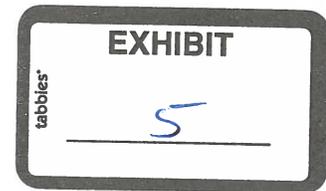




COLORADO
Department of Natural Resources

Executive Director's Office
1313 Sherman Street, Room 718
Denver, CO 80203



MEMORANDUM

May 2, 2018

Office of the State Controller
Attn: Doug Platt
1525 Sherman Street, Fifth Floor
Denver, CO 80203

Re: Proposed Revisions to the Department of Personnel & Administration, Division of Finance and Procurement State Fiscal Rules (SOS Tracking Number 2018-00117)

Dear Mr. Platt:

On behalf of the Department of Natural Resources (DNR), I submit the following comments on the proposed revisions to the Department of Personnel & Administration, Division of Finance and Procurement State Fiscal Rules submitted to the Colorado Secretary of State on March 28, 2018 (the "Proposed Fiscal Rules").

Proposed Fiscal Rule 3-1

Subject to a number of exceptions, the Proposed Fiscal Rules generally prohibit the advance payment of funds for goods, services, and other contractual obligations, Proposed Fiscal Rule 3-1, §§ 9.1, 9.4; however, the general prohibition on advance payments does not apply where payment is made up to one year in advance for "water rights purchases, temporary water leases, or water storage payments." Proposed Fiscal Rule 3-1, § 9.4.30. DNR recommends that "water assessments," which involve the same considerations as the other types of excepted water transactions, be included in Proposed Fiscal Rule 3-1, § 9.4.30.

As you may know, several DNR divisions have regularly obtained blanket waivers from the Controller for water assessment payments made to water co-operatives and ditch companies. We believe that formally incorporating this waiver into the rule itself would improve efficiency by removing the need to extend the blanket waivers every three years.

Proposed Fiscal Rule 3-3

Under the Proposed Fiscal Rules, Controller review and approval is required for "all expenditure contracts, task order contracts, and price agreements." Proposed Fiscal Rule 3-3, § 8. The following comments are intended to clarify the scope of the Controller's review and approval responsibility.

(a) Definition of "Expenditure Contract" (Proposed Fiscal Rule 3-3, § 2.9)

Proposed Fiscal Rule 3-3 expands the scope of the term "Expenditure Contract" to include contracts for services that involve an expenditure of state funds in the event of an agency's



failure to perform its contractual obligations. This new definition could include almost every services contract entered into by DNR, including revenue generating contracts such as leases, because monetary damages are almost always a potential remedy in the event a party, including a state agency, is found to be in breach of its contractual obligations. *See, e.g., Thompson Creek Townhomes, LLC v. Tabernash Meadows Water & Sanitation Dist.*, 240 P.3d 554, 556 (Colo. App. 2010) (citing *Ace Flying Serv., Inc. v. Colo. Dep't of Agric.*, 136 Colo. 19, 22, 314 P.2d 278, 280 (1957)).

It seems unlikely that this was the intent in drafting the Proposed Fiscal Rules. Despite the significant increase in the Controller's review and approval burden that would be caused by the Proposed Fiscal Rules, there is no indication the Controller analyzed the fiscal impact of the Proposed Fiscal Rules or the additional FTEs required to fulfill the expanded review and approval duties imposed by the Proposed Fiscal Rules in a timely manner. DNR recommends the following modifications to the revised definition of "Expenditure Contract" to require Controller review of only those services contracts most likely to involve an expenditure in the event of a breach.

First, while the Proposed Fiscal Rules categorize real property leases/licenses when the State is landlord or licensor as Revenue Contracts, Proposed Fiscal Rule 3-3, § 3.2.2, without a definition of "service contract," it is unclear whether leases are considered service contracts. DNR recommends the new definition of "Expenditure Contract" be amended to clarify that lease agreements in which the State is the lessor are excluded from the definition of Expenditure Contracts.

Second, it is unclear which services contracts are "likely" to result in an expenditure of state funds in the event of a breach by the State. DNR recommends the new definition of "Expenditure Contract" be amended to clarify that only those services contracts whereby a state agency assumes contractual liability for liquidated damages in the event of a breach are subject to Controller review and approval.

Third, the newly added language including revenue diversion agreements as Expenditure Contracts expands the scope of the Controller's review responsibility to encompass any modification to leases to address, for example, drought relief or other issues during the life of the lease, although the modification will only change the revenue to be received from what could be classified as a Revenue Contract. DNR recommends the new definition of "Expenditure Contract" be amended to clarify that agreements to change the revenue owed under a Revenue Contract are not themselves Expenditure Contracts.

DNR's proposed modifications are reflected below:

Rule 3-3, 2.9 Expenditure Contract - A State Contract where a State Agency or Institution of Higher Education is required to make payment, either in funds or in-kind, to another Party, directly or indirectly, and includes any agreements that divert revenue that would otherwise be due to the State from a source other than the original State Contract. An agreement where the State is required to perform a service for another Party is an Expenditure Contract if it is likely that the State's failure to perform would result in the payment of State funds to the other Party includes a liquidated damages provision whereby the State assumes express liability for such damages in the event of a failure to fulfill its contractual obligations.

(b) *Definition of “Non-Expenditure Contract”* (Proposed Fiscal Rule 3-3, § 2.19)

Proposed Fiscal Rule 3-3 adopts a new definition for the term “Non-Expenditure Contract.” Consistent with the proposed revision to the definition of “Expenditure Contract,” the definition of “Non-Expenditure Contract” excludes those contracts likely to result in an expenditure of state funds if an agency fails to perform its contractual obligations. As above, it seems unlikely that this expansion of the Controller’s review responsibility was intended, and DNR recommends the following modification to the new definition of “Non-Expenditure Contract” to enhance simplicity and clarity:

Rule 3-3, 2.19 Non-Expenditure Contract - An agreement between a State Agency or Institution of Higher Education and another party that is not an Expenditure Contract ~~involving an exchange of resources, goods, or services, that does not result in the expenditure of funds by the State Agency or Institution of Higher Education or that is a Revenue Contract, and the likely result of a failure to perform by the State Agency or Institution of Higher Education would be the inability of the State Agency or Institution of Higher Education to receive the benefit of the Contract and not the expenditure of State funds.~~

(c) *Definition of “Settlement Agreement”* (Proposed Fiscal Rule 3-3, § 2.30)

The Proposed Fiscal Rules expand the definition of the term “Settlement Agreement” to include contracts “ratifying agreements concerning . . . legal disputes, regardless of which party is making payment under the Settlement Agreement.” Moreover, the Proposed Fiscal Rules classify “Settlement agreements” as “Expenditure Contracts.” Proposed Fiscal Rule 3-3, § 3.1.12. These revisions significantly expand the scope of the Controller’s review responsibility.

Instead of making it clear that the Controller’s review responsibility extends only to Settlement Agreements requiring the expenditure of state funds, the Proposed Fiscal Rules extend the Controller’s review responsibility to all Settlement Agreements, even those that do not involve the expenditure of state funds. For example, under the Proposed Fiscal Rules, Controller review would be required for Settlement Agreements whereby a third-party agrees to pay money to the State. Although such agreements are most accurately characterized as “Revenue Contracts,” *see* Proposed Fiscal Rule 3-3, § 2.27, under the Proposed Fiscal Rules such agreements require Controller review and approval. Furthermore, the Proposed Fiscal Rules apparently extend Controller review to Settlement Agreements that do not involve the payment of any funds by either party.

Previously, the Fiscal Rules only required review of contracts ratifying agreements concerning employment or contractual disputes. Fiscal Rule 3-1, § 2.36. *See also* State Controller Contract, Grant, and Purchase Order Policies, Settlement Agreement Policy (Jan. 2009). The review of such agreements is consistent with the Controller’s review of “Expenditure Contracts,” because the settlement of contract and employment disputes often involves the expenditure of funds by a state agency. The changes in the Proposed Fiscal Rules extend the scope of Controller review to contracts ratifying settlements in all legal disputes, but fail to incorporate the limitations implicit in the previous definition and in the Controller’s Settlement Agreement Policy.

DNR recommends the following modification to the revised definition of “Settlement Agreement” to expressly confirm our understanding that the Controller’s review responsibility applies only to Settlement Agreements involving the expenditure of state funds¹:

Rule 3-3, 2.30 Settlement Agreement - A State Contract between a State Agency or Institution of Higher Education and another party for the purpose of ratifying agreements concerning employment, contractual, or legal disputes involving payment by the State. ~~, regardless of which party is making payment under the Settlement Agreement.~~

Finally, in defining the terms required to be included in Settlement Agreements, the Proposed Fiscal Rules incorporate by reference the State Controller Contract, Grant, and Purchase Order Policies. Proposed Fiscal Rules 3-3, § 5.1.4. The current version of those Policies, last updated in January 2009, reflects the previous definition of the term “Settlement Agreement.” We presume the Controller will update the Policies to reflect the changes in the Proposed Fiscal Rules, but without access to the proposed changes to the Controller’s Settlement Agreements Policy, it is not possible to fully comment on the content of the Proposed Fiscal Rules.

(d) Process for Review, Approval, and Signature (Proposed Fiscal Rule 3-3, § 8.3)

The Proposed Fiscal Rules largely adopt, with minor, non-substantive revisions, the previous provisions regarding the Controller’s process for review, approval, and signature of Expenditure Contracts. *Compare* Fiscal Rule 3-1, § 9.3 *with* Proposed Fiscal Rule 3-3, § 8.3. Although DNR has no objection to the changes made, it takes this opportunity to request consideration of an additional change to these provisions.

Many of the transactions and agreements entered into by DNR, notably Colorado Parks and Wildlife (CPW) and State Land Board (SLB), are subject to special timing considerations. For instance, both CPW and SLB are often involved in complex real estate transactions with multiple parties in the ever-competitive market of open lands purchases. Timing is often a crucial consideration in the negotiation of these transactions, and the lack of certainty regarding the length of time required for Controller review can make parties reluctant to contract with CPW and SLB. These difficulties affect CPW’s and SLB’s ability to compete in the open market, and, as a result, they may be required to make additional concessions.

Although DNR appreciates the significant burden imposed by the Controller’s responsibility to review all Expenditure Contracts, it requests that the Controller consider adding guidance regarding the length of time required for Controller review and approval. Such guidance would significantly aid DNR in its ability to compete with private parties for scarce resources, in the process fulfilling its constitutional and statutory missions.

¹ This understanding is informed in part by the present version of the Fiscal Rules and in part by the limited scope of the Controller’s powers, duties, and functions, which relate to acting as the State’s chief fiscal officer and managing the State’s fiscal affairs. See Colo. Rev. Stat. § 24-30-201(1) (cataloging the Controller’s powers, duties, and functions) and § 24-30-202(10) (vesting in the Attorney General final authority regarding “the legality of any obligation by or claim against the state”).

Thank you for the opportunity to review and comment on the Proposed Fiscal Rules. Please do not hesitate to contact me directly if you have any questions regarding these comments.

Sincerely,

Tobin Follenweider
Chief Operating and Performance Officer
Department of Natural Resources