Meeting Minutes
Governmental Services Committee
Taxation and Budget Reform Commission
Senate Office Building, Room 301
Tallahassee, Florida
Thursday, November 1, 2007
8:30 a.m. – 10:30 a.m.

Committee Members: *Roberto Martínez, Chair; Barney Barnett; Martha Barnett; Mark Bostick; Talbot D'Alemberte; Bruce Kyle; Robert McKee; Les Miller, Jr.; Randy Miller; Jade Moore; James Scott*

Members Present:

Barney Barnett
Martha Barnett
Robert McKee
Les Miller, Jr. (Acting Chair)
Randy Miller
Jade Moore

Members Present by Phone:

Roberto Martínez
James Scott

Members Absent:

Talbot D'Alemberte
Bruce Kyle

Acting Chair Les Miller called the meeting to order at 8:40 a.m.

Staff called roll and announced the presence of a quorum. Other commission members in attendance included Chair Allan Bense, Mike Hogan, Jacinta Mathis (by phone), and Darryl Rouson.

Approval of the September 27, 2007 meeting minutes was tabled until members had sufficient time for review.

Acting Chair Miller introduced the first presenter, Ted Hoepner, Chairman of the Board of the Florida College Prepaid Program, to provide an overview of the program's activities and plans, as well as an analysis of future projections.

Mr. Hoepner indicated that there have been 1.2 million prepaid college plans purchased since the program's inception in 1988-89 and that more than 73,000 students are using the prepaid benefits. He explained that there are three tuition plan types; the 4-Year University Tuition Plan, the 2-Year Community College Tuition Plan, and the 2+2 Tuition Plan that includes two years at a community college and two years at a university. Additional plans offered include a Local Fee Plan that covers student activities, health and athletic fees, and technology fees; a Tuition Differential Fee Plan that covers the supplemental fee for instruction provided by a public university; and the Dormitory Plan that covers a standard, double-occupancy, air-conditioned dormitory room at either the University of Florida, Florida State University, the University of South Florida, or the University of Central Florida. Mr. Hoepner stated that there is a 15 percent per year maximum increase in cost.

Mr. Hoepner explained that the plan(s) selected may be paid for either as a single lump-sum payment, as monthly payments over five years, or as monthly payments until the child goes to college. He indicated that the cost of the 4-Year University Tuition Plan is approximately $3 per day or $93.12 per month for a newborn (or $13,516 for four years) and that the Tuition Differential Fee Plan costs approximately $4,000. Additionally, Mr. Hoepner stated that the cost of the 2-Year Community College Tuition Plan is approximately $1 per day or $30.15 per month for a newborn and that the cost of the 2+2 Tuition Plan is approximately $2.60 per day or $77.51 per month for a newborn.

Mr. Hoepner indicated that the approximate total is $31,000 for a 4-Year education utilizing the prepaid plan, which is nearly half of the total cost of a 4-Year education. He stated that by investing, the prepaid plan will have enough funds to pay the full cost at the time of use.

Mr. Hoepner reported that a summary of the family income at the time of plan purchase breaks down as follows: 58 percent have a family income of less than $70,000 and 42 percent have a family income of more than $70,000. He indicated that while diversity was not a focus at the beginning of the program, they now specifically target minority populations, which has resulted in a 13 percent increase in the number of minority families participating in the program.

Mr. Hoepner stated that the geographic distribution of prepaid contracts is as follows: 50 percent in South Florida, 35 percent in Central Florida, and 15 percent in North Florida. He explained that they are focused on getting more North Florida students involved in the program.

Mr. Hoepner indicated that 91 percent of the 73,616 students utilizing the program this year are in-state, attending a university, community college, private college, or technical center. He explained that the largest program enrollments are at the University of Florida, University of Central Florida, Florida State University, University of South Florida, Florida International University, Miami-Dade College, Broward Community College, Valencia Community College, and Santa Fe Community College.

Mr. Hoepner stated that their Board is responsible for preparing an annual Comprehensive Investment Plan for the State Board of Administration. He explained that the policy goals are 1) fiduciary safety, 2) liquidity of funds, and 3) yield on investment and that its purpose is to meet the forecasted actuarial liability projections.

Mr. Hoepner identified Florida as one of the few states that have been able to keep their program sound based on adopting an asset allocation policy that balances risk and return.

He explained that the policy allows for investment in domestic equities to the total actuarial reserve, not to exceed 15 percent of the total program trust fund, with the remainder of the assets invested in an Immunized Fixed Income Portfolio.

Mr. Hoepner reported the present value of the program's balance sheet as of June 30, 2007 by citing that the current total assets are more than $7.4 billion with $847 million in actuarial reserves. He explained that the trust fund is actuarially sound since the expected value of assets exceeds the expected value of liabilities for all contracts purchased through 2007. Mr. Hoepner indicated that the two key economic assumptions which determine the financial viability of the Prepaid Plan are the rate of return on the investment portfolio and the rate of tuition increases. He explained that other actuarial assumptions include drop-outs, no-shows, and administrative expenses.

Commissioner McKee asked where the money comes from if they experience a spike in tuition. Mr. Hoepner replied that the money comes from the actuarial reserve and explained that as tuition rates increase, their reserve will decrease. He stated that the Prepaid Plan could withstand an annual 8.68 percent tuition increase and zero out the reserve, but indicated that is a risk that seems high. He explained that they try to keep a 5 percent reserve in order to be able to withstand a 7.5 percent tuition increase, and that it is always their request to exempt current contract holders from tuition increases.

Commissioner Martha Barnett asked if this would include differential tuition rates at universities. Mr. Hoepner replied that the program has fought tuition increases, but this year the Board of Governors determined there would be differential tuitions at research universities such as the University of Florida, Florida State University, the University of South Florida, and the University of Central Florida. He explained that 30 to 40 percent of the cost of tuition is being borne by the student.

Chairman Martinez asked if the College Prepaid Tuition Plan works as an impediment to tuition increases, and, if not, can it adjust to tuition increases? Commissioner Martha Barnett asked additionally if a small segment of the student population is keeping the state from increasing tuition and what is the interaction of Bright Futures with their program. Mr. Hoepner replied that the College Prepaid Plan does not serve to make tuition increases impossible, and that it could adjust to a degree, but that affordability and accessibility are their primary goals. He indicated that already a 40 percent increase in tuition at the four research universities have been factored into their plans. He explained that Bright Futures students with Prepaid Plan contracts can either supplement earlier contracts or get a "paycheck" for going to school.

Commissioner Barney Barnett asked how contracts are priced based on the age of the student, from newborn to 16 year old. Mr. Hoepner explained that the price is based on the number of years until use of service. Commissioner Barnett replied that the price for a 16-year-old's contract should be close to actual cost and suggested to the committee members that they need to understand why the state is in this business of financing 18 percent of students.

Commissioner Randy Miller asked how many students with Prepaid Plan contracts do not go to college. Mr. Hoepner replied that approximately 12 percent of contracts are cancelled and are refunded without interest. Commissioner Miller followed up by asking how many states have this program. Mr. Hoepner replied that every state has tried and most have failed due to market failures in the 1990s.

Acting Chair Miller introduced the second presenter, Nate Johnson, Executive Director for Planning and Analysis, Board of Governors, to provide an overview on cost projections, trends, and student requirements of Florida's Bright Futures Scholarship program on behalf of Mark Rosenberg, Chancellor, State University System.

In his opening remarks, Mr. Johnson explained that the real question is the question of resources for universities. He indicated that funding per student in Florida has declined by approximately 20 percent, and that Florida is last in the country for revenues per student and tuition charged per student.

Mr. Johnson stated that the Florida Legislature created the Florida Bright Futures Scholarship Program in 1997 and established that it be funded by the Florida Lottery. He explained that in 2007-08, Bright Futures represents 60 percent of the state's allocation of financial aid, while only 23 percent is need-based (the majority going to the Florida Student Assistance Grant), and an additional 15 percent goes to the Florida Resident Assistance Grant for private tuition assistance.

Mr. Johnson explained that there are two major components of the Bright Futures program: Medallion and Academic. He indicated that the Medallion program constituted 67 percent of the 2006-07 Bright Futures allocation representing $233 million, while the Academic program made up 32 percent or $111 million. The Medallion program covers 75 percent of a student's tuition costs and requires a minimum 3.0 GPA with a 970 SAT score. The Academic program covers 100 percent of a student's tuition plus a $600 book allowance and requires a minimum 3.5 GPA with a 1270 SAT score.

Mr. Johnson reported that Bright Futures began in 1997-98 with 42,000 students in the program and a total cost of $70 million. He explained that, based on consensus estimates through 2010-11 and assuming a 6.5 percent average annual tuition rate, Bright Futures is expected to grow to 186,000 students in the program and a total cost of $867 million by 2017-18.

Mr. Johnson detailed that in 2006-07, the program is serving 149,000 students at a total cost of $347 million. He outlined the demographic information for the current year as follows: 32 percent are first-time award recipients, 7 percent are non-Hispanic Black, 14 percent are Hispanic, 67 percent are non-Hispanic White, 60 percent are female, and 19 percent qualify for Pell Grants. Mr. Johnson explained that many students do not complete the Free Application for Federal Student Aid (FAFSA), so the Bright Futures program has to base much of their analysis on "neighborhood demographics."

Mr. Johnson stated that 76 percent of the $347 million went to students in the State University System, with $74 million of that going to the University of Florida and $50 million to the University of Central Florida. He indicated that $39 million went to private colleges, with $11 million of that going to the University of Miami. He explained that students who use their Bright Futures scholarship at a private college only receive 75 percent of the average tuition costs for a 4-year degree at a public university.

Mr. Johnson reported that, in Fall 2006, 83 percent of the new freshmen in the State University System received Bright Futures scholarships. He stated that this figure is up from 77 percent in Fall 2004. Mr. Johnson indicated that students receiving only a 75 percent Bright Futures scholarship still pay less than 10 percent of the cost of instruction. He explained that more than 15 percent of undergraduates have Prepaid Tuition Plans and that two-thirds of those students also receive a Bright Futures scholarship which means that 10 percent of undergraduates actually get money back when tuition increases. He stated that a $1 increase in tuition per credit hour generates $6 million in tuition revenue and costs $2.7 million in Bright Futures scholarship dollar increases.

Mr. Johnson then posed the following questions:

- If by better motivating students in high school, could a less expensive program achieve the same result?
- If the goal is to help families and students afford college, how many could afford it anyway and is $400 million in no-need aid a best practice?
- If it is important to keep students in state, are their more efficient ways to do it and could improved universities keep students in-state as well?

Commissioner Mathis asked if Bright Futures students also get the Florida Resident Access Grant (FRAG). Mr. Johnson replied that some students do, and could also qualify for need-based aid as well.

Commissioner Randy Miller explained that FRAG is a subsidy to defray the cost of attending a private school or Independent Colleges and Universities of Florida (ICUF) institution up to 15 percent.

Commissioner McKee asked if that means the state pays a student more to attend a private school and, if so, expressed his concern.

Acting Chair Les Miller explained that before the state had enough state schools, a policy decision was made to keep students in Florida at private schools. He indicated that the Office of Program Policy Analysis and Government Accountability (OPPAGA) did work in this area approximately seven years ago and that the commission members should get a copy of that report.

TBRC Chairman Bense asked that TBRC staff locate the OPPAGA report and distribute it to the members. He explained that while it might be good to look at moving to need-based aid, this is the only break given to the middle class.

Acting Chair Miller introduced the final presenter, Leo DiBenigno, Secretary, Florida Department of Lottery, to provide an overview on past, present and future costs, revenues, and budget information.

In his opening remarks, Secretary DiBenigno explained that he is in the enviable position of getting to raise money for education through the sale of Florida Lottery tickets, while experts with the Department of Education must determine how best to spend those funds. He stated that the Florida Lottery was created in 1986 with a 64 percent voter approval and that the Lottery is about to celebrate its 20th anniversary.

Secretary DiBenigno indicated that the first Lottery ticket went on sale January 12, 1988 and that the first week sales exceeded $95 million. He explained that they do not generate that much revenue in a week today. Secretary DiBenigno explained that all Lottery funds are to be used for education purposes and that the Lottery receives statutory exemptions from procurement guidelines (Chapter. 287, F.S.) and personnel provisions (Chapter 110, F.S.) through Section 24.104, F.S.

Secretary DiBenigno stated that, if the Lottery were a private company, it would rank fifth in the state of Florida in revenue production. He explained that according to an OPPAGA report from December 2004, the Florida Lottery ranks first in the nation in total transfers to the state and that a New York Times report from October 2007 shows that the Florida and California Lotteries have nearly the same profit even though California has twice the population.

Secretary DiBenigno explained that the Lottery has a two-fold strategy to increase sales and lower operating costs to ensure that greater profits go to the Florida Education Enhancement Trust Fund (EETF). He stated that with $4.12 billion in total net sales in 2006-07, the Florida Lottery has nearly doubled its sales in the last ten years and is the third largest lottery in the United States, behind only New York and Massachusetts and ahead of Texas and California.

Secretary DiBenigno reported that net sales from on-line products, such as Florida Lotto, Fantasy 4, Mega Money, Play 4, and Cash 3, were $1.84 billion for 2006-07 and that net sales from scratch-off products such as Sleigh Bills totaled more than $2 billion in 2006-07. He indicated that the Lottery is looking at ways to bring the success of scratch-off products to on-line product sales and hopes to increase the number of point-of-sale retailers from 12,900 today to 13,500 by 2008 with the reintroduction of Instant Ticket Vending Machines.

Secretary DiBenigno showed a break down of the Florida Lottery total expenses as follows: 59 percent to Prizes, 31 percent to the EETF, 2 percent to Vendors, and 2 percent to Operations. He explained that Operations includes expenses related to advertising, staff, and all office operations. He suggested that a measure of business success is through employee efficiency and that the Florida Lottery generates $1.26 billion in profits to the EETF with only 440 employees (compared to Wal-Mart which generates $11.3 billion in profits with 1.9 million employees).

Secretary DiBenigno explained that, of the 43 domestic lotteries, 40 are state agencies and three are publicly-chartered corporations including Georgia, Tennessee, and

Connecticut. He stated that there are no United States lotteries that are privately run at this time, but the United Kingdom national lottery is private.

Secretary DiBenigno summarized the Lottery's weaknesses as including:

- A slower growth rate;
- Low market penetration;
- Insufficient advertising funding;
- Florida Lotto slumping sales;
- A heavy reliance on jackpot rollovers; and
- An inability to replace the aging infrastructure without legislative authority.

Secretary DiBenigno detailed the Lottery's future threats as including:

- Policy constraints that conflict with the legislative intent to operate as an entrepreneurial business enterprise;
- Competition with expanding gambling in and around Florida;
- An inability to reinvest achieved efficiencies for future growth; and
- An inability to support retail-industry trends/processes, limiting access to major retail chains.

Secretary DiBenigno explained that even if the Lottery sales decline because of gambling, ultimately the money will still go to the EETF. He indicated that there is a tension between the business model and the overgrowth of product and mechanism, and that he would like to have the ability to re-invest the savings from efficiencies back into advertising and technology. He stated that the "big box" retailers would like a universal process for handling state and multi-state lotteries, and that Florida could serve as a model for those plans going forward.

TBRC Chair Bense asked about the Lottery's decreasing growth rate over the past few years. Secretary DiBenigno replied that the growth rate is slowing because, after nearly 20 years, it is a mature industry. He explained that there is still plenty of upside potential, but they need flexibility in order to keep the growth curve growing.

Commissioner Randy Miller asked what type of flexibility he needs. Secretary DiBenigno replied that it is difficult to operate in a changing market when they still have to go through the legislative budget process to get authorization for expenditures. He compared Florida to Georgia and Tennessee whose lotteries have broad authority to spend above a set amount if they meet various benchmarks.

Commissioner Moore commented that given the growth rate of the Bright Futures program, it will consume 80 percent of the Lottery in the next ten years.

Acting Chair Miller reminded the committee members that the Governmental Services committee would plan to meet again from 10:45 a.m.-12:45 p.m. in Tallahassee on Friday, November 16, 2007 and tentatively again on Thursday, November 29, 2007.

There being no further business, the meeting was adjourned at 10:31 a.m.