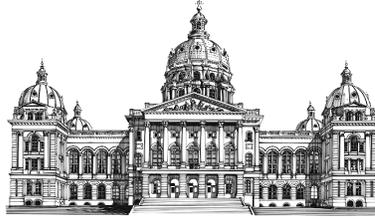

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Iowa Innovations Fund

ISSUE

This *Issue Review* provides an overview of the establishment of the Iowa Innovations Fund, and the Fund's operations and investment activities.

AFFECTED AGENCIES

Department of Management (DOM)

CODE AUTHORITY

Section 8.63, Code of Iowa

BACKGROUND

The Iowa Innovations Fund was created in SF 475 (State Financial Provisions Act) during the 1995 Legislative Session. Under the control of the Department of Management (DOM), the Fund was designed to stimulate and encourage innovation and entrepreneurship in State government by awarding repayable loans to State agencies. As required, the Director of the DOM established an eight-member State Innovations Fund Committee to review all requests and approve qualified loans.

Senate File 481 (FY 1996 Transportation and Capitals Appropriations Act) provided startup funding with a \$1.0 million appropriation from the Rebuild Iowa Infrastructure Fund (RIIF). During the 1999 Legislative Session, HF 782 (Miscellaneous Supplemental and Other Appropriations and Provisions Act) established a standing limited appropriation for the repayment of certain loans.

During the 2003 Legislative Session, HF 534 (Department of Administrative Services Act) extended the loan program to include enterprise loans. Enterprise loans are used to provide internal services to government.

AGENCY ELIGIBILITY AND LOAN PAYMENTS

A project loan may be funded if the Committee determines that an agency request will result in cost savings or added revenue to the General Fund. In order to be eligible, projects must not be able to be funded from the agency's operating budget without adversely affecting the agency's normal service levels, and projects may include, but are not limited to, the purchase of advanced technology, contracting for expert services, and acquisition of equipment or supplies.

Enterprise loans may be funded if the Committee determines that an agency or business unit has a viable business plan and the capability to use the loan to provide internal services to government. The enterprise is expected to receive payment for services from customers and use those payments to cover expenses, including repayment of the loan.

When considering applications for project loans, the Committee uses a return on investment concept that demonstrates how General Fund expenditures will be reduced or how General Fund revenues will increase. As an incentive to increase General Fund revenues, an agency may retain up to 50.0% of the savings realized in connection with a project loan. The Committee determines the amount retained. For enterprise loans, a business plan must demonstrate how the enterprise will meet customer needs, provide value to customers, and demonstrate financial viability.

In order for the Innovations Fund to be self-supporting, the Committee establishes repayment schedules for each loan. Agencies repay the loans with interest over a period not to exceed five years at a rate to be determined by the Committee.

If the DOM and the Department of Administrative Services certify that the savings from a proposed project will result in a net increase in the balance of the General Fund without a corresponding cost savings to the agency, and if the requesting agency meets all other eligibility requirements, the Committee may approve the loan for the project and not require repayment by the agency. In these cases, a standing unlimited appropriation in an amount sufficient to repay the loan is made from the General Fund.

Interests on moneys deposited into the Innovations Fund are credited to the Fund. Funds remaining in the Innovations Fund at the end of a fiscal year do not revert to the General Fund.

CURRENT SITUATION

The following loans have been provided from the Innovations Fund through FY 2003:

- The Department of Natural Resources (DNR) received loan disbursements of \$3,000 in FY 1996, \$122,000 in FY 1997, and \$25,000 in FY 1998 for a total loan of \$150,000. The loan disbursements were used to develop a comprehensive energy plan, update technical engineering analyses, provide project management, and monitor savings, for immediate assistance to State agencies in order to reduce funds spent for utility costs by capitalizing on energy efficiency improvements. The facilities were responsible for implementing the improvements. The loan was repaid with a portion of the savings from the implementation of the energy improvements. The DNR paid a total of \$171,000 into the Fund. The loan has not produced anything other than the payment of interest and principal for the Fund. The DNR budget has not benefited from any cost savings from the project. The term of the loan expired on July 1, 2000.
- The Department of Revenue received \$275,000 in FY 1997. The loan allowed for the upgrade of automation environment for field audit, collections, and taxpayer services staff by upgrading

network capabilities and security systems to permit remote site access. The loan was repaid from the increase in revenue collections. The Department has paid a total of \$5.7 million into the Fund. This includes \$313,000 in principal and interest, and \$5.3 million from increased revenue collections. The Department continues to retain 50.0% of the increased revenue collections and the Fund continues to receive 50.0% of the increased revenue collections although the loan expired on February 1, 2000. An agreement was reached between the Department and the DOM, in August 1997, to extend the distribution of savings through June 1, 2001. In September 2000, an agreement was reached to indefinitely extend the distribution of savings.

- The Department of General Services received \$292,000 in FY 1997. The loan was used to acquire specialized computer equipment and software to enable the electronic verification of addresses and to generate correct zip and postal codes thereby reducing postal costs. The Department has paid a total of \$348,000 into the Fund. This includes the payment of \$324,000 in principal and interest, and \$23,000 in postal costs savings that was paid after the expiration of the loan on June 15, 2000.
- The Department of Inspections and Appeals received loan disbursements of \$75,000 in FY 1998, \$161,000 in FY 1999, \$150,000 in FY 2000, and \$43,000 in FY 2001 for a total loan of \$429,000. The loan disbursements were used to contract with private contractors to perform front-end investigation of welfare applications and to handle special collection activities thereby reducing State operating costs and increasing incidence of fraud identified for recovery. The Department has paid \$51,000 in principal and interest into the Fund. The DOM does not anticipate receiving any additional funds from the Department of Inspections and Appeals. The Department of Human Services (DHS) and the federal government realized the savings that resulted from the front- end investigation of welfare payments. The Department of Inspections and Appeals was unable to enlist the cooperation of the DHS or the federal government in repayment of the loan, and the Department of Inspections and Appeals did not have sufficient financial resources within its operating budget to repay the loan. The term of the loan expired on March 1, 2001.
- The Iowa Communications Network (ICN) received \$77,000 in FY 1998, and \$34,000 in FY 1999 for a total loan of \$111,000. The loans were used to simplify, improve, and make the ICN's customer billings process more cost effective so all billings activities could be handled in-house. The ICN has paid a total of \$135,000 into the Fund. This includes \$117,000 in principal and interest and \$19,000 in cost savings achieved during the term of the loan. The term of the loan expired on December 31, 1999.
- The Department of General Services received \$300,000 in FY 2000. The loan was used to purchase and install a fleet management information system designed to enhance data and decision making, improve fleet performance, reduce duplication within the accounting system, and reduce the operating cost of the fleet. The Department has paid a total of \$260,000 in principal and interest into the Fund. The term of the loan expires on January 1, 2004.
- The Treasurer of State received \$599,000 in FY 2001. The loan was used to provide online access to the College Savings Iowa Program and reduce staff and support costs. The Office has paid a total of \$345,000 in principal and interest into the Fund. The term of the loan expires on November 1, 2007.
- The Department of Personnel received \$330,000 in FY 2001. The loan was used to design and implement a Deferred Compensation Match Program. The savings were to result from the State not having to provide Social Security or Medicare withholding payments for the State match.

The Department has paid a total of \$329,000 in principal and interest into the Fund. The term of the loan expires on December 31, 2003.

- The Department of Management (DOM) received \$277,000 in FY 2002. The loan was used to enable the State to increase the utilization of grants by implementing an enterprise-wide system of identifying, tracking, and sharing funding opportunities through the Grants Enterprise Management System (GEMS). The loan was to assist in achieving an increase in the State's federal indirect cost recovery. The first payment is due in FY 2004. The term of the loan expires on January 10, 2007.
- The Department of Revenue received \$103,375 in FY 2003. The loan was used to convert over 55,000 businesses from monthly filing status to less frequent filing including quarterly and annual filing. The savings were to result from a reduction in the cost of handling communications submitted with the monthly deposits. The Department was not to begin payments until FY 2004. The term of the loan expires on October 1, 2007.

ALTERNATIVES

- Section 8.63(5), Code of Iowa, provides that an agency may retain up to 50.0% of savings realized in connection with a project loan from the Innovations Fund. The Legislature may want to consider if agencies should retain 50.0% of the savings beyond the term of the loan.
- Section 8.63(3), Code of Iowa, provides that a loan can be funded if the Innovations Fund Committee determines that an agency request would result in cost savings or additional revenue for the General Fund. The Legislature may want to consider if the Fund should retain the 50.0% of the savings not retained by an agency.

BUDGET IMPACT

The Fund had a balance of \$2.9 million at the close of FY 2003. Since the establishment of the Fund in FY 1996, \$545,000 in interest earned on the Fund balance has remained in the Fund. The Fund has outstanding loans in the principal amount of \$610,000 as of October 21, 2003, not including the loan to the Department of Inspections and Appeals that was forgiven due to the Department's inability to make payments.

Since the establishment of the Fund in FY 1996, a total of \$11.2 million in identified savings has been divided evenly between the agencies and the Fund.

The Fund transferred \$300,000 in FY 2000 and \$400,000 in FY 2003 to the General Fund. In FY 2001, the Department of Human Rights received an appropriation of \$2.3 million from the Fund to provide payments under the Low-Income Home Energy Assistance Program (LIHEAP).

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