



State of Utah

Privatization
Policy Board

JON M. HUNTSMAN, JR.
Governor

GARY R. HERBERT
Lieutenant Governor

December 22, 2004

Honorable Alma L. Mansell, President
Utah State Senate
W115 Capitol Complex
Salt Lake City, UT 84114

Honorable Martin R. Stephens, Speaker
Utah House of Representatives
W030 Capitol Complex
Salt Lake City, UT 84114

Honorable Olene S. Walker, Governor
Office of the Governor
E220 Capitol Complex
Salt Lake City, Utah 84114

Dear State Leaders:

The Utah State Privatization Policy Board was established by the State Legislature to study and make recommendations to state and local agencies regarding effective privatization of government services. It also functions as an avenue to address concerns from the private sector regarding unfair competition. In 2004 the board studied issues in both these areas of responsibility. As required by statute, we are submitting the enclosed annual report, which details the board's activities.

It is worth noting that the board is a balanced body composed of majority and minority members of both houses of the state legislature, as well as representatives from local government, state administration, higher education, public employees and private enterprise. Special thanks go to past chairman James Kesler for his leadership over the past several years.

While the board has no power to mandate action on the results of its findings, it has the responsibility to see that administrative and legislative entities of government are made aware of them, and wherever possible, to support and pursue the implementation of these findings through the appropriate entity.

The Privatization Policy Board respectfully requests that you thoughtfully review this annual report and consider implementation of the needs identified. The board stands ready to assist the legislature in its deliberations regarding these and any other privatization issues that may merit consideration.

Sincerely,

Ramona Rudert, Chair

UTAH PRIVATIZATION POLICY BOARD

2004 ANNUAL REPORT

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Privatization Policy Board Annual Report

Annual Report 2004

Issues Considered

During the course of the year, several potential issues were brought to the attention of the Board. Each issue is listed below, along with the rationale for the Board's decision whether to review and report on the topic. For issues that were taken under study, an issue summary and the Board's final recommendations are included.

Privatization of Certain Economic Development Functions

- Who brought forward this issue? Senator Dan Eastman and Senator Ron Allen.
- Selected for review and reporting? Yes

Rationale: State government is faced with the challenge of funding all its functions with limited resources. In particular, public and higher education, which already consume the lion's share of all forms of tax revenue, are projected to need increased funding based on growth demographics. If the state is to avoid tax increases, one solution is to "grow the pie" by increasing the number of high-paying jobs, thereby growing tax revenue. Although there are several non-profit and government entities engaged in economic development activities in Utah, job growth has been sluggish in this decade. Bringing new employers to Utah typically has tax incentives therefore; creating high-paying jobs without offsetting liabilities is the "holy grail" of economic development. Novel approaches, perhaps including privatization, are needed in the area of economic development.

Board Action:

At the January 2004 meeting, the board heard a presentation from Steven Jury, managing partner of U'n UTAH, a private economic development company. Based on his research among economic development professionals and top executives of Fortune 500 companies, Mr. Jury made the following contentions:

- The number one reason companies select sites is not incentives, but the work ethic, stability and educational level of potential workers
- Utah has been under-represented by DCED, EDCU and site selection professionals. Site selectors often pass over Utah because of perceptions about its culture—but the reality is different and needs to be presented in a more effective manner.
- DCED lacks the budget and structure to follow through on the leads generated by its marketing efforts (trade shows, receptions, etc) and close sales.
- Privatizing the sales function of economic development makes sense. With private investment and a profit incentive, U'n Utah could bring in as many as 50,000 high-paying jobs by 2008.
- Because compensation to U'n Utah is entirely performance based, there is no risk to the state for undertaking privatization of a portion of its economic development activities.

- U' n Utah's activities would enhance rather than compete with DCED's traditional role.

The board invited DCED to make a follow-up presentation at its March meeting. Presenters were Director of the Department of Community and Economic Development David Harmer and Director of Business and Economic Development Jeff Gochnour. Their presentations can be summarized as follows:

- The pool of available, potential jobs among Fortune 1000 companies simply isn't large enough to provide 50,000 new jobs in Utah.
- Fortune 500 companies do not make their decisions based on the criteria suggested by Mr. Jury. Rather, they look for opportunities to consolidate operations or save money.
- Fortune 500 companies engage professionals to select sites for them; direct calls to company executives would not be effective
- U' n Utah's efforts would hamper or conflict with DCED's efforts. Payment of commissions would simply dilute the supply of funds available to provide economic incentives for companies to locate operations here.

In April, Mr. Jury returned to provide a rebuttal to the March presentation. His presentation included draft specifications for a request for proposal to engage a private company to recruit business to locate in Utah.

Board Recommendation:

The Board adopted a position as follows:

“The board cannot find a reason why a privatized pilot project on economic development should not be tested.” Letters stating these findings were sent to legislative leadership and the governor's office (copy attached).

Unfair Government Competition in the Optical Industry

- Brought by: Noall Knighton, Principal, Knighton Optical
- Selected for review and reporting: Yes

Rationale: The board provides a forum for reviewing cases where privatization results in unfair government competition. In the case brought by Mr. Knighton, the John A. Moran Eye Center, under the umbrella of the University of Utah, has opened a network of retail optometric outlets, one of which is inside the Moran Eye Center itself. This store was opened on site in direct competition with the center's tenant, Knighton Optical. Furthermore, Moran Eye Center intends to begin manufacturing lenses at its new campus facility upon completion of construction, which is currently under way.

Board Action:

At its June and August meetings, the board heard arguments from Noall Knighton of Knighton Optical and Randall Olson, M.D., director of the Moran Eye Center. Dr. Olson

bought with him legal counsel and administrative staff from the Moran Eye Center and the university.

Mr. Knighton's position was based on the following points:

- Knighton Optical maintains a current lease, which was awarded by competitive bid process at Moran Eye Center nearly nine years ago. Moran opened a competitive optical store in December 2002. The Optical store is a commercial enterprise and does not have an educational or research mission.
- Moran continues to open other stores in valley. These locations compete as commercial optical stores and with private optometrists. The university does not provide degrees in opticianry or optometry. The community in the private sector is serving these functions.
- Moran plan to open lens production facility on campus to compete with private wholesale labs. This should be prevented.
- Moran holds contracts with private, for profit health insurance companies such as Altius. Knighton has spoken with Altius, and they do not feel it necessary to have contracts sent out for bid because the "University gives us such a good price." Price cutting by the University should be prevented.

Dr. Olson responded to Knighton's arguments and provided the following facts:

- The Moran Eye Center is home to the University of Utah's Department of Ophthalmology and Visual Sciences. Its annual cost of education totals some \$1.2 million dollars, 72% of which is raised through its clinical programs, 21% from Federal Medicaid matching funds and just 7% from direct State funding (including tuition).
- The center's residency program is consistently ranked among the best in the country. Dozens of medical students rotate through the center each year as part of their clinical training. Students should be exposed to the full range of services that support their ophthalmic education.
- As researchers, educators and physicians, the medical faculty at the center provides cutting-edge clinical care to patients. The state can be proud to have a state of the art facility that enhances the university's reputation.
- As part of the overall trend in healthcare, medical school budgets have become increasingly strained because of reduced reimbursements from health plans. In the case of Moran, funds available from the legislature for higher education are under increasing pressure. Like many schools of ophthalmology, Moran has expanded into retail business in order to build alternative streams of income.

At its March meeting, the Board invited Noall Knighton to provide further clarification regarding his contention of unfair competition. Mr. Knighton held that although the center receives less than 7% of its funding from state sources, deriving the balance from its clinical and retail activities, it enjoys a number of advantages not available to private sector companies:

- Property taxes
- Liability insurance—covered by the state’s umbrella, which caps liability at \$250,000 per occurrence
- Full time fund development staff which raises donor funds with no cost of goods associated with that income
- Benefits available to staff and their families, including free tuition
- Access to capital and favorable borrowing rates
- Support provided the university’s legal counsel, information technology systems, lobbyists, marketing staff and infrastructure

Board Recommendation:

The Board recommended that the Legislature address this issue. Letters stating these findings were sent to legislative leadership and the governor’s office (copy attached). The letter summarized that “two laudable goals are in conflict with one another: one of keeping public agencies from unfairly competing against the private sector, and the other of making institutions of higher learning less dependent on public funding. The Privatization Policy Board sees the overriding issue in this case as whether the Moran Eye Center is competing unfairly in its eyeglass and contact lens operation. We therefore recommend that this issue be addressed by the Utah Legislature.”

UTOPIA

- Brought by: John Christensen, Murray City Council, Russ Wall, Taylorsville City Council and Nancy Saxton, Salt Lake City Council.
- Selected for and review and reporting: No

Rationale: The Utah Telecommunication Open Infrastructure Agency (UTOPIA) is a self-described consortium of 14 Utah cities engaged in deploying and operating a 100% fiber optic network to every business and household (about 140,000) within its footprint. Operating at the wholesale level, it supports open access and promotes competition in all telecommunications services.

The board saw this as a case of reverse privatization, i.e. one in which government proposed to engage in a business that would otherwise belong in the private sector. Proponents argued that universal fiber optic infrastructure would promote economic development. Opponents felt government bonding was too risky in the telecom industry, where technology changes rapidly and investment outcomes are volatile.

The Board agreed to watch the development of the UTOPIA proposal. Members agreed to take it under review only if the proposal were to gain traction and if the board could add value by reviewing it and making a recommendation. Public discussion, including media coverage, took place throughout the first part of 2004. By June, the UTOPIA

proposal was adequately vetted by government at all levels. After several cities initially signed on, support dwindled and it now appears that the statewide proposal will die a natural death. Therefore, there is little impetus for the Board to take it under further study.

Catering Services

- Brought by: Maxine Turner, Cuisine Unlimited.
- Selected for and review and reporting: No

Rationale: Ms. Turner indicated that she was representing the catering association and discussed what they believe are challenges in providing catering at public venues. She indicated that at the present time there is not concern about unfair competition with private caterers. The group's concerns center around institutions (i.e. Red Butte Gardens) creating a "preferred vendor" list and the differences in catering requirements between various entities in state and local governments. Ms. Turner feels that there is no regulation. She feels that the state, county, and city should operate under the same guidelines. She would like the board to take a look at the requirements for guidelines for the various entities, and she recommends more openness for caterers to provide their services at the various venues. The Board decided that it did not have jurisdiction to address/resolve this issue.

Conclusion

While the board has no power to mandate action on the results of its findings, it has the responsibility to see that administrative and legislative entities of government are made aware of them, and wherever possible, to support and pursue the implementation of these findings through the appropriate entity. In 2004, recommendations were made as noted in this report. The attached exhibits include copies of communications sent to legislative leadership and the governor's office.

The Privatization Policy Board respectfully requests that you thoughtfully review this annual report. The board stands ready to assist the legislature in its deliberations regarding these and any other privatization issues that may merit consideration. It is also prepared to respond to the business community regarding cases of unfair government competition with the private sector.