

PROGRAM REVIEW AND INVESTIGATIONS COMMITTEE

Minutes

June 7, 2019

Call to Order and Roll Call

The Program Review and Investigations Committee met on Friday, June 7, 2019, at 8:00 AM, in Room 131 of the Capitol Annex. Senator Danny Carroll, Chair, called the meeting to order, and the secretary called the roll.

Present were:

Members: Senator Danny Carroll, Co-Chair; Representative Rob Rothenburger, Co-Chair; Senators Reginald Thomas, Stephen West, and Phillip Wheeler; Representatives Lynn Bechler, Chris Fugate, Al Gentry, and Ruth Ann Palumbo.

Guests: Deck Decker, Interim Executive Director; Mike Hayden, Chief Operating Officer; Kentucky Communications Network Authority; K. Gail Russell, Secretary, Public Protection Cabinet; Steve Milby, Commissioner of the Department of Housing, Buildings, and Construction; Michael Haney, Director of Division of Fire Prevention, State Fire Marshal.

LRC Staff: Greg Hager, Committee Staff Administrator; Chris Hall; Van Knowles; Jean Ann Myatt; Sarah Ortkiese; Jeremy Skinner; William Spears; Shane Stevens; Susannah Stitzer; Joel Thomas; and Kate Talley, Committee Assistant.

Minutes for May 9, 2019

Upon motion by Rep. Fugate and second by Representative Rothenburger, minutes for the May 9, 2019 meeting were approved by voice vote without objection.

Staff Presentation: KentuckyWired Status Update

Mr. Knowles said the committee had voted to study KentuckyWired at its June 2018 meeting. The Auditor of Public Accounts has issued a report on its own investigation, which was presented to the committee in October 2018. Program Review's investigation has focused primarily on risk allocation, financing, future prospects, and procedural matters. Program Review staff plan to pursue additional lines of investigation, including aspects of the procurement, which remains a focus of the auditor.

He described the time line of the project, beginning with concept development in 2011 or early 2012 for a statewide middle mile network to provide high-speed broadband to which local providers could connect. In early 2014, Columbia Telecommunications

began to gather information and assist in developing a request for proposals for a public-private partnership (P3). By late 2014, a contract had been awarded to Macquarie Infrastructure Developments. The scope of work was “to explore the feasibility of the finance, design, construction, operation, maintenance, and refreshing” of the network. During 2015, Macquarie and the state negotiated plans for financing and carrying out the project. The parties rewrote the contract as a new structure of several contracts specifying a construction cost of nearly \$275 million. The contracts, which also created the complex structure of KentuckyWired, were signed in early September after several series of bonds were sold for more than \$313 million. The Macquarie consortium contributed \$6.5 million as equity.

Within 4 weeks of the 2015 bond sale came the first of many claims requesting schedule changes and additional compensation that eventually were estimated to be more than \$191 million. The planned completion date of July 2018 was missed. During most of 2018, the parties negotiated a settlement that reduced the payments to \$101 million and changed the contracts to reduce future problems. The General Assembly authorized \$110 million of additional borrowing to cover the settlement and future supervening events. This year, the Kentucky Communications Network Authority (KCNA) is seeking ways to borrow funds to cover the settlement payments. The revised completion date is October 2020.

The financing method Macquarie proposed was and is common for P3s. Technically, borrowing was “non-recourse,” meaning the lenders cannot turn directly to the state if project revenues are insufficient to pay the debt. However, the state promised to make availability payments starting when the first network sections became operational and continuing for the 30-year term. State officials assumed that all state agencies, K-12 schools, and higher education would use the new network, so existing broadband spending could cover the availability payments indefinitely. However, the Kentucky Department of Education warned that it could not just switch to a new network because of rules governing the federal E-rate rebate program. The state attempted and failed to cancel the existing AT&T contract in order to award a new contract to KentuckyWired. The state’s share of wholesale revenue from the leasing of extra capacity, projected by Macquarie to be more than \$1 billion, was seen as supplemental income for the state.

Mr. Skinner described conclusions and findings related to financing and funding, and policies and procedures. Mr. Knowles described conclusions and findings related to project structure and risks, and project justification.

In response to a question from Senator Carroll about the staff’s process for the investigation and any impediments to it, Mr. Knowles said that staff have primarily reviewed documents and have conducted some interviews. Potentially, there will be over 1 million emails to review. Claims of attorney-client privilege have been an issue.

In response to questions from Senator West about the AT&T contract, Mr. Knowles said the Finance and Administration Cabinet issued a request for proposals (RFP) in 2015 for providing Internet service to state agencies, higher education, and K-12 schools. AT&T, the current provider, protested. The cabinet canceled the RFP.

In response to questions from Senator West about the 55 percent of revenue not accounted for by K-12 schools, Mr. Skinner said that it primarily represents the cost of internet service for state agencies and higher education. Mr. Knowles said the 55 percent is not at risk because of the AT&T contract, but the state has the option to move service for state agencies to another provider. Higher education can do the same. Some potential customers have expressed concern about reliability should that occur.

In response to questions about the agreement with the Center for Rural Development, Mr. Knowles said he cannot speculate as to why the agreement came to be. The center would receive 100 percent of wholesale revenue from the eastern Kentucky portions of the project and 50 percent of the wholesale revenue from the I-75 corridor. The state would get 100 percent of the revenue from western Kentucky. Sen. Carroll said that there are concerns that the western Kentucky ring will be completed, which means that, at most, the state would be getting one half of the revenue.

In response to questions from Senator Carroll, Mr. Knowles said that the project agreement requires that refreshes be done every 10 years. There are indications that more frequent refreshes will be needed to be competitive. Mr. Skinner said that the settlement agreement did not change the intervals at which the KentuckyWired system would be refreshed. Mr. Knowles said that staff did not know whether the current technology being installed is the same technology that was purchased at the beginning of the project.

Senator Wheeler asked whether the project's justification has changed, and if not, has there been any investigation into the services being provided to underserved areas and alternatives to KentuckyWired. Mr. Knowles said that staff have been unable to answer the question about current provision of services, in part because information about current middle mile service is proprietary. Senator Wheeler said that Internet service in Pikeville, where he is from, is terrible. He said that it seemed that service would already have been provided to underserved areas if providers were capable of doing so. He asked whether the fact that there are underserved areas is a justification for KentuckyWired. Mr. Knowles said that staff are not able to speculate as to the status of the current service providers in the state, but it would be up to the local service providers to build the last mile service and connect to the KentuckyWired network.

In response to a question from Senator West, Mr. Knowles said that income from state agencies is not included in the revenue shared with the Center for Rural Development, which receives a share of wholesale revenue.

In response to questions from Senator Thomas about why the KentuckyWired project cannot rework projections, whether the technology can be tested as the network is built, and construction in western Kentucky, Mr. Knowles said that KCNA officials may be able to answer. Senator Thomas said the focus should be on how this project can be moved forward.

Senator Carroll said the focus for this investigation is on the poor decisions that have led to the state of the project and the lessons to be learned from that. The focus is not to make recommendations or decisions on the project moving forward.

In response to questions from Representative Rothenburger about the Center for Rural Development agreement, Mr. Knowles said staff are looking into the wholesale revenue the center would receive and the status of the agreement. The center provided \$23.5 million of federal grant funding, for which the memorandum of agreement established the rules for the state to receive it. The addendum was apparently added later; Program Review staff do not know when. The federal grant money is not linked to the addendum. Mr. Skinner said the state will receive the federal grant money upon the completion of Ring 1B in eastern Kentucky.

In response to questions from Representative Rothenburger, Mr. Knowles said KCNA has testified that there has been interest by parties in buying wholesale service. Staff have not looked into marketing of the wholesale fiber.

In response to questions by Representative Rothenburger as to when risks were mentioned to the state, Mr. Knowles said Columbia Telecommunications outlined many issues in May 2014 to state officials. Concerns about risks were also mentioned in responses to the request for information. Mr. Knowles said that Program Review staff do not know whether the risks were properly assessed before the decision was made to move forward with the project.

Representative Rothenburger commented that before 2015 a superintendent had expressed concern to him about how devastating it would be to local school districts to lose E-rate funding.

In response to a question from Senator Carroll, Mr. Skinner said that there are contractual elements for the private partner investment and the return on that investment. The return on investment will come from state payments.

In response to questions from Senator West, Mr. Skinner said the \$23.5 million in funding from the center will go to the design builder, not the general fund. This is typical for a public private partnership. The private partner has not made its full \$6 million contribution at this time, it is on a schedule.

Senator Carroll requested that representatives from KCNA give a brief update on where the project is and when the state can expect it to be online. Mr. Hayden said the network is still scheduled to be completed by October 2020. It is typical to do a project like this in phases. Ring 1A and 1B will be done simultaneously and the central Kentucky ring will be done a month after. Contractors have been working faster than scheduled.

Senator Carroll said that the problem is not the current officials. The committee is looking at past decisions and contracts.

Mr. Decker said the project has worked through most of the delays, but western Kentucky will present challenges. All the contracts are not in place there but will be soon. Ring 1A is being tested now. Mr. Hayden said Ring 1A has to be brought up first because it has the Commonwealth Data Center.

In response to a question from Senator West, Mr. Hayden said approximately 1,500 miles have been completed, which is nearly half the total.

In response to a question from Representative Gentry, Mr. Decker said that the October 2020 completion date is realistic. The only concern is Ring 4, which is the only possible delay if the contract is not established.

Senator Thomas said he is encouraged by what Mr. Hayden and Mr. Decker have said. He asked if projections of revenues have been done and if those revenues are more or less than the original \$1 billion. Mr. Hayden said several conditions have changed in the past 5 years. Internet rates have dropped across the state. KCNA is looking at market conditions and original projections. They are working to get the projections done but do not have them today.

In response to questions from Representative Bechler about the settlement contracts, Mr. Hayden said the settlement contracts have been signed and have paid \$9.5 million to \$10 million so far.

Senator Carroll said that some legislators are ready to pull the plug on this project. He said it is crucial to complete the area west of I-75 to generate revenue. Mr. Hayden said that not completing areas west of I-75 will create issues, for example, only having half of the community college campuses in the system.

Senator Carroll said that there will be discussions as to how the committee should proceed from here.

Overview of State Fire Marshal's Office

Ms. Russell introduced herself, Mr. Milby, and Mr. Haney. Mr. Haney described how the Division of Fire Prevention accomplishes its mission through inspections,

education, and coordination with local fire departments and the organizational structure of the division. Mr. Milby provided an overview of the downward trend in restricted fund revenue for the division and described funding challenges. The number of personnel in the declined from 40 in 2017 to 27 in 2019. Because nonsalary costs such as pension contributions have increased, personnel costs have not decreased as much as the number of personnel. Ms. Russell said that the decrease in resources limits what the division can do. As a result, there will be a request for up to \$3 million in additional revenue for the next biennium.

In response to questions from Senator Carroll, Mr. Haney said that local inspectors do not have time to perform inspections outside of their districts.

In response to Senator Carroll's question about the details of the \$3 million request, Mr. Milby said it includes \$150,000 for each of the 10 inspectors who would be hired, which includes vehicles, equipment, fringe benefits, and pension. The cost for each of the three office personnel is \$75,000. The remainder would be for training.

In response to a question from Senator Wheeler about training, Mr. Haney said the training includes doing inspections, fire schools, and teaching volunteer firefighters to do investigations. Training is free and open to the public. Ms. Russell said the fire marshal takes over inspections once the building is not new construction. Mr. Haney said the growth in technology and complexity of buildings is why more assistance is needed.

Senator Carroll asked why there is no fee charged for the inspections and whether other states charge for inspections. Mr. Milby said this is because of statute. Mr. Haney said that the focus is on public protection. Mr. Haney said Virginia and West Virginia have minimum fees; some local jurisdictions in other states have fees. Ms. Russell said there is a distinction between charging a fee related to new construction, in which case the facility cannot open until the inspection takes place and is paid for, and existing buildings, which may be impractical to close if the fee is not paid.

In response to Representative Rothenburger's questions about the sources of restricted fund revenue, Mr. Milby said that this includes hazmat inspections and fuel tank inspections. The decline in fire prevention revenue is partly because of the end, because of a lack of personnel, of a memorandum of agreement the division had to do sprinkler inspections for state-owned buildings.

Representative Rothenburger asked about the status of doing building plan reviews. Mr. Milby said that the Department for Building Codes has more personnel than before. There was a backlog, in part because of increased construction and retirements in the department. Mr. Milby said that currently the department takes 20 days for plan review and is moving toward 7 to 10 days.

In response to a question from Representative Rothenburger about software updates by the state fire commission, Mr. Haney said that the Department of Housing, Buildings, and Construction has its own software, so his division is not connected to the fire commission's system.

Representative Rothenburger asked if the division has adequate staff to implement the school safety legislation. Mr. Haney said that to do annual inspections of prioritized buildings, which includes schools, daycares, and hospitals, they have to deprioritize smaller places of assembly.

Senator Carroll asked if the department has run numbers based on charging a fee for inspections. Mr. Haney said that they had not done one but would try to get those numbers to the committee.

Representative Bechler said that the appropriation for fiscal year 2020 will be 2.8 percent greater than fiscal year 2019. Representative Bechler said there was a 2.3 percent average increase from fiscal year 2016 to fiscal year 2020. Mr. Milby said that is correct. Representative Bechler asked for fire prevention personnel costs for fiscal year 2020. Mr. Milby said that he will provide this information. In response to a question from Representative Bechler, Mr. Haney said that fire protection is in the KERS Nonhazardous system.

In response to questions from Representative Gentry about people assembling in large numbers in the capitol, Mr. Haney said the authority lies with the state police. Fire marshals give numbers for specific areas and areas that should be kept clear in case of an emergency. He said that if it were up to the fire marshals, they would remove people from where there is no exit. They work with police and try to enforce the code as compassionately as possible. In response to Representative Gentry's question, Mr. Haney said that building codes and regulations are mostly from the state.

Representative Gentry said he had a press conference held on the House floor that multiple people in wheelchairs could not access. In response his question about the Americans with Disabilities Act (ADA), Mr. Milby said new buildings meet the requirements of the act. If there are changes in the use of a building, the building must be brought into compliance with the ADA. Older buildings present a challenge. Mr. Haney said that fire marshals ensure that buildings' ADA compliance is maintained but cannot make buildings install new ADA elements.

Senator Carroll thanked the officials for their testimony and complimented field inspectors with whom he has interacted.

The meeting was adjourned at 10:02 AM.