

STATE OF ARIZONA

Joint Committee on Capital Review

STATE
SENATE

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RUSSELL K. PEARCE
STEPHEN TULLY

**MINUTES OF THE MEETING
JOINT COMMITTEE ON CAPITAL REVIEW**

Thursday, September 1, 2005

The Chairman called the meeting to order at 1:40 p.m., Thursday, September 1, 2005 in Senate Appropriations Room 109 and attendance was as follows:

Members:	Senator Burns, Chairman	Representative Pearce, Vice-Chairman
	Senator L. Aguirre	Representative A. Aguirre
	Senator Bee	Representative Biggs
	Senator Giffords	Representative Boone
	Senator Gould	Representative Brown
	Senator Johnson	Representative Tully
Absent:	Senator Cannell	Representative Lopes

Senator Burns moved the Committee approve the minutes of July 21, 2005 as presented. The motion carried.

ARIZONA DEPARTMENT OF ADMINISTRATION – Review of FY 2006 Building Renewal Allocation Plan.

Mr. Tyler Palmer, JLBC Staff, presented the Arizona Department of Administration (ADOA) request for review of the revised FY 2006 Building Renewal Allocation Plan. At the July 21, 2005 meeting, the Committee reviewed a portion of the \$3.4 million Capital Outlay Stabilization Fund (COSF) appropriation. This plan contains 10 projects which are outlined in the JLBC recommendation memo.

There was no discussion on this item.

Representative Pearce moved the Committee give a favorable review of the \$1,914,000 representing \$1,740,000 for the 10 projects detailed in the ADOA Building Renewal Allocation Plan, plus \$174,000 for emergency projects and \$275,000 for project management as authorized in the Capital Outlay Bill with the following provisions:

- *ADOA submit for Committee review any reallocation above \$50,000 between the individual projects in the favorably reviewed \$2,633,000 (prior \$893,000 plus current \$1,740,000) Building Renewal Plan.*
- *ADOA report to JLBC Staff any allocations for FY 2006 emergency projects from the total reviewed \$256,000 (prior \$82,000 plus current \$174,000) amount. JLBC Staff will report to the Committee on significant allocations, typically those above \$50,000.*

The motion carried.

ARIZONA DEPARTMENT OF ADMINISTRATION – Review of Refinancing and Renegotiation of the 2000 Private Lease-to-Own Agreement.

Mr. Tyler Palmer, JLBC Staff, presented the ADOA request for review of the refinancing and renegotiation of the 2000 Private Lease-to-Own (PLTO I) agreement. Because of a decline in the interest rates in the market, ADOA projects a savings of up to \$12 million for refinancing the \$80.3 million PLTO agreement.

Representative Pearce asked if ADOA can guarantee the refinance will not result in higher fees from the private entity, Phoenix Industrial Development Authority (Phoenix IDA).

Mr. Palmer stated that since entering this agreement in 2000, Phoenix IDA has raised their fees. The agency met with Phoenix IDA and agreed to a fee schedule that increases the fees slightly, but still results in savings for the state.

Mr. Clark Partridge, State Comptroller, Arizona Department of Administration, General Accounting Office stated that they have met with Phoenix IDA. Phoenix IDA has proposed they change their fees substantially. Director Betsey Bayless wrote a letter to Phoenix IDA requesting that we maintain the existing fee structure, which is \$3,000 per year. They indicated their fee structure under the current model would have been closer to \$64,000 per year plus the same amount as initial refunding. However, the fees have been lowered to a 2-basis point initial fee, which would be a little over \$16,000 as a one-time fee. Then 1-basis point on an on-going basis, which would be \$8,000 a year, but is on a declining balance, so that amount would decline as we paid down the principle of the balance. The savings we are achieving on even the early years will more than make up the fee increase. Phoenix IDA was able to make significant concessions as requested.

Representative Pearce asked what the number is of the anticipated savings.

Mr. Partridge said the savings is about \$12.6 million in total overall. On a net present value basis, those numbers are about \$3.8 million after the financing cots, etc, are all taken into account. Some of the numbers, such as the issuance costs, are high estimates, and we are attempting to get better numbers.

Representative Pearce moved the Committee give a favorable review of the refinancing and renegotiation of the 2000 Private Lease-to-Own (PLTO I) agreement, with the following stipulations:

- *ADOA report back to the Committee on the interest rate, debt service schedule, costs and estimated savings of the refinanced PLTO after the issuance*
- *ADOA report back to the Committee details concerning the potential for additional interest rate savings from other debt financed capital projects*

The motion carried.

ARIZONA DEPARTMENT OF ADMINISTRATION – Review of Energy Savings Performance Contract.

This item was not presented. This item will be held until additional information on the progress of the contract is available.

ARIZONA DEPARTMENT OF JUVENILE CORRECTIONS – Review of Suicide Prevention Renovations.

Ms. Kimberly Cordes-Sween, JLBC Staff, presented the Department of Juvenile Corrections (DJC) request to use \$1.1 million of its FY 2006 operating budget for suicide prevention renovations related to a federal audit. As authorized in the General Appropriation Act, the department may use \$6.7 million of its FY 2006 operating budget for audit related operating and capital issues. These projects will renovate 8 housing units.

Senator Karen Johnson distributed a handout listing psychotropic drugs and known side effects. Senator Johnson requested DJC provide its perspective on the handout (at a later time).

Mr. Michael Branham, Director, Arizona Department of Juvenile Corrections, stated that this issue is continually worked on and is willing to discuss this issue in length.

Representative Russell Pearce asked if the federal government had any requirements related to the use of psychotropic drugs.

Mr. Branham answered that as treatment of all kinds of mental illness progresses, our hope is that there will be better ways for this to be handled without the use of psychotropic drugs. Many of the people show up already using these types of drugs and we have to find a way to help them step down so that we do not endanger them more. We need to continue to work with the federal government and with the medical and mental health community to find better options.

Representative Pearce asked if the renovations end the obligation to the federal issues.

Mr. Branham said we are not at the point where we can say this is the last time this will come before the Committee for renovation issues. We take seriously the role that we need to continue to find ways to improve and stay within budget. We have a population that has not dipped but instead has gone up, and other issues which require us to place into operation older buildings. The department is evaluating what we do right now and what we do in the future for buildings for ADJC.

Representative Pearce stated as clarification that this does not complete the obligation.

Mr. Branham answered that is correct, but we are getting close.

Representative Pearce asked if what we are doing is more than what is required in response to the federal issues.

Mr. Branham said we are trying to make the old buildings safe while trying to change programming and other components of operations. The system will ultimately be better, appropriate, and not overdone.

Representative Pearce moved the Committee give a favorable review to the use of \$1,094,500 from the DJC operating budget for suicide prevention modifications of secure care facilities with the provision that DJC report back to the Committee about whether the Department of Justice (DOJ) believes any additional suicide prevention renovations are required at any DJC facilities. If additional capital work is required, DJC should specify the individual projects required by the federal government to satisfy the terms of the federal audit.

The Committee further requests that DJC's report to the Committee include any correspondence that indicates the federal government perspective on whether DJC's renovation projects have satisfied the conditions of the federal audit.

The motion carried.

ARIZONA DEPARTMENT OF TRANSPORTATION – Review of FY 2006 Building Renewal Allocation Plan.

Mr. Bob Hull, JLBC Staff, presented the Arizona Department of Transportation's FY 2006 building renewal allocation plan totaling \$3.7 million, including \$3.6 million from the State Highway Fund for 223 projects with \$225,300 for contingencies, and \$75,800 from State Aviation Fund for 2 projects.

There was no discussion on this item.

Representative Pearce moved the Committee give a favorable review of the \$3,702,900 FY 2006 Building Renewal allocation plan, including \$3,627,100 from the State Highway Fund and \$75,800 from the State Aviation Fund with the following provisions:

- ADOT report to JLBC Staff any allocations for FY 2006 projects from the \$225,300 contingency amount. JLBC Staff will report to the Committee on significant allocations, typically those above \$50,000.
- ADOT submit for Committee review any reallocation above \$50,000 between the individual projects in the \$3,702,900 favorably reviewed plan.

The motion carried.

ARIZONA STATE UNIVERSITY – Review of Academic Renovations and Deferred Maintenance Phase I Update.

Ms. Shelli Carol, JLBC Staff, presented the Arizona State University (ASU) request for review of scope revisions for Academic Renovations and Deferred Maintenance, Phase I, a \$10 million system revenue bond project that was first reviewed in June 2004. The Committee heard scope changes last month and at that time unfavorably reviewed the \$3 million elevator upgrades component pending additional information from the Arizona Industrial Commission. The Committee favorably reviewed all other components of this project. There was previously \$1.8 million unallocated that has gone to expanding the scope of 2 renovations and 2 new renovations. The per square foot cost is still above average for the project, but they are lower than last month.

Last month Representative Tom Boone requested a comparison between Construction Manager at Risk (CMAR) and the Design-Bid-Build methods. ASU reported the example of Interdisciplinary Science and Technology Building (ISTB) II, an \$18 million research infrastructure project reviewed in March 2004. CMAR saved 8 weeks and \$680,000.

The Industrial Commission responded to JLBC Staff inquiries that the elevator changes they are requiring align with national codes and without those changes, rapid elevator falls, serious injuries and liabilities are possible. The Commission claims that it set no deadline for ASU and provided a rough cost estimate per elevator of \$30,000-\$40,000 just for this upgrade. ASU states that it has 18 elevators that would be covered by the code revision and it would cost \$50,000 per elevator just to address this upgrade. However, codes require that when an elevator is renovated all of its deficiencies be address so ASU estimates an additional \$150,000 would need to be allocated per elevator to do all the remaining code work. The Industrial Commission verbally suggested that ASU complete the project by December 2005 and ASU lawyers believe that to be legally binding.

Representative Andy Biggs asked if there were elevator failures in this state and where the Industrial Commission derived the evidence of failures in the elevators that occurred elsewhere in the country.

Ms. Carol answered that the Industrial Commission did not provide any more detail in the statement.

Representative Biggs asked what the Industrial Commission's response was on the request for clarification for giving ASU no deadline on the elevator upgrade.

Ms. Carol stated that the Industrial Commission viewed it as a suggestion. ASU believed that even though it was a suggestion, it had the force of authority.

Mr. Stavneak stated that there may have been a verbal conversation as opposed to a written conversation. There was a discussion between ASU and the Industrial Commission, but when JLBC Staff asked for it in writing, the Industrial Commission provided a letter stating they provided no deadline to ASU, but were willing to work with them over a period of time.

Representative Pearce asked why the Industrial Commission could not put their conversation with ASU in writing and stated that he is disappointed that the Commission declined the invitation to speak at the meeting.

Mr. Scott Cole, Deputy Executive Vice President, Arizona State University, stated that part of what was provided to JLBC Staff on this issue is the order which has the date from the Industrial Commission. Legal counsel advised that it was a binding order.

Representative Russell Pearce said there was a verbal conversation since the order issuance that was suggested to be followed, but JLBC Staff has a letter from the Industrial Commission saying there is no timeline.

Mr. Cole stated that there was documentation submitted to JLBC Staff which chronicled the conversations with the Commission. They would verbally give additional time to respond, they did not follow up in writing. We went to legal counsel and were told this order is binding and we should try to meet the order. We cannot meet the order, so we told the Commission. We provided a letter with a list of the elevators that we need to upgrade, and they did not acknowledge that they received the list.

Representative Pearce asked if ASU is requesting that the Committee approve the recommendation even though there is a question as to whether the upgrade is needed.

Mr. Cole answered that ASU would like a stipulation given that would allow 2 years to accomplish the elevator upgrades because they are not able to finish by January.

Senator Karen Johnson requested more information on where the elevator failures occurred, the problems that exist, and the reason the Industrial Commission requires the elevators to be retrofitted.

Ms. Carol explained the information provided by Industrial Commission on what could happen with an elevator failure. The code addresses upgrades to hydraulic cylinders that may corrode over time.

Senator Johnson asked for the frequency of elevator failures.

Ms. Carol answered that the information was not provided.

Representative Biggs asked in reference to the Commission's explanation of corrosion in the elevators, if the elevators were inspected for corrosion.

Mr. Cole answered that a contractor inspected the elevators and they showed no signs of corrosion or weakness on any of the hydraulic cylinders. The elevators are maintained.

Chairman Robert Burns stated that the issue of the elevators on this item will be held over to the next meeting September 28 so that the Industrial Commission can have a representative present to answer the Committee questions.

Representative Pearce asked for additional information on the difference in cost between the Commission's amount of \$50,000 and ASU's amount of \$200,000.

Mr. Cole stated that once you open the elevators to work on it, the rest of the cars and controls need to be up to current code. The Commission does not address the code compliance to be at another \$110,000 per elevator.

Representative Pearce asked if the Commission knows that the other components of the elevator need to be up to code, why the information would not be put in their total cost assessment.

Ms. Carol stated that the code applies to elevators built before 1971 and the Industrial Commission does not have records of these older elevators. The only information they have is what ASU provides. They would not know what else needs to be done to the elevators.

Representative Tom Boone asked for more specific information in regard to Interdisciplinary Science and Technology Building (ISTB) II project and the Construction Manager at Risk (CMAR) method: 1) Is CMAR the only procurement method that allows the General Contractor to pre-purchase certain materials? Why or why not? 2) Please breakdown the \$602,000 change order cost avoidance. Which change orders were avoided with CMAR and why? Why would this be the case under the CMAR but not the any other method? 3) What components under CMAR were of higher quality? Why would that occur only with CMAR?

Representative Pearce moved the Committee hold reconsideration of elevator code upgrade component of this issue to permit the Industrial Commission to appear at the next scheduled meeting. Also the Committee give a favorable review to the remainder of Academic Renovations and Deferred Maintenance, with the following standard university financing provisions:

- *ASU shall report to the Committee with a comparison between any compliance costs of the Governor's Executive Order 2005-05, concerning energy efficiency, and operating and other savings generated through those efficiencies.*
- *ASU shall report to the Committee before expenditure of any allocations that exceed the greater of \$100,000 or 10% of the reported contingency amount total for add-alternates that do not expand the scope of the project. ASU shall also report to the Committee before any reallocation exceeding \$100,000 among the individual planned renovations.*
- *ASU shall submit for Committee review any allocations that exceed the greater of \$100,000 or 10% of the reported contingency amount total for add-alternates that expand the scope of the project. In case of an emergency, ASU may immediately report on the scope and estimated cost of the emergency rather than submit the item for review. JLBC Staff will inform the university if they do not concur with the emergency nature of the change in scope.*

The motion carried.

NORTHERN ARIZONA UNIVERSITY – Review of New Parking Structure

Ms. Shelli Carol, JLBC Staff, presented the Northern Arizona University (NAU) request for review of the \$15 million parking structure. It would have 900 spaces on 4 levels and would allow the university to consolidate 5 surface parking lots and reclaim the land for other purposes. This project includes building a pedestrian bridge from the parking structure to an adjoining building and realigning a road. It would be financed with auxiliary revenue bonds for a term of 35 years at a 5.5% interest rate. Annual debt service of \$935,000 would be paid from parking revenues. This project would increase the NAU debt ratio from 5.7% to 5.9%. The cost per space of \$15,400 is slightly high, reflecting materials cost inflation as well as general premium of construction in Flagstaff.

Representative Russell Pearce asked how NAU determined the number of spaces needed and if this project would accommodate long-term parking needs.

Mr. Richard Bowen, Vice President, Administration of Finance, Northern Arizona University stated that there was a master plan process that identified locations and the size of a parking structure on the campus. We do not want to continue to expand the campus we want to build within the existing boundaries of the campus.

Representative Pearce asked if the addition of this structure completes the parking requirements for NAU.

Mr. Bowen stated they have grown from last year and still growing this year, hoping this is the beginning of an upward trend. There is no need for additional parking, but NAU would like to remove surface parking in the central core of campus where new buildings should go.

Representative Pearce asked if this was increasing the parking spaces.

Mr. Bowen answered that it will initially until the surface parking lots are removed. This will give no net gain in the total number of parking spaces. There will be no need to add more spaces until the university is able to grow at another level.

Representative Pearce asked what money is this being used to build the new parking structure.

Mr. Bowen answered that the money is coming from the parking fees, auxiliaries will pay debt service.

Representative Pearce clarified this is not an obligation of the General Fund to repay the Certificates of Participation. These are self-supported revenues that will pay for this entirely. He asked if the market cost per space is \$10,000, why NAU is spending \$15,000 per space.

Mr. Bowen stated that the \$10,000 cost was used long ago, the nature of the land at the campus adds to the cost of building as compared to building in southern Arizona.

Senator Ron Gould asked for clarification on whether the university is going to displace 208 parking spaces to build the new parking structure, and netting an additional 593 parking spaces at a cost of \$15 million for the overall cost of the parking structure. The university is actually spending \$25,337 per parking space.

Mr. Bowen said that was correct, the total cost includes the road realignment and the pedestrian bridge.

Representative Tom Boone asked the following questions be addressed regarding the Construction Manager at Risk (CMAR) method: 1) Why does NAU believe the CMAR method is the best approach and will yield the most cost effective parking structure? 2) Describe the procedure for post-audit of General Contractor payments. 3) Document the cost effectiveness of CMAR, including building quality, occurrence of change orders, and cost savings for a previous capital project.

Chairman Robert Burns asked for clarification on the 65 acres used in eliminating the parking spaces to put in a 900 space parking garage.

Mr. Bowen stated that the university has a higher percentage of cars on the campus compared to other urban campuses. There are 65 acres total of parking lots. There are 900 parking spaces in the garage. The total number of acres will be reduced, not all the acres will be eliminated.

Representative Steve Tully asked if the 35 year bond payment is standard.

Mr. Nick Dodd, Dain Rauscher, Bond Counsel for NAU answered that 35 years is longer than average financing for some university projects. The average financing range is 20-30 years. NAU has financed over 35 years on other issuances and the average life of the facility justifies it. There is a federal tax law that requires the life of the facility to fall with the financing term.

Representative Tully asked if the term is long because of wanting to get the lowest payment.

Mr. Dodd answered the interest rate is low right now going out 35-40 years, at a flat yield curve. The university could borrow at 25 years for 5% and 35 years at 10-15 basis points more. We looked at the impact of the annual debt services and the ability to stretch it to 35 years as opposed to 25-30 years for the university. The additional cost was minimal when compared to the cash flow relief it provided by going out a little further. The university elected for the 35 year structure as opposed to something shorter.

Representative Boone asked if this is a cash flow issue based upon the projected fees coming in.

Mr. Dodd said the university is heavily front-loaded regarding debt service at \$16 million this year and next year. Then it drops significantly, with debt service requirements dropping \$2 million or \$3 million per year in the out years. This structure follows better with the existing debt which is rapid in comparison to other universities.

Representative Boone asked if the cash flow on the fees collected for parking is the only source for revenue to repay the bonds.

Mr. Bowen stated they would only use the parking fees to pay the debt service.

Representative Boone stated that the length of the bond is to relieve the cash flow by paying more interest overall. The university has extended 35 years instead of 25 years for the cash flow relief because of projections on the fees being collected.

Mr. Bowen said that is correct.

Representative Pearce asked what the difference in dollars is on the cost of 25 years versus 35 years.

Mr. Dodds stated that the difference would probably be an extra \$100,000 to \$150,000 in additional interest.

Representative Pearce asked if the interest is minimal for a 10 year addition.

Mr. Bowen stated that the bonds are front-loaded so most of the money is paid in the first period of time. The bonds are sold in larger denominations in the shorter period so that the university is not carrying a longer term and the commitment drops in the out years.

Representative Pearce moved the Committee give a favorable review to the parking structure project with the standard university financing provisions:

- *NAU shall report to the Committee before expenditure of any allocations that exceed the greater of \$100,000 or 10% of the reported contingency amount total for add-alternates that do not expand the scope of the project.*
- *NAU shall submit for Committee review any allocations that exceed the greater of \$100,000 or 10% of the reported contingency amount total for add-alternates that expand the scope of the project. In case of an emergency, NAU may immediately report on the scope and estimated cost of the emergency rather than submit the item for review. JLBC Staff will inform the university if they do not concur with the emergency nature of the change in scope.*
- *A favorable review by the Committee does not constitute endorsement of General Fund appropriations to offset any auxiliary revenues that may be required for debt service costs when the project is complete. These costs should be considered by the entire Legislature through the budget development process.*

The motion carried.

Without objection the Committee meeting adjourned at 2:45 p.m.

Respectfully submitted:

Yvette Medina, Secretary

Lorenzo Martinez, Assistant Director

Senator Bob Burns, Chairman

NOTE: A full tape recording of this meeting is available at the JLBC Staff Office, 1716 W. Adams.