

**Testimony of Treasurer Robert M. McCord
on the Fiscal Year 2014-15 Executive Budget Proposal for Pennsylvania Treasury
House Appropriations Committee
Tuesday, February 11, 2014**

Chairman Adolph, Chairman Markosek, and Committee members, thank you for the opportunity today to discuss Treasury's appropriation for Fiscal Year 2014-15.

I want to start by thanking the legislators again. During my first term and again this past year, Treasury has received valuable bipartisan support from the General Assembly for our work on behalf of the people of the Commonwealth. I really am grateful for the bipartisan cooperation that has aided my staff and me as well as the many hard-working career employees of the Treasury as we carry out our mission.

Treasury has an important fiduciary responsibility to the people of Pennsylvania to safeguard and invest their financial assets, and you have recognized the critical role Treasury plays in serving the public.

Treasury and the General Assembly have a mutually beneficial relationship. When you give us the wherewithal to do our job well – as you have done the past five years – we in turn can help you do your job well by increasing the revenues you have available to address the needs and priorities of your constituents and the entire commonwealth.

I believe the people of Pennsylvania have gained from our cooperation. Each of Treasury's major programs – the PA529 college savings plan, unclaimed property, and investments – had a strong year, and a strong five years, through our work together.

Before I discuss those programs in more detail, however, let me focus on the most significant change that would affect Treasury in the governor's proposed budget. It includes an increase of \$3.5 million to the General Government Operations (GGO) line item to support increased processing and advertising costs for the unclaimed property program. The governor proposed to shorten the dormancy period from five to three years for most property types.

The governor's budget estimates that Fiscal Year (FY) 2014-15 General Fund revenues from unclaimed property will go from \$196 million in FY12-13 to \$399.5 million in FY14-15. The estimate includes \$150 million growth in near-term revenue from changing the dormancy period and an additional \$54.6 million from ongoing holder reporting.

Our department is fine with providing the work to adapt to new rules and earlier revenue claims. But I want to be clear, most of the revenue that results is a "one-time pop" in revenues that are, essentially, just carried forward by two years. Plus, I generally rely on conservative revenue models, and I worry the Budget Office's forecast could prove too optimistic.

There is room for reasonable debate. It is hard to predict collections, and we are mindful that in several recent years, there have been some significant settlements that have increased unclaimed property revenues.

Certainly, our ability to meet any expectations for additional revenue will be contingent on available resources – and some modest updates to the unclaimed property law to assist us in our efforts to increase compliance and enforcement.

The additional cost associated with the change in the dormancy period and the resultant budgetary advantage for the commonwealth leads me to a broader cost/benefit analysis of Treasury's budget.

In reviewing our budget request, the most important thing to understand is that Treasury is different from virtually every other commonwealth agency. Our principal function is not to implement public-facing programs legislated by the General Assembly. While we do perform a service function in making payments for other agencies, our real value is that we generate significant amounts of revenue to support other agencies in carrying out their missions.

In short, Treasury is an important commonwealth profit center:

* We generate revenue for the commonwealth through our investment activity. Since I took office, investment returns have totaled \$2.32 billion.

* We generate revenue for the commonwealth through our fiscal review activities. We are mandated by the Fiscal Code to audit each proposed payment, and to make only those we find lawful and correct. In the last five fiscal years, our auditors have blocked \$450 million in improper payments. That is, of course, the same as generating \$450 million in revenue for the commonwealth.

* Our efforts to get holders of unclaimed property to submit it to Treasury generate large numbers: in the last five calendar years, we have collected property worth \$1.134 billion. We returned \$518 million back to the rightful owners, meaning \$616 million went to the General Fund.

All told, just these activities have generated about \$3.39 billion in revenue for the commonwealth over the past five years. The total cost to operate our office during that time was less than \$250 million, or roughly 1/14th of what we produced.

Ensuring compliance in the areas of Treasury responsibility is labor-intensive. That is true with unclaimed property, it is true with fiscal review, and it is true regarding the kind of analysis necessary to produce strong investment returns. Budgets that require Treasury to reduce staff have a damaging impact on commonwealth finances. They do not save money, they cost money, because reductions in our staff inevitably result in reductions in the revenue we generate from our activities.

We have about reached the limit of our ability to maintain our strong level of performance with fewer people. Despite a reduction in personnel of 130 since I took office – from 507 to 377 – we have managed to increase the financial benefit we produce for the commonwealth. We could, however, do even better if we had more resources to apply to some of those functions. Conversely, the commonwealth will almost certainly see lower revenue from Treasury activities if our budget requires us to eliminate any of our money-generating positions.

One very simple way to describe sustainable behavior is to say, "don't eat your seed corn." That is what budget cuts to Treasury will mean: if we cannot maintain our staff, we will not be able to make our contributions to commonwealth revenues.

And our seed kernels grow into bumper crops. For every \$58,000 we save in average salary and benefits through the departure of yet another fiscal review auditor or unclaimed property employee, we risk losing more than \$1 million per year in average revenue they generate. We also know of revenue opportunities we aren't currently reaching because we don't have the staff to address them.

So, as you consider the change to the dormancy period, please consider that it would be counterproductive to make changes to the escheat law in the hopes of bringing in more revenue while at the same time requiring Treasury to reduce the staff it needs to carry out functions that raise revenue.

Governor Corbett has proposed \$35.728 million in GGO support for Treasury next year, including \$3.5 million more than the current year's appropriation due to changes in the unclaimed property law. The proposed level funding looks good on paper, but in practical terms, it represents funding for fewer employees than Treasury had at the beginning of the current fiscal year because each year, Treasury faces higher personnel costs tied to collective bargaining agreements, union salary increases, and the increased costs for health care benefits, retirement contributions, and, to a lesser extent, unemployment compensation.

I should also provide some additional information on Treasury programs.

In Treasury's fiscal watchdog role, as I noted above, we prevented more than \$450 million in erroneous payments over the past five fiscal years. Looking at the most recently complete year, FY12-13, Treasury processed more than 30 million requested payments, and we stopped \$58 million in erroneous payments. Some \$36 million of that total came from the savings generated by our Personal Income Tax unit alone – enough to fund Treasury's entire GGO line item in the budget.

The Bureau of Unclaimed Property also had a very good calendar year 2013. Treasury returned \$111 million in unclaimed property to rightful owners or heirs in 2013, the highest yearly return amount in the five years I have been in office. Unclaimed property collections in 2013 also reached a new high for my years at Treasury, collecting \$281 million.

Of course, the third area where Treasury earns significant amounts of money for the commonwealth is investments. We continued to experience positive growth in our investments across each of the four primary "pools" we manage at Treasury: Pools 198 and 99, the Tuition Account Program, and OPEB, which stands for Other-Post Employment Benefits (covers non-

pension benefits that accrue to Commonwealth employees, such as life insurance, deferred compensation, and healthcare). Looking at the last calendar year, we gained nearly \$540 million in Treasury-managed funds. Looking at the three-year returns, we see strong returns net of fees, from 8.04% in Pool 198, to 10.00% for the Tuition Account Program Fund, and nearly 12.62% in OPEB.

Looking at total assets in the Tuition Account, or PA 529, Program, we ended 2013 at \$3.1 billion – the highest year-end amount in the program's history. This represents a 19% increase over the year-end figures for 2012. Of this total, \$1.6 billion was invested in the PA 529 Guaranteed Savings Plan and \$1.5 billion was saved in the Investment Plan.

The increase in assets was fueled by impressive growth in contributions, and this often resulted in great marketing and public education provided by Treasury staff. Last year, families saved over \$419.1 million with the program. That amount was about 11% greater than contributions made in 2012.

After facing a \$400 million deficit and only 70 percent of full funding in 2008, the GSP plan reach 100 percent funding last year. We are immensely proud of this achievement.

I would also again like to thank the Legislature for recognizing Treasury's urgent need to upgrade our woefully outdated information technology systems and for the appropriations you have provided over the past several years for IT modernization (roughly \$27.2 million). I am pleased with the progress we are making, and it appears we might be able to reduce our budget request even further. (We will be in a better position several months from now to identify accurately these anticipated cost savings.)

You can rest assured we have put those IT modernization funds to good use as we have begun a significant agency-wide transformation project, which I believe will serve as a model for how to undertake a project of this scale. To date, we have:

- * Migrated our payment operations off the old and vulnerable mainframe to a more efficient and secure client server, which has enabled us to reduce costs and improve the reliability of Treasury's processes.
- * Improved efficiencies by automating the process we used to post deposits from the Department of Revenue into Treasury's Automated Bookkeeping System, or TABS. This process eliminated the need to manually enter 90% of revenue deposits from paper into the Treasury computer system. By automating this process, Treasury was able to save three employees from doing this work and redeploy them to other critical functions.
- * Replaced outdated printing hardware to improve reliability.
- * Completed the two-part procurement process by which we selected Oracle PeopleSoft as our software solution for the ERP (enterprise resource planning) project.

In particular, I would like to update you on the flagship portion of this program, the implementation of an agency-wide Enterprise Resource Planning system. This is the primary project toward which we have directed the current year's appropriation of \$9 million. Having

procured Oracle's PeopleSoft program and CherryRoad Technologies as our implementation partner, we began this project in spring 2012. As part of the initial planning and information gathering stages of this effort, our project team met with different agency heads, as well as the comptrollers, IT representatives, and change agents from different departments to discuss the potential for changes, some of which are likely to be mutually beneficial. With that input, the team finalized the requirements and completed the design and development work. Our project team is working with agencies testing the systems for user acceptance.

Training will start in April. The project is scheduled to go live in the next several months. And we will be completing the ERP project phase 1 this year. After we go live, we will evaluate the additional functionalities of the modules and plan an upgrade to complete the final phase of the project.

After 18 months, the implementation team has completed 90% of the system testing associated with this project. We are also conducting User Acceptance tests, which will help us to confirm the business requirements.

In addition, we are focusing on change management, thorough communication, training, business process optimization, and ensuring technical and functional readiness. Any large project will have an impact on user productivity; we are working hard to make this a smooth transition.

Chairman Adolph, Chairman Markosek, and members of the Committee, as you know, Treasury operates a number of other programs in addition to the ones I have highlighted in my testimony today. I would be happy to discuss them with you at any time and answer any questions. We will continue our best efforts to generate positive returns on the public's investments, to drive up revenue from operations, and generally, to do all we can to improve the prosperity and economic security of all Pennsylvanians.

Again, I want to end where I began, by thanking you for bipartisan understanding and support.

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