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The USTAR Audit: A Follow Up

The December 2013 edition of "The Utah Taxpayer" reported the results of a legislative audit of USTAR, the Utah Science Technology and Research Initiative. That article reported that the Audit highlighted a variety of discrepancies between what USTAR told the Legislature and what USTAR records show. The article also reviewed USTAR's response published with the Audit, in which USTAR agreed with all of the Legislative Auditor's 15 recommendations.

While USTAR agrees with and is implementing the Auditor's recommendations, USTAR has finalized a more formal response to the USTAR audit, which they shared with members of the Legislature and your Taxpayers Association. The formal response acknowledges that the audit compared USTAR's performance against a one-page promotional piece USTAR provided to Legislators during the 2013 General Session.

USTAR notes that its Governing Authority did not fully vet that piece, which "unintentionally mischaracterized USTAR's Total Economic Impact as 'Return on Investment.'" This one-page piece also failed to incorporate the "promises and expectations" contained in USTAR's 2005 Prospectus. The Auditors were asked to verify the claims of this one-page summary, which they did. As the formal response indicates, USTAR has been successful "in meeting the performance measurements projected to date in the 2005 Prospectus." In other words, the audit focused on the promotional piece, not USTAR's original Prospectus.

Tanner Report confirms USTAR's economic impact

USTAR's formal response builds on accounting procedures conducted by Tanner LLC, a local CPA firm. USTAR hired Tanner LLC to verify projections provided to the Legislature when the USTAR Prospectus was created with USTAR's actual performance. These projections focused on the number of jobs USTAR would create and the amount of outside dollars USTAR would attract, while accounting for the lower than projected revenues the Legislature actually appropriated for USTAR.

As Table 1 notes from the Governing Authority, USTAR's economic impact has been significant. External funding through USTAR have far exceeded both original and revised cumulative economic commitments between 2006 and 2013. USTAR engineering contracts have also emerged much more quickly than USTAR's Prospectus envisioned. The Governing Authority notes that developing appropriate technology to bring to market and license takes longer, so licensing revenue is below projections. The number of jobs created is also behind projections. Nonetheless, USTAR has always understood that it is an investment in the future, and is moving forward to meet its short, medium, and long-term goals.

USTAR Governing Authority Notes Differences with Audit

Much of the rest of USTAR's formal response to the Audit focuses on differences in tone and severity between the Audit's findings and USTAR. For example, the Audit claimed that USTAR failed to budget for sales tax in the construction of its nanofabrication facility, resulting in significant change orders. USTAR's formal response lays the blame for the sales tax mistake with an error by the architect. According to the USTAR Governing Authority's formal response, "The state filed a lawsuit against the architectural firm that designed the facility, and settled for $700,000."

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Table 1: Summarizing USTAR's Key Performance Metrics, 2006 – 2013

	Original Economic Impact Commitment Cumulative (2006-2013)	Revised Economic Impact Commitment Cumulative (2006-2013)	Actual Economic Impact Cumulative (2006-2013)
External Funding	$204,000,000	$165,000,000	$285,206,516
Engineering Contracts	$0	$0	$151,544,942
Licensing Revenue	$2,996,000	$2,355,000	$95,433
Total Jobs	4,511	3,564	1,315

Source: Tanner Report and the USTAR Governing Authority's Formal Response.

The formal response further notes that the Audit faulted USTAR for not having appropriate contracts in place between USTAR and its Bioinnovation Gateway (BiG) after June 30, 2011. The formal response notes that USTAR and BiG signed the 2013 memorandum of understanding (MOU) in July 2012, and the 2014 MOU on November 22, 2013.

Recommendations from Your Taxpayers Association

Your Taxpayers Association has spoken with USTAR's then executive director, Ted McAleer, and with the Legislative Auditor General, John Schaff. It's clear that USTAR management did not get as involved in the audit process as they should have. They were more focused on USTAR's research, and in their political naivete didn't recognize what negative repercussions the audit could, and eventually did produce for USTAR.

As with every audit, the Legislative Auditors gave USTAR many opportunities over several months to review the auditor's facts, findings and recommendations. However, USTAR management did not check and double check the facts and findings against their own understanding and internal documentation.

Your Taxpayers Association appreciates the important work the Legislative Auditor General and USTAR both do for the state of Utah. We recommend that improved protocols between the Legislative Auditor General and entities being audited be put in place to ensure that formal agency responses address not only audit recommendations, but also the audit's facts and findings.

This audit has helped all Utahns better understand how transparency and accountability protect Utah taxpayers, and insure elected and appointed public officials are effectively managing the programs enacted by the Legislature and Governor.

My Corner: What will the 2014 Legislature do with transportation funding?

Association VP Royce Van Tassel

While Howard Stephenson is serving at the Legislature, Mr. Van Tassell will write the corner.

Transportation funding continues to be a hot topic on Capitol Hill and in city council meetings around the state. Utah has not raised the gas tax since 1997, and inflation has eaten away 40 percent of the gas tax's buying power in the 17 intervening years.

Unsurprisingly, transportation advocates and many local governments have been clamoring for the Legislature to raise the gas tax, if only to offset the effects of inflation.

The Taxpayers Association supports transportation. An effective transportation system is necessary for consumers to buy what producers make. We also know that keeping taxes low makes Utah more attractive for economic expansion.

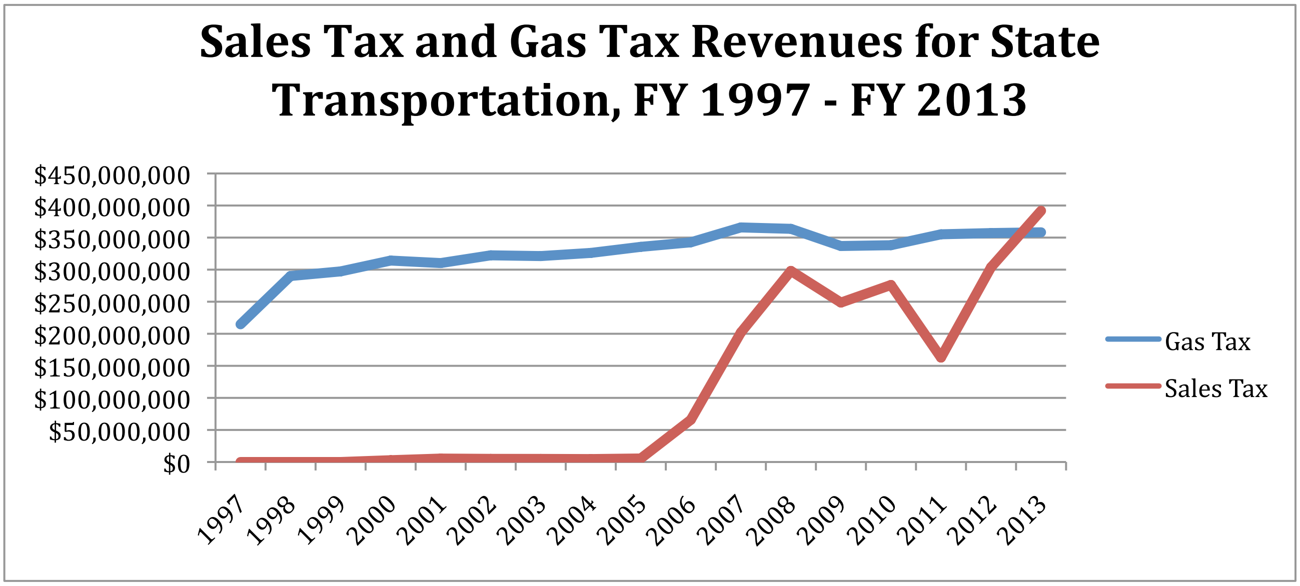
The 1997 Legislature embraced those principles, when they increased the gas tax to pay for roads, but lowered the sales tax to make it revenue neutral. Since 1997, your Taxpayers Association has repeatedly called on the Legislature to raise the gas tax and lower the state's income tax.

Utah Uses Sales and Gas Taxes to Pay for Roads

Too many legislators and transportation advocates today want higher gas taxes with no accompanying cut in other taxes. They bemoan the gas tax's diminished buying power, but ignore the dramatic increases in transportation spending from sales tax over the same time.

As Chart 1 indicates, sales tax revenue going to transportation has skyrocketed since 1997. In 1997, the Legislature appropriated $0 from sales taxes for UDOT construction. By 2013, UDOT was receiving more than $391.8 million in sales taxes, which is even more than the state received in gas taxes. In other words, total road spending has dramatically increased since the 1997 gas tax increase.

Chart 1: Annual Gas Tax and Sales Tax Revenue Used for State Roads, FY1997 to FY2013



Source: Utah Department of Transportation

Despite the dramatic increases in sales tax funding for roads Chart 1 shows, UDOT says it no longer has sufficient revenue to do preventative maintenance on all state roads, let alone the additional state roads being built each year. Instead UDOT focuses their preventative maintenance on interstate and "Tier 1" highways, i.e. those carrying the most traffic. "Tier 2" highways get patches, but no preventative maintenance.

Why Use Sales Tax For Roads

In general, using sales tax to pay for roads is poor policy. The better option is to keep the connection between the thing being taxed and how government uses the tax as close as possible. For example, it's better to use gas tax to pay for roads than it is to use the sales tax paid on a new pair of skis.

The Legislature has used sales tax revenue for transportation for several reasons. First, it's available. Even though Utah has cut taxes by more than $400 million since 1997, sales taxes have been available. Second, the Legislature believes sales taxes derived from "car-related" purchases are nearly as closely related to transportation as gas taxes.

Third, the Legislature puts sales taxes into road funding as a way of not increasing ongoing spending. When the economy is strong, the state collects much more sales tax than when the economy is soft. Rather than putting that additional sales tax revenue into "nice-to-have-but-difficult-to-cut" programs, the Legislature puts sales tax into roads. Then when the economy softens, they pull sales tax out of roads to pay for critical programs like Medicaid, Workforce Services, higher education, etc.

The Politics of the Gas Tax

Those are just some of the policy considerations the 2014 Legislature is evaluating as they consider how best to build and operate Utah's roads. The political considerations are just as important. Very few Legislators want to enter the 2014 election season having just voted for a gas tax increase. (Most observers agree that voters' disgust for gas taxes is only exceeded by their hatred of property taxes.)

Legislators' unsurprising fear of raising the gas tax mixes uneasily at best with the difficult realities of building new roads and maintaining existing roads, so they are getting creative. Representative Johnny Andersen is drafting a complex proposal to cut the gas tax in half and raise the statewide sales tax by the same amount. That way, he says, inflation won't consume all of the state's transportation revenue. Senator John Valentine has a similar proposal. Representative Jim Nielson has already released two other transportation proposals (HB 240 and HB 266).

You'll hear lots of huffing and puffing about fixing Utah's gas tax this year, but it will likely only be huffing and puffing. It's hard to see any realistic chance that both the House and Senate will agree on fixes to Utah's transportation funding proposals. The likely outcome is that this year's huffing and puffing will clear the way for the Legislature to enact transportation reforms in 2015.

-You're Invited-
Legislative Committee Meetings for the 2014 General Session

The Utah Taxpayers Association will hold Legislative Committee meetings during the Legislative Session every Thursday at 7:00 am, in the Seagull Room in the East Annex building (Senate building) near the Capitol cafeteria. These meetings are open to all members of the Association and will begin on January 30th and will continue through March 6th. We will discuss the progress of bills of interest, provide updated legislative watchlists and answer questions about the legislative session. Please join us on Thursdays at 7:00am.

UTOPIA and Macquarie: The latest attempt at protecting UTOPIA taxpayers?

Last month we wrote about the proposed Macquarie-UTOPIA deal, suggesting it would be good in the same way that Google's purchase of UTOPIA was a good deal. UTOPIA is a group of 11 cities that formed a municipal fiber network. Since then, we have learned more specifics about the deal; however, many questions remain. UTOPIA, Macquarie and their member cities are beginning a lengthy potentially four-step or "Milestone" process to determine the specific details of a potential deal.

The Macquarie – UTOPIA Pre Development Agreement

On January 7, the Lindon City Council began debating whether to move forward with the proposed Macquarie – UTOPIA deal. The staff report to the council published on the Lindon City website includes the Pre Development Agreement (PDA) between UTOPIA and Macquarie. That agreement describes the outer limits of the proposed deal and a series of Milestones towards achieving that deal.

Each Milestone includes deadlines and deliverables. When the terms of a Milestone are reached, individual UTOPIA cities and/or UTOPIA and/or UTOPIA's member cities can elect to proceed (or not) to the next Milestone. The first Milestone evaluates whether a business case exists to make this project work, including whether the political will exists to continue the proposed structure of the project. Milestone 2 will refine the scope of the proposed project and develop a full term sheet for the project. Milestone 3 will be the commercial close of the project, followed by the financial close of the project in Milestone 4.

If UTOPIA's member cities proceed to Milestone 4, Macquarie will operate the UTOPIA network for the next 30 years and invest between $350 million and $400 million to complete the network throughout participating UTOPIA cities. UTOPIA and its member cities would retain ownership of the network. At the end of the 30 years, Macquarie would return the fully built-out network to UTOPIA's member cities.

An Availability Payment ?

Some residents in UTOPIA cities have focused on the PDA's "availability payment" participating UTOPIA cities may make "to repay [Macquarie's] capital costs and … operating and maintenance expenses." Since UTOPIA's member cities do not have an existing revenue stream to make this "availability payment," participating member cities may "enact a utility fee on all … addresses that have access to the network whether or not the owner of the property … chooses to utilize the network."

While that language is concerning, your Taxpayers Association is taking a "wait and see" approach. Unlike previous iterations of UTOPIA's makeovers, the PDA specifies the full extent of possible changes well in advance of the cities making a decision. UTOPIA city councils and mayors will continue to work with Macquarie in evaluating potential terms between Macquarie, UTOPIA and its member cities.

By publishing the PDA, which is really a "worst case scenario," and allowing taxpayers and policy makers to fully vet the proposal over a series of months and weeks, UTOPIA is turning over a new leaf. We hope that Macquarie, UTOPIA and its member cities will settle on terms that transfer the risk of UTOPIA's failure from taxpayers to Macquarie and avoid a deal that would increase taxes or fees on UTOPIA's beleaguered taxpaying public.

Obamacare's Insurer Tax's Impact on Utah

In past editions of the Utah Taxpayer we have expressed concerns with expanding Medicaid. The July 2013 edition, noted that while the federal government is promising a large amount of money to fund the expansion, there is reason to doubt that the state would receive all the money promised, especially when Medicaid is already underfunded.

There is now more reason for concern about expanding Medicaid. Beginning this year, Obamacare imposes an $8 billion annual tax on health insurers who provide Medicaid plans. The tax grows to $14.3 billion in 2018, indexed to growth in insurance premium rates thereafter.

Almost all Utah health and dental insurance plans must pay this Obamacare tax, including Medicaid and CHIP plans. For-profit plans must pay 100% of the tax liability, while most non-profit plans pay 50%. Non-profit plans who receive 80% of their revenue from Medicare, Medicaid, CHIP, and dual eligible plans are exempt from the tax.

The tax is imposed on qualifying insurers based on market share of premium revenue from the previous year (i.e., the 2014 tax is based on 2013 revenue). Insurers calculate the tax each August and pay in September. Utah insurers will have an estimated, combined liability of $8 million dollars in 2014.

Impacts to Utah

There are two ways to pay for the tax. First, the insurance companies can pay the tax. However, the insurers are left in a difficult position because the tax adds a significant financial burden on administering Medicaid plans. This tax incentivizes insurers to stop providing Medicaid plans because they do not have the funds needed to fully administer Medicaid.

The other option is to have the state pay the tax. States receive matching federal funds for the Medicaid and CHIP programs. Utah currently receives a 70% match rate on funds; thus, the remaining liability is 30% of the estimated $8 million dollars due in 2014 (approximately $2.4 million). There are various mechanisms that the state could use to pay the tax. The way the state pays the tax is not as important as the effects of the state paying the tax has on insurers. Because the burden of the tax is born by the state, insurers will be able to continue to provide Medicaid plans.

Medicaid is a government program, and the government should fund the costs of providing the program. However, if the insurers or the state pay the tax, it increases the cost of administering Medicaid. This Obamacare tax is one of the many concerning issues that face Utah if we move forward to fully expand Medicaid.

2014 Legislative Watch List Priority Bills

The accompanying table shows some of the priority bills your Utah Taxpayers Association is monitoring. This priority list will continue to grow throughout the legislative session. Visit www.utahtaxpayer.org to view the full Utah Taxpayers Association legislative watch list and stay updated on the Legislature's progress. For additional information, join us at our weekly legislative committee meetings on Thursdays at 7:00am in the Seagull Room in the East Annex building of the Capitol.

Bill	Title	Sponsor	Description	Position
HB 60	Interlocal Entity Service Prohibition	Webb	Requires cities to formally join UTOPIA, before UTOPIA can operate in their cities	Support
HB 66, 1st sub	Municipal Enterprise Fund Amendments	Wilson	Clarifies that cities must provide notice and hold a public hearing to transfer enterprise funds to the general fund	Support
HB 266	Motor Fuel and Special Fuel Tax Rate Indexing Amendments	Nielson	Indexes the gas tax to the "Chained Consumer Price Index for all Urban Consumers;" caps annual rate increases at 5% of previous year; rounds rate increase to nearest tenth of a percentage; if Index falls, then gas tax stays the same	Oppose
HJR 2	Joint Resolution on Business Personal Property Tax Exemption	Nielson	Proposed amendment to the state Constitution authorizing the Legislature to statutorily exempt all business personal property from property tax; eliminates the equal protection clause of the state constitution for property taxes, which would eliminate legal and statutory protections against the Legislature preferring some types of property over others	Oppose
SB 19	Appointment and Qualifications of Members of the State Tax Commission	H. Stephenson	Significantly increases the qualifications threshold for members of the State Tax Commission	Support
SJR 7	Joint Resolution Regarding Qualifications of State Tax Commission Members	Valentine	Removes partisan qualifications in appointing tax commissioners	Support
SB 118	School Funding Through Income Tax Revisions	Jones	Eliminates the personal exemption from the individual income tax over a 5 year period, and authorizes the individual schools to create school level plans to spend the additional money generated by the bill	Oppose
SB 119	Sales and Use Tax Exemption Amendments	Reid	Allows manufacturers to claim a sales tax exemption for all manufacturing inputs, including consumables	Support