AGENDA
ASSEMBLY BUDGET SUBCOMMITTEE NO. 4
ON STATE ADMINISTRATION

Assemblymember Rudy Bermudez, Chair

WEDNESDAY, APRIL 6, 2005, 1:30 PM
STATE CAPITOL, ROOM 437

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ITEMS TO BE HEARD

ITEM 0390 CONTRIBUTIONS TO JUDGES' RETIREMENT

The Judges' Retirement System provided retirement, disability, and death benefits to participants based upon age, years of service and compensation of active judges. This system is not based upon an actuarially funded model and therefore augmentations are base upon primarily on the current year obligations (pay as you go). Despite statutory contributions by judges and the State based upon a percentage of salary, the state is estimated to fund additional liabilities for this system pursuant to Government Code section 75101.

The Judges' Retirement System II was established in 1994 and provides retirement coverage for all judges appointed on or after November 9, 1994. Contributions to this system by the judges are fixed and the employer's contribution is adjusted on an actuarial basis.

ISSUE 1: STATE CONTRIBUTIONS

For the Budget Year the Administration estimates State Contributions of $1.15 million in support of Supreme and Appellate Court Judge obligations and $$109.2 million in support of Superior Court Judges. Final rates for the 2005-06 have not been established but are expected by the May Revision.

ITEM 0855 CALIFORNIA GAMBLING CONTROL COMMISSION

The California Gambling Control Commission has jurisdiction over the operation, concentration, and supervision of gaming entities (card rooms and tribal casinos) and over persons that own or operate those establishments. The Commission acts as a regulatory body over gambling activities by setting policy, establishing regulations, issuing licenses, and serving as an appellate body for licensing denials. The Commission exercises its authority to restrict the issuance of licenses and permits to those that would negatively affect the public health and safety of the gaming industry.

The Commission also acts as the trustee for the Special Distribution and Revenue Sharing Trust Funds which collects funds from gaming tribes, oversees the funding of the state's gambling addiction programs, distributes the funds to non-gaming tribes, state oversees tribal gaming, allocates funds to local governments and other statutory requirements.

ISSUE 1: WORKLOAD INCREASE

The Commission has requested $4.8 million (and 45.5 positions) in support of additional workload associated with the new and amended (Post 1999 agreements) tribal gaming contracts successfully negotiated last year. This request includes funding for 15 auditors to audit the financial records of tribes to verify that the appropriate amounts are remitted to the state; 13 gaming testing laboratory and filed staff to test slot machines and gaming software; 9 licensing and investigative staff to review licenses for key employees and vendors; and 7.5 positions to provide administrative support. The administration proposes the use of special distribution funds in support of this additional work.

The Legislative Analyst's Office has recommended the rejection of this proposal on the basis that the Administration has provided little justification as to what problems would be addressed. For instance, 7 of the auditing staff were requested to audit payments to the Special Distribution Fund. As the post 1999 agreements do not include payments to the SDF, the nexus between the new agreements and the Commission's request is not clear.

In an April 1 Finance Letter the Administration has proposed a reduced augmentation of $2.25 million (22.3 positions) that include 6 special consultants. The subcommittee may want to ask the following of the Commission related to this request:

- What would be the duties of the proposed positions (including the special consultant positions)?

- What is the estimated workload to be addressed by the augmentation? How would this workload complement the work performed by the rest of the Commission's workload?

- What are the workload standards associated with each position?

- What is the nexus between the duties and responsibilities of the positions requested and the post 1999 compact agreements? Is there any workload addressed with regards the 1999 agreements? How was the determination made to divide the funding and positions between the Special Distribution Fund and the Revenue Sharing Fund?

- Does the Commission currently have any backlog in the approval process regarding applications by owners, key players, or vendors to card rooms or tribal casinos?

- What is the average turnaround time for the processing of applications for owners, key employees, or vendors?

- What analysis has the Commission performed to determine whether additional resources to the Department of Justice, Division of Gambling would improve the overall function of the Commission?

ISSUE 2: FINANCE LETTER – FIRE MARSHALL INSPECTION REIMBURSEMENT

In an April 1, Finance Letter, the Commission requests $276,000 from the Special Distributions Fund to reimburse the State Fire Marshall for conducting building code and fire safety inspection verification of tribal casinos. While it may be appropriate for public buildings to be safe from structural failure and fire, the subcommittee may want to ask the Commission:

- What is the nature of the inspections proposed?
- Under what authority are the inspections authorized? Do the owners of the casinos have to provide consent?
- How frequently will the inspections be performed?
- Under what conditions will any follow-ups inspections be performed? Who will pay for them?
- What does the Commission intend to do if the inspections identify sub-standard conditions that are not being resolved?
- Does the Commission have an agreement with the State Fire Marshall to perform the inspections? Why doesn't the State Fire Marshall directly perform the inspections rather than go through the Commission?

ITEM 1900 PUBLIC EMPLOYEES' RETIREMENT SYSTEM

The California Public Employees' Retirement System (Cal PERS) administers the retirement and health benefit programs for more than 1.4 million active employees and retirees of state and local agencies. Benefits under the system include: retirement; disability any survivor's benefits. CalPERS also administers a long-term care insurance program for members and eligible individuals.

ISSUE 1: PENSION REFORM

In the Governor's State of the State Address, the Governor proposes a change from a defined benefit retirement plan to a defined contribution program. Under the existing defined benefit program, contributions from the employee and the employer fund a program that provides the employee a fixed monthly payment upon retirement based upon the member's age, final salary and years of service. The state program also provides disability and death survivor benefits to eligible beneficiaries. The California Public Employees' Retirement System has the responsibility for the collection of contributions from the employer, employee and maximize the return on these collections using prudent investment techniques in order to provide adequate funds to meet the obligations of the beneficiaries. Should the liabilities under the system increase, the employer's contribution would increase. As the liabilities decrease, the employer has the option to reduce the level of contributions to reflect the actuarial obligations for that period, or continue the existing level of contributions in order to mitigate shortfalls in future years. Under a defined contribution program, benefits to the retiree are not guaranteed and are limited to the contributions of the employee and the associated investment earnings. Under some variations of a defined contribution plan, employers may provide some or all of the contributions into the plan.

Three legislative proposals relate to a change from defined benefit to defined contribution plans. ACA 5 (December 6, 2004 version) would, effective July 1, 2007, prohibit new public agency employees from participating in a defined benefit pension program, and would only allow the enrollment in a defined contribution plan. Under this proposal, employers would be prohibited from contributing to the defined contribution plan in excess of an unspecified amount. Existing employees would be able to move the present value of his/her interest in the defined benefit program to a defined contribution program.

The subcommittee may want to ask the Administration the following related to ACA 5:

- Does ACA 5 represent the Administration's proposal to transition from a defined benefit to defined contribution plan?

- How does ACA 5 define a new employee for purposes of the July 1, 2007 effective date? How would this address someone who returns from a leave of absence?

- Does ACA 5 specifically have provisions to provide reciprocity for persons transfer from one retirement system (e.g. State Teachers Retirement, University of California, or 1937 Act county retirement systems)

- What type of disability, and survivor benefits does ACA 5 specifically provide?

- How does ACA 5 calculate the present value of the employee's contribution for transfer to a defined contribution plan? Will this reflect the actual returns of CalPERS or an average rate? Does ACA 5 define the member's interest as the present value of employee's actuarial liability at the time of departure? Does that include the employer's contribution? Investment income on the employer's contribution? Unfunded liabilities?

- Does the present value include contributions where the employer assumed the actuarial liability in lieu of payment by the employee?

- How many employees that are currently involved in the defined benefit program are expected to convert to a defined contribution program?

- What factors will the Administration consider when determining the limit on employer contributions for the defined contribution programs?

- What is the Administration's estimate of the state costs to PERS on closing the fund to new employees? What impact will the closure of the defined benefit plan have on the employer contribution rates assuming that the investment rates of return do not change and there is no other changes in the actuarial assumptions regarding the remaining employees?

- How does closing the defined benefit program affect the investment rate of return for the remaining life of the fund?

- How would closing the defined benefit program affect the fund's plan to eliminate the existing unfunded liability? Does the Administration propose to liquidate the unfunded liability immediately in 2005-06 to minimize the cost of interest associated with the liquidation? What would that cost be?

- Which agency would administer the defined contribution program? What type of investment options would be available under ACA 5 as compared to the current CalPERS portfolio?

- Does ACA 5 provide any fiscal relief to local governments that may experience cash flow problems associated with the closing of a defined benefit plan?

ACA X1 (January 6, 2005 version) would also limit new employees to public entities hired after July 1, 2007 to a defined contribution plan. It would also allow employees to take the net present value of his/her interest and place it in a defined contribution program. This proposal does not address limits on employer contributions under the defined contribution plan.

The subcommittee may want to ask the Administration the following related to ACA X1:

- Does ACA X1 represent the Administration's proposal to transition from a defined benefit to defined contribution plan?

- How does ACA X1 define a new employee for purposes of the July 1, 2007 effective date? How would this address someone who returns from a leave of absence?

- Does ACA X1 specifically have provisions to provide reciprocity for persons transfer from one retirement system (e.g. State Teachers Retirement, University of California, or 1937 Act counties)

- What type of disability, and survivor benefits does ACA X1 specifically provide?

- How does ACA X1 calculate the present value of the employee's contribution for transfer to a defined contribution plan? Will this reflect the actual returns of CalPERS or an average rate? Does ACA X1 define the member's interest as the present value of employee's actuarial liability at the time of departure? Does that include the employer's contribution? Investment income on the employer's contribution? Unfunded liabilities?

- Does the present value include contributions where the employer assumed the actuarial liability in lieu of payment by the employee?

- How many employees that are currently involved in the defined benefit program are expected to convert to a defined contribution program?

- What is the Administration's estimate of the state costs to PERS on closing the fund to new employees? What impact will the closure of the defined benefit plan have on the employer contribution rates assuming that the investment rates of return do not change and there is no other changes in the actuarial assumptions regarding the remaining employees?

- How does closing the defined benefit program affect the investment rate of return for the remaining life of the fund?

- How would closing the defined benefit program affect the fund's plan to eliminate the existing unfunded liability? Does the Administration propose to liquidate the unfunded liability in 2005-06 to minimize the cost of interest associated with the liquidation? What would that cost be?

- Which agency would administer the defined contribution program? What type of investment options would be available under ACA X1 as compared to the current CalPERS portfolio?

- Does ACA X1 provide any fiscal relief to local governments that may experience cash flow problems associated with the closing of a defined benefit plan?

AB 511(February 16, 2005 version) would limit employer contributions to a defined contribution plan to 6 percent for most employees and 9 percent for peace officer/firefighters. If those employees were not a participant of the Social Security system, the maximum employer contributions would be 3 percent and 4.5 percent higher respectively. This bill would require some matching contributions by employees to qualify for the employer contributions.

The subcommittee may want to seek the following information from the Administration:

- Does AB 511 represent the Administration proposal to transition from a defined benefit plan to a defined contribution plan?

- Does the Administration propose to contribute the maximum amount of employer contribution as identified in AB 511?

- Has the Administration estimated the cost/savings associated with this proposal? If so, is that information available to this subcommittee?

The subcommittee may want to determine the fiscal impact in future years of the Administration's proposal.

ISSUE 2: INCREASED EMPLOYEE CONTRIBUTION

The Administration proposes to evenly share the cost of retirement between employers and employees. Currently, employees pay a fixed percentage of salary toward the total retirement costs. Recently, the State agreed to assume liability for the employee's share of costs for selective bargaining units in lieu of actual increases in base salary. For general administrative workers, the employee's of retirement contributions are approximately 5 percent of salary. While the final rates have not been determined for 2005-06, the Governor's Budget proposes an employer contribution rate of 17.022 percent of the employee's salary. The employer and employee costs include the normal costs (prospective costs associated with the benefits guaranteed under the defined benefit programs) and the amortization of unfunded liabilities (unfunded prior costs that could be from the deferral of prior year costs, or the amortization of benefits associated with prior periods) Under the Administration's proposal, employees would now contribute approximately 11 percent of salary, an increase of 6 percent. The Administration has estimated savings of $208 million from this proposal. The savings assumes that employees will participate in this program as soon as the associated labor bargaining agreements expire. It is not clear if the Administration proposes to give up the ability to temporarily suspend contributions or re-amortize unfunded liabilities as both the employer and employee would participate in any rate changes as opposed to current policy of fixing the employee's contribution while the employer receives the entire benefit from any reduction in the total liability in any particular year.

The subcommittee may want to seek the following information from the Administration:

- Can the Administration provide its savings estimate by collective bargaining unit?

- Why didn't the Administration propose to share only the normal costs rather than include the amortization of costs that the Administration could have liquidated in prior periods (excluding adjustments due to changes in the member's demographic attributes)?

- Does the Administration propose to give up options to defer payments in the future that would increase the total costs due to imputed rate of return on assets of 7.75 percent and therefore increase the costs to both the employee and the State?

- Does the Administration propose to give employees additional influence in funding of the pension obligations as it proposes to be equal partners in the cost to support the system?

- What does the Administration propose to exchange for the increased employee contribution?

ISSUE 3: TRANSFER OF EXISTING EMPLOYEES TO DEFINED CONTRIBUTION PLANS

The Administration proposes to allow employees to leave the defined benefit plan. Subsequent to that decision, the employee would receive what had previously been his/her contribution (generally 5 percent of salary). In addition, the State would contribute 50 percent of the normal retirement cost to the employee (estimated to be approximately 5 percent of salary) . Since the normal cost would vary from year to year, it is not expected that this payment would be included as part of the salary base. This proposal is estimated to save $90 million in the Budget Year.

The subcommittee may want to seek the following information from the Administration:

- How many employees are estimated to leave the defined benefit program? What is the average savings per employee? What does the Administration estimate the impact of this proposal in 2006-07 and future years?

- Does the "normal cost" include just the employer's share? Is there any part of the employee's contribution that is part of the normal cost?

- Would the employee that leaves the defined benefit program be able to withdraw funds contributed into that system? How would the amount be determined? Would the Administration propose that the employee be allowed to take out the present value of the employee's interest in the retirement system as specified in ACA 5 and ACA X1?

ITEM 8120 COMMISSION ON PEACE OFFICER STANDARDS AND TRAINING

The Commission on Peace Officer Standards and Training is responsible for setting the standards for law enforcement officers in California. It establishes minimum selection and training standards for these officers. It also provides financial assistance to local agencies in order to facilitate the training of law enforcement officers. The Commission's budget is proposed to increase by $6 million in the Budget Year. The majority of that increase is related to the funding for state mandated programs (Domestic Violence Arrest Policies and Standards Chapter 246, Statutes of 1995) of $4.5 million and the increase of training funds by $1.5 million.

ISSUE 1: RESTORATION OF PRIOR YEAR REDUCTIONS

The Commission requests $721,000 from the Peace Officers' Training Fund and 6 positions in the budget year. This request to upgrade current curriculum represents the partial restoration of unallocated reductions resulting in the loss of 20 positions in the 2002-03 and 2003-04 fiscal years.

ITEM 8380 DEPARTMENT OF PERSONNEL ADMINISTRATION

The Department of Personnel Administration is the Administration's primary personnel policy advisor. The department represents the Governor as the employer in matters of employee- employer relations, including salaries, benefits, position classification, and training. The Department also administers the tax deferred IRC Section 401k and 457 programs.

ISSUE 1: ALTERNATE RETIREMENT PROGRAM – ADDITIONAL FUNDING

The Budget Act of 2004 (SB 1105) amended sections of the Government Code that establish an Alternate Retirement Program for new state employees. Effective August 11, 2004, during the first 24 months of employment neither the employer nor the employee make contributions to the California Public Employees' Retirement System. (CalPERS). Instead, the employee will contribute a portion of their salary to the Alternate Retirement Program. These funds would be placed in an IRC Section 401(a) account. The employer will not make a contribution to this plan, thus saving approximately 17 percent of its salary costs for the average miscellaneous employee. At the end of the 24-month period, the employee would be enrolled in the PERS system that would include both employer and employee contributions The ARP program is to be administered by the Department of Personnel Administration. DPA's Savings Plus Program is designated to implement this program on behalf of the department.

The Governor's Budget proposes $446,000 in the current year and $536,000 in 2005-06 in support of this program. The Administration estimates savings of $85.5 million from this program in the Budget Year.

ISSUE 2: FURLOUGH OF STATE EMPLOYEES

The Administration proposes giving the Governor the authority to furlough state employees up to 5 days a year. Public safety and 24 hour care employees would be exempt. The Governor would be able to trigger the furloughs based upon: a General Fund reserve of less than 3 percent; General Fund reserves of less than that determined by the May Revision for the period between May 1 through September 30; or notification to the Legislature that there will not be a transfer to the Budget Stabilization Account pursuant to Proposition 58. The Administration estimates a General Fund savings of $60 million ($109 million all funds) associated with a 5-day furlough.

Should the Administration propose the maximum 5-day furlough at the beginning of the year, an employee could take a day off approximately every other month. This would result in an average reduction in salary of approximately 2 percent over the year. If the 5 days of furlough were taken in one month this could result in a reduction of salary of nearly 24 percent in a 21-day month.

The subcommittee may want to seek information regarding the following:

- What criteria will the Administration use to determine whether it will propose a 1 day, 2 day, 3 day, 4 day or 5 day furlough?
- Is the 5-day furlough authority to be designated by fiscal year? Calendar year? Any 12-month period? Would it be possible to have more than 5 days of furlough in any 12-month period?
- How does the Administration propose to provide the great number of months (and greatest flexibility) for the employee to take the furlough days?
- Does the Administration propose to allow the employee to take the days of at their discretion or will the department identify the furlough days?
- Does the Administration propose any strategies for mitigating the fiscal impact of a furlough plan in any particular month?
- Will the Administration implement any policies to ensure that employees actually take off their furlough days?

ISSUE 3: REVISED OVERTIME CALCULATIONS

The Administration proposed to exclude the use of time off because of holidays, sick leave, vacation, annual leave, compensating time off or other paid time off, when calculating time worked for determining overtime pay, even if the time off or the extra working hours were not voluntary. The Administration estimates General Fund saving of $20 million ($36.4 million all funds).

ISSUE 4: ELIMINATION OF STATE HOLIDAYS

The Administration proposes the elimination of two state holidays. The Administration estimates the General Fund savings in 2005-06 and 2006-07 would be $1.7 million ($3.1 million all funds). General Fund saving in 2007-08 is estimated at $9.7 million ($17.6 million all funds). The increase is attributed to the expiration of collective bargaining agreements for peace officers and firefighters.

ISSUE 5: LIMITED ACCRUAL OF VACATION

Current regulations provide for employees to earn vacation or annual leave time on a monthly basis. The amount of monthly accrual is dependant upon the years of service. Amounts of leave that are not used in a particular year can be rolled over to a future year. Outstanding balances of leave are reimbursable to the employee upon separation from employment. The state has established upper limits for the accrual of leave time. If the employee's leave balance is expected to exceed the established limits, he/she is required to develop, in conjunction with his/her supervisor, a plan for using enough leave time so that the year-end balance of leave credits will be below the limits established by the state. The Administration proposes to limit the accrual of leave time by employees that reach the limit of 640 hours. This would limit the fiscal liability of the department upon separation of the employee (e.g. retirement).

The accrual of leave balances in excess of 640 hours would appear to be in violation of the directives to develop a plan to reduce leave balances below the limit. Under these conditions, it would appear that the management has not properly implemented the plan to use excess leave time, or it was the intent of the agency to allow the employee to use these leave credits but would not allow the employee to actually take the time necessary to comply with the provisions of the plan. In either case, the failure to bring the employee's leave balances below the limit was under the control of the departmental management.

ITEM 9650 HEALTH AND DENTAL BENEFITS FOR ANNUITANTS

This item funds the payment of health and dental insurance premiums for annuitants. While the appropriation from this item is made from the General Fund, approximately one third of the total costs are recovered from special funds through pro rata (allocation of administrative costs) charges.

ISSUE 1: HEALTH CARE PREMIUM RATES

The Administration proposes $861 million in support of annuitant health and dental premium benefits. This is $65 million higher than in the current year. This reflects enrollment growth of approximately 3.5 percent and rate increases of 5 percent. Final rates for calendar year 2006 have not been determined.

ISSUE 2: FEDERAL PRESCRIPTION DRUG PROGRAM

The Administration's estimates for this item includes offsetting savings of $34.5 million for one-half year associated with the implementation of the Medicare Part D prescription drug program that becomes effective January 1, 2006. For retiree programs that provide coverage that exceed the coverage in Part D, the federal government should subsidize a portion of the prescription costs. The estimated value of this subsidy is $611 per Medicare enrollee for 2006.

The Public Employees' Retirement System (CalPERS) has expressed concern that it may be premature to adopt this reduction to premiums.

The subcommittee may want to seek updated information from the Administration and CalPERS regarding the level of estimated savings resulting from the implementation of the Medicare Part D program.