainder for the Modrall Law Firm and RBC Capital Markets as independent advisers to the Board of Regents.

Ms. Bays said charges for the new housing unit will be about $2,550 per semester, which is about $100 more than the housing in the unit that was built in the 1960s. She said occupancy is very high in the older building, so they do not anticipate a problem with the slightly higher amount being charged. She said the fee is right in line with other universities in New Mexico and is in fact on the low end – they charge less because they have lagged in bringing in new residential housing.

Ms. Bays stated that about $3.2 million remains outstanding from another bond series, which will be paid off in 2019 but will drop off in 2017.

Mr. Cassidy noted that the total pledged revenues, which are the current fund revenues, in 2011 totaled $12.9 million. The current debt service in the 2005 bonds is $578,000, so there is 22x coverage in debt service currently, and they expected 9x coverage when the new series is issued – this is very healthy.
Board legal counsel Zack Shandler read a summary of the parameters resolution into the record: “This is the Regents of Western New Mexico University’s System Revenue Bonds, Series 2012, with a principal not to exceed $13,000,000. The proceeds will be used to plan, design and erect new buildings, including a student housing facility. The final maturity date is June 1, 2038, with a net effective interest rate expected at 4.163% but not to exceed 5% per annum. The Board’s approval is subject to compliance with 2.61.5.16 NMAC.”

Dr. Clifford asked if there is an option to retire this loan early even though the bond is being issued by NMFA and WNMU is borrowing from them.

Mr. Cassidy responded that NMFA will sell a bond issue Thursday morning, subject to approval of the Board today, at a competitive sale, and two issues (including WNMU’s) will be included in that issue. The interest rates and terms will be passed on to WNMU directly, and the bonds that will be sold have a nine-year optional call date at par, so the bonds mature in 2022 and will be called in 2021. He said the terms will exactly match WNMU’s bond issue. He noted that this is a purchase of bonds as opposed to a loan.

Dr. Clifford asked if there is a reason for this structure.

Mr. Brown responded that universities understand the bond issuing process and historically have requested them from NMFA. While the loan process is identical, he said the bonding process fits better with the universities’ programs.

Mr. Brasher moved for approval of Item #14. Mr. Spencer seconded the motion, which passed 4-0 by voice vote.

Mr. Shandler requested that approval of Item #15 be made contingent upon availability of the proceeds from the 2012 System Revenue Bonds.

Mr. Spencer moved approval of Item #15, contingent upon availability of the proceeds from the 2012 System Revenue Bonds. Mr. Brasher seconded the motion, which passed 4-0 by voice vote.
System Revenue Refunding Bond Series 2012 ($18,500,000)

Dr. Russell stated that this is not a new issuance, but a refinancing of existing bonds.

Dr. Fries requested approval of the issuance of System Revenue Refunding Bonds Series 2012. He stated that, in 2008, NMHU issued bonds that were bought by the New Mexico Finance Authority for the purpose of providing funds for the construction of a new 296-bed residence hall. The facility has served their students well, and is very popular in terms of the various housing options that are available, and has contributed to NMHU’s continued modest enrollment growth. He said the sale of the bonds included a one-year call, so NMHU now has the opportunity to refinance the bonds at significant savings in both present value and cash flow.

Mr. Cassidy stated that the bonds issued in 2008 had an interest rate of 4.41%, and at the time NMFA was structuring their bonds with a limited call option. He said NMHU has applied to NMFA to refinance those, and the terms would be a negotiated price that will be worked out with NMFA tomorrow. He said the interest rate they expect to negotiate would be about 3.5% in today’s market, with an anticipated savings to NMHU’s housing fund of between $60,000 and $90,000. He said RBC anticipates savings to be at about $75,000.

Mr. Cassidy said NMHU’s housing fund is self-sufficient and is not subsidized, and charges rates to make the enterprise healthy and able to stand on its own.

Mr. Cassidy stated that they are not extending the final maturity, and expect the optional call date on the loan to be a 10-year par call.

Mr. Spencer commented that a one-year call on a long-term bond is rather unusual, in his experience, and also asked if the bonds issued by NMFA in 2008 also had a one-year call.

Mr. Cassidy responded that NMHU sold a bond issue to finance this loan with a 10-year par call at the time. Between about 2003 and 2008, the bonds NMFA issued had one-year calls, as they were trying to structure them to give communities flexibility. With the fall in interest rates, a lot of people are coming back to have the one-year calls exercised, so NMFA in fact loses income. He said they are trying to deal with that in the way they are structuring bonds today so they don’t have a cash flow problem.

Board legal counsel Zack Shandler read a summary of the parameters resolution into the record: “This is the Regents of New Mexico Highlands University System Refunding Revenue Bonds, Series 2012, with a principal not to exceed $18,500,000. The proceeds will be used to refund outstanding System Revenue Bonds Series 2008. The final maturity date is May 1, 2034, with a net effective interest rate not to exceed 5% per annum. The Board’s approval is subject to compliance with 2.61.5.16 NMAC.”

Mr. Brasher moved for approval. Governor Martinez seconded the motion, which passed 4-0 by voice vote.
**STAFF ITEMS**
Presenter: Stephanie Schardin Clarke, Director

20. **Recommendation of Selection of Contractor to Perform Arbitrage Consulting and Compliance Services**

Ms. Clarke stated that the Board of Finance issued an RFP for arbitration consulting and compliance services in January 2012, with responsive proposals received on February 14, 2012, from five firms: AMTEC; Arbitrage Compliance Specialists; BLX; First Southwest; and Kutak Rock. She said two additional proposals were disqualified for failure to meet all mandatory requirements.

Ms. Clarke said the evaluation committee reviewed the five proposals based on the criteria and weights assigned in the RFP, and assigned the following total scores: AMTEC, 892.6; Arbitrage Compliance Specialists, 850.3; BLX, 882.5; First Southwest, 723.0; and Kutak Rock, 486.3.

Ms. Clarke said the evaluation committee recommends selection of AMTEC to begin negotiations of an agreement with staff for arbitration consulting and compliance services. Additional information related to these proposals and their evaluation remains confidential until final award. Board members who have signed a confidentiality agreement have been provided with the proposals and evaluation committee report; and if the Board has any additional questions at this point, the Procurement Code requires that they be asked in closed session.

Mr. Spencer moved for approval of a tentative award to AMTEC. Mr. Brasher seconded the motion, which passed 4-0 by voice vote.

**BONDS**
Presenter: Stephanie Schardin Clarke, Director

8. **Approval of State Board of Finance Debt Policies**

Ms. Clarke stated that before the Board today is the adoption of updated debt policies, which were discussed in some detail by the Board at the February 21 meeting; and after that discussion, the Board tabled the item so that staff could incorporate additional comments received by Board members and Dr. Clifford.

Ms. Clarke said the updated draft before the Board today contains changes that were incorporated over the last month. Under Policy 2, Capital Planning, additional language was added to describe the process by which bonding capacity is allocated in statute as well as through the legislative process; and a new Policy #17 was added, stating in effect that the Board has procured experts to provide financial advisory services, bond counsel, disclosure counsel, and arbitrage services, and that the Board will continue to retain qualified experts to help the Board remain fully informed about fiduciary duties, legal issues, disclosure obligations and post issuance compliance related to tax exempt bonds.
Ms. Clarke reviewed additional technical comments submitted today by Board bond counsel and indicated those comments would be incorporated into the final version.

Dr. Clifford commented that the additional language under Policy 2 (Capital Planning), which was developed by staff in response to Board questions about more complete disclosure of the process, seems like a very good description.

Mr. Brasher moved for approval, with the amendments as stated. Mr. Gasparich seconded the motion, which passed 4-0 by voice vote.

9. **Letter to Legislators Regarding Capital Outlay Reform and Bond Ratings**

Ms. Clarke reported that, at the last Board meeting, there was discussion about the importance of reforming the Board’s capital outlay process not only because it is the best way to use the Board’s scarce resources, but because it is also important for the Board’s bond ratings. Before the Board today is a draft of a letter to the Legislature; so if the Board adopts this letter or a version of it, staff can circulate it.

Ms. Clarke said the letter discusses, among other things, the intense scrutiny that municipal bond ratings have been under since 2008 especially, and includes some recommendations of changes to the capital outlay process, most of which would require statutory changes.

Ms. Clarke summarized the recommendations:

-- Establishment of a state capital outlay planning board that would meet year round to review capital outlay requests. The board could include representatives from the Executive and Legislative branches’ high level staff. The board would draft and update a five-year comprehensive plan for capital outlay, including all possible funding sources and covering estimates for the cost of design, land acquisition, construction, operations and life cycle maintenance. The board would annually make recommendations for projects that should be funded from Severance Tax and general obligation bonds. Any project that wants to get legislative funding would have to go through this process.

-- Prohibit using long-term bonds to finance assets with life spans shorter than the life of the bonds.

-- Cease the funding of public school capital projects using Senior Severance Tax Bonds and instead fund all such projects with Supplemental Severance Tax Bonds.

-- Establish a minimum project size for Severance Tax Bond and General Obligation Bond projects.
-- Limit the number of prioritized projects local governments can request to two or three per year, and project recipients to demonstrate progress on existing projects before additional requests are made.

-- Require local governments to contribute non-state matching funds to be eligible for state capital outlay funding with a smaller percent match required of areas with lower populations.

-- Limit “reauthorization” of unused capital appropriations in duration and amount or discontinue practice altogether to allow these proceeds to revert to appropriate funds.

-- Lawmakers wishing to target particular projects for financing would be required to coordinate their request with local governments and the state capital outlay planning board. Projects would be funded only if consistent with the board’s identified priorities.

-- Require project recipients to replace or repair any capital asset funded through state bonds if it is lost or damaged within 10 years of state funding.

-- Amend statute to prohibit the State Board of Finance from issuing bonds to fund projects that do not meet certain minimum criteria, such as minimum useful asset life and minimum project size.

Ms. Clarke noted that these ideas before the Board today generally have bipartisan support and make good sense, in her opinion.

Dr. Clifford submitted additional edits for discussion purposes and made the following comments:

-- It is probably okay to cease the funding of public school capital projects using Senior Severance Tax Bonds and instead fund all such projects with Supplemental Severance Tax Bonds, because there are a lot of funds available for public schools through local general obligation debt in particular. However, perhaps the state should periodically review the adequacy of total funding for public school construction and compare that adequacy with the adequacy of funding for other statewide capital outlay needs. If public schools are funded to a much greater extent than other statewide needs, consideration should be given to reallocating a portion of supplemental severance bond capacity to meet other statewide needs.

-- Establishing a minimum project size would increase the likelihood that projects are fully funded, thus avoiding the delays and potential for waste associated with piecemeal projects. However, instead of incorporating his amendment, a separate bullet should be added saying that the state should prioritize fully funding projects or at least a usable phase of any given project that is being funded.

-- Limit the number of prioritized projects local governments can request to two or three per year, and require project recipients to demonstrate progress on existing projects before
additional requests are made. Also limit funding to recipients who have misused funds in the past until a demonstration is made that financial deficiencies have been addressed.

-- Require local governments to contribute non-state matching funds to be eligible for state capital outlay funding with a smaller percent match required of areas with lower populations, low average income and/or low property tax capacity.

-- Re: “Amend statute to prohibit the State Board of Finance from issuing bonds to fund projects that do not meet certain minimum criteria,” soften language by saying, in effect, “permit the Board to decide not to fund.” Give the Board some discretion about whether to fund projects unless they meet criteria as established by the Legislature.

Dr. Clifford said it could be argued that one Legislature cannot bind another one to a project, so there is a question of how these criteria play out with regard to future appropriation statutes.

Governor Martinez noted that, once the capital outlay bill arrived at her office, the review she and her staff attempted was with very limited information. She said often there was a single sentence that said, “Plan, design and construct” an entity such as a community center or a road with $10,000 or $20,000; so they didn’t know whether the allocated funding was for the plan, the design, the construction, or for all three. She said there was never information provided to her by the Legislature as to whether there was matching federal or local funding, or that this funding was necessary to get that match. She stated that the phase of a project was also unknown.

Governor Martinez stated that the Department of Transportation has hundreds of millions of dollars in projects on their books, yet these capital outlay amounts are in the thousands of dollars toward projects that may cost multiple millions of dollars. She said the Department of Transportation already has a list of priorities for roads that need fixing, so this is a complete misuse of capital outlay dollars to have the money linger because someone thought that $50,000 would repave a road several miles long. She commented that there is no documentation to back up that the figure didn’t come out of thin air – there is no engineer’s report stating that a particular $20 million wouldn’t be misspent.

Governor Martinez stated that there was an article in the newspaper about purchasing propane for veterans who attended a particular chapter on Navajo Nation. She said her office tried to find out whether this was for the chapter house or for the homes for the veterans, and later learned from the newspaper that the chapter house was in Arizona. She said it was subsequently discovered that this capital outlay appropriation was never for the chapter house, but for the veterans’ private homes, which is unconstitutional.

Ms. Clarke agreed with the Governor that projects should be vetted at the front end. She noted that the Board is obligated to fund projects that are otherwise legally sufficient. If there is an anti-donation issue, they wouldn’t include it in a bond sale, but things are sort of backwards – it often happens that a project will make it all the way to the Board of Finance for a legal review, only to have staff discover there is an anti-donation problem.
Governor Martinez said there should be a clear message to the Legislature that the public does not see this as a smart way of spending their money – they do not view the bonding of equipment for 10 years when the Governor’s Office has asked for millions of dollars to repair dams and bridges that were completely ignored or outrageously under-funded. She added, “Once again, we’re stuck with $146 million in 284 line items with one sentence descriptors, and some of them had nothing.”

Mr. Spencer moved to authorize that the letter be revised and sent to the Legislature.

Governor Martinez seconded the motion with the amendment that the letter be resent to the Legislature after the November elections should the bodies change.

Governor Martinez added that the Board should be happy to meet with legislators in the interim to start making the changes in advance of the elections.

Ms. Clarke said she would add language at the end of the letter inviting that dialogue.

Secretary Gasparich asked Linda Kehoe, analyst with the Legislative Finance Committee, if she would like to comment.

Ms. Kehoe said she agreed with everything the Governor has stated, and made additional comments:

-- None of the capital outlay is audited. In 2007 or 2008 the LFC recommended that some capital outlay money be set aside for audits as a deterrent to fraud and misuse of money. Right now the LFC tracks 85% of all outstanding money, or about $386 million at the current time.

-- All state agencies are understaffed. In order to have oversight of capital outlay projects, one or two people should report to the LFC quarterly.

-- Regarding the form that the Legislative Council Service declined to release because the information submitted was proprietary when the request was done, probably 95% of all of those forms are filled out by the COGs or local government entity, so they should have been made available by the local governmental entity to say who will own the property and if they have operating and maintenance money. She was not involved from the beginning nor was she asked how these forms could be obtained outside of the LCS.

-- Statute requires that a project using severance tax bonding money should be 5% complete within the first six months, which means the RFP should be out for the plan or design within that timeframe. It is also required that the project be 85% complete by the end of the third year. Board of Finance staff is understaffed and therefore is not enforcing some of these items.

-- Certification form put out by the Board of Finance should be updated to ask questions that would effectively vet a project before bonds are sold. Projects could then be rejected if application forms are not complete, etc.
Ms. Kehoe said she makes no recommendation on a state-owned facility without having toured it.

Ms. Kehoe said she and Mr. Abbey tried to meet with DFA staff early last year to help develop guidelines and a process to be shared with the Legislature, but they were told that the priority at that time was to work with incomplete budgets only. She said she developed guidelines anyway and gave them to legislators.

Ms. Kehoe stated that, in previous years, the Governor and DFA Secretary came to caucuses and proposed recommendations for state-owned facilities and their operating budget. She said she felt a presentation from the Executive branch at these caucuses would be extremely important so that the Governor’s wishes could be known early on.

Mr. Brasher suggested that the Executive branch consider holding public meetings with community leaders and the public to not only get input from them on their needs and interests, but also to explain how the capital outlay process works. He said the Board of Finance or some other entity could schedule these meetings.

The motion passed 4-0 by voice vote.

21. Fiscal Agent/Custodial Bank Fees

Ms. Clarke stated that fiscal agent billings are in line with historic averages, but are reduced significantly because the State Treasurer is holding higher balances at the fiscal agent bank to earn soft-dollar earnings credits. She said custody bank fees are also in line with historic averages.

22. Joint Powers Agreement

The Joint Powers Agreement report was read into the record.
ADJOURNMENT

Its business completed, the State Board of Finance adjourned the meeting at 11:30 a.m.

[Signature]  
Susana Martinez, President

[Signature]  
May 1, 2012

Date

[Signature]  
John Gasparich, Secretary

[Signature]  
5/1/12

Date