AGENDA

ASSEMBLY BUDGET SUBCOMMITTEE NO. 4 ON STATE ADMNISTRATION

ASSEMBLYMEMBER JOAN BUCHANAN, CHAIR

PART 1

WEDNESDAY, MARCH 7, 2012
1:30 A.M. - STATE CAPITOL ROOM 437

CONSENT CALENDAR

ITEMS TO BE HEARD

CONSENT CALENDAR

1920 CALIFORNIA PUBLIC EMPLOYEES RETIREMENT SYSTEM

ISSUE 1: BUDGET BILL LANGUAGE—EXPENDITURES FOR EXTERNAL ADVISORS REPORT

The California Public Employees Retirement Fund (CalPERS) has approved the use of external investment advisors to manage a portion of its investment portfolio. CalPERS selects managers and advisors based on experience in investing in certain asset classes. When external managers are selected, fees are negotiated in an effort to ensure that CalPERS receives an appropriate return on the dollars invested. CalPERS pays fees to managers based on a formula that incorporates assets under management, committed capital, and in some cases, performance of the portfolio.

Pursuant to recurring Section 2 of Item 1900-002-0835 of the Annual Budget Act, CalPERS is to provide two reports to the Joint Legislative Budget Committee (JLBC), the Legislature's fiscal committees, and Legislative Counsel by January 10 of each year regarding the nature of the expenditures for these external contracts. The reports provide a summary and comparison of externally managed portfolios, a description of actions to be taken to achieve greater returns, and a listing of advisor contracts in effect and approved for the future. The reports taken together provide final expenditures for previous fiscal year, revisions regarding the current year expenditures, and proposed expenditures for the next fiscal year. CalPERS indicates that the reports are duplicative of what also is presented in its Comprehensive Annual Financial Report (CAFR). The CAFRs are available in November or December prior to the January 10 due date for the submission of the external investment advisors report to the Legislature. The CAFR for the most recent year ending June 30, 2011, is dated December 31, 2011.

CalPERS has requested that given the redundancy of the reporting, the BBL for the external investment advisors report to the Legislature be eliminated.

ISSUE 2: BUDGET BILL LANGUAGE—QUARTERLY BUDGET AND EXPENDITURES REPORT

CalPERS is required through budget bill language to report to the Legislature on a quarterly and annual basis expenditures and performance workload data in sufficient detail to be useful for legislative oversight purposes and to sustain a thorough ongoing review of the retirement system. This requirement is contained in Item 1900-015-0815, Section 1 of the budget act. Given that the final report encompasses quarterly data, the quarterly reports appear to represent a redundant reporting requirement

CalPERS has requested that the language be modified to remove the quarterly reporting but leave the annual reporting requirement in place.

1920 CALIFORNIA STATE TEACHERS RETIREMENT SYSTEM

ISSUE 1: BUDGET BILL LANGUAGE—EXPENDITURES FOR EXTERNAL ADVISORS REPORT

As of June 30, 2011, the CalSTRS portfolio held $155.5 billion in investments. CalSTRS internally manages 33 percent of these assets and retains external managers for the remaining 67 percent. CalSTRS hires firms to manage discrete portions of the portfolio according to terms set forth under personal service contracts. Pursuant to recurring Section 2 of Item 1920-002-0835 of the Annual Budget Act, CalSTRS is to provide two reports to the JLBC, the Legislature's fiscal committees, and Legislative Counsel by January 10 of each year regarding the nature of the expenditures for these external contracts.

The reports provide a summary and comparison of externally managed portfolios, a description of actions to be taken to achieve greater returns, and a listing of advisor contracts in effect and approved for the future. The reports taken together provide final expenditures for previous fiscal year, revisions regarding the current year expenditures, and proposed expenditures for the next fiscal year. CalSTRS indicates that the reports are duplicative of what also is presented in the agency's Comprehensive Annual Financial Report (CAFR). The CAFRs are available in November or December prior to the January 10 due date for the submission of the external investment advisors report to the Legislature. The CAFR for the most recent year ending June 30, 2011 is dated December 20, 2011.

CalSTRS has requested that given the redundancy of the reporting, the BBL for the external investment advisors report to the Legislature be eliminated.

ITEMS TO BE HEARD

1900 / CS 4.21 CALIFORNIA PUBLIC EMPLOYEES RETIREMENT SYSTEM

The California Public Employees Retirement System (CalPERS) administers the retirement benefits for state and local agency employees. CalPERS also provides health benefits for retired and active employees. CalPERS is governed by a Board of Administration that has authority over the administration of the retirement system. CalPERS receives funding from non-General Fund sources for administrative costs, largely from retirement fund resources themselves. The budget state operations proposed for 2012-13 are $333.9 million and 2,434.6 positions compared to $334.0 million and 2,466.6 positions in the current year. The workforce cap goals will be met through a reduction in the Public Employees Contingency Reserve Fund of $319,000. CalPERs will be placed in the new Governmental Operations Agency (GOA) under the Governor's reorganization plan.

2012-13 Governor's Budget

Fund Source (millions)	2010-11 Actual	2011-12 Projected	2012-13 Proposed	BY to CY Change	% Change
General Fund	$0.0	$0.0	$0.0	$0.0	0.0
Public Employees' Retirement Fund	16,306.9	17,707.3	18,966.8	1,259.5	7.1
Public Employees' Health Care Fund	1,783.0	1,986.4	2,219.9	233.5	11.8
Other Retirement Funds	102.2	113.3	117.5	4.2	3.7
Total Expenditure	$18,192.1	$19,807.0	$21,304.2	1,497.2	7.6
Positions	2,291.7	2,466.6	2,434.6	-32.0	-1.3

Budget year payments for CalPERS for the funding of retirement benefits will be $1.8 billion General Fund, $911 million special funds, and $403 million from non-governmental cost funds. In addition, the state payment to California State University for retirement costs will total $404 million General Fund; in the past, the state has paid these costs directly to CalPERS. These non-add amounts are not reflected in the figure above. In addition, the General Fund supports health benefits payments for retired public employees requiring funding of roughly $1.7 billion in 2012-13.

The Governor has called for long-term changes to pensions to ensure "continued viability of the system." In October of last year, the Governor put forth a 12-point plan to put the state on a "more sustainable path" for providing retirement benefits. The plan includes provisions to: equal sharing of normal pension costs between employers and employees; place new employees in a "hybrid" risk sharing pension plan; increase retirement ages for new employees; calculate benefits based on regular, recurring pay; limit post-retirement employment; require felons to forfeit pension benefits; prohibit retroactive pension benefits; prohibit pension payment holidays; prohibit purchase of "airtime"; change the make-up of the CalPERS Board; and require new employees to wait longer to vest for retiree health benefits and bear a larger share of those costs. The Governor's proposal is currently before the Conference Committee on Public Employee Pensions.

ISSUE 1: CALPERS HEALTH BENEFITS PROGRAM

As part of the 2011-12 budget agreement, Control Section 4.21 stipulated the following:

> *SEC. 4.21. The Public Employees' Retirement System (PERS) will achieve a one-time savings of $80,000,000 of General Fund moneys and $35,704,000 of other funds' moneys in the 2011–12 Health Benefits Program. Beginning in the 2012–13 fiscal year, PERS will achieve an equivalent amount of ongoing savings in the Health Benefits Program based on the core health plan option or other cost saving measures, or both. Before October 10, 2011, PERS shall notify the Joint Legislative Budget Committee, and the Director of Finance that these savings have been achieved and the source of these savings for the 2011–12 fiscal year.*

CalPERS notified the Joint Legislative Budget Committee (JLBC) in October 2011 that although it achieved General Fund savings in the 2012 calendar year, it fell short of the 2011-12 state fiscal year target, in part because of the timing of the rate setting process. In a November 2011 follow-up letter adding additional information, CalPERS indicated that for 2011-12 there would be ongoing General Fund savings of $20 million and one-time General Fund savings of $42.6 million, for a total of $62.6 million. The one-time savings include reinsurance programs, risk-sharing agreements, and excess self-funded plan reserves. One-time savings do not result in reduced baseline expenditures. DOF has indicated that for budget purposes, of the $62.6 million General Fund, $46.8 million can be scored as savings during the current year.

As part of the Governor's Budget, Control Section 4.21 stipulates the following:

> *SEC. 4.21. (a) The Public Employees' Retirement System (PERS) will achieve savings of $45,383,000 of General Fund moneys and $22,450,000 of other funds' moneys in the 2012–13 Health Benefits Program and PERS will achieve an equivalent amount of ongoing savings based on the core health plan option or other cost saving measures, or both. Before October 10, 2012, PERS shall notify the Joint Legislative Budget Committee, and the Director of Finance that these savings have been achieved and the source of these savings for the 2012–13 fiscal year. (b) Notwithstanding any other provision of law, the Director of Finance shall adjust items 9650 and 9800 pursuant to the health rates adopted by the Board of Administration of the California Public Employees' Retirement System for the 2012–13 fiscal year, as appropriate.*

STAFF COMMENT / QUESTIONS

The expected reduction in on-going General Fund savings in 2012-13 are substantially less than that included in the 2011-12 budget agreement. The Committee may want to be informed of the changes in circumstances that have led to savings reduction. The exact nature of the one-time savings was not specifically identified in the letter to the JLBC and the Committee may want these explained in order to appreciate the impact of the program. The savings proposed for 2012-13 are roughly the same as the one-time savings achieved in 2011-12, so CalPERS will need to identify completely new sources of one-time savings or additional . The Committee may request this information be provided to them. In addition, the Committee may inquire regarding the status of the core health plan option and the other possible sources of on-going savings. As noted above, the on-going savings achievable in the budget year are substantially less than the amount of on-going savings called for in the out-years in the 2011-12 budget agreement. LAO has indicated that it is premature to assume any savings from the health care premiums until further along in the process; the formal negotiation process does not begin until April.

ISSUE 2: BUDGET BILL LANGUAGE—ANNUAL HEALTH PREMIUMS REPORT

CalPERS is required to submit a report regarding the adoption of annual health premium increases or decreases by the CalPERS Board to the JLBC, the chairpersons of the committees and subcommittees in the Assembly and the Senate that consider CalPERS' budget, the Controller, Director of Finance, and the Legislative Analyst's Office. The report is due within 100 days of the adoption of health premium increases or decreases and is required to describe the methods it employed to moderate annual increases in premiums when taking action. The report is also required to include a discussion of actions it proposes to take to reduce premiums during years when increases are in excess of the amounts anticipated.

CalPERS has indicated that the reporting requirement is redundant, since such information is already included in several other documents, including in the rate information provided to the CalPERS Board of Administration each June and presented in the statistical section of the CalPERS Comprehensive Annual Financial Report (CAFR) required by the Government Code. In addition, CalPERS notes that representatives of the Legislature sit on the CalPERS board and have access to additional material, if needed. The CAFR is available late fall or early winter for the year ending the prior June 30.

STAFF COMMENT / QUESTIONS

Health care premium costs is an ongoing concern that requires sufficient and timely legislative oversight. While the information required in the report is also made available through two other written reports, the information may not be readily available in a format that facilitates legislative review and analysis. In addition, there may be an issue with timing of the receipt of these reports in the event that premium changes occur soon after the release of the reports noted above. If this were the case, then the information would be made available substantially beyond the 100-day period required by the current language. Given this, the Committee may want to consider leaving this reporting requirement in place.

1920 CALIFORNIA STATE TEACHERS RETIREMENT SYSTEM

The California State Teachers Retirement System (CalSTRS) administers the retirement benefits for active and retired elementary school and community college district teachers. The CalSTRS board has exclusive control over investment and administration of the retirement fund. The twelve-member board consists of Superintendent of Public Instruction, State Treasurer, State Controller, Director of Finance, five members appointed by the Governor, and three members elected by active CalSTRS members. The primary responsibilities of CalSTRS is to maintain a financial sound retirement system, maintain an efficient operational program, and improve the delivery of benefits and services to members. CalSTRS is responsible for the determination and payments of benefits to members, retirees, and their beneficiaries. CalSTRS receives funding from non-General Fund sources for administrative and operational costs, largely from retirement fund resources themselves. For 2012-13, the state operations budget is $177.0 million and 904.4 positions versus $165.8 million and 885.5 positions in the current year.

2012-13 Governor's Budget

Fund Source (millions)	2010-11 Actual	2011-12 Projected	2012-13 Proposed	BY to CY Change	% Change
General Fund	$0.0	$0.0	$0.0	$0.0	0.0
Teachers Retirement Fund	10,466.4	11,489.6	12,510.8	1,021.2	8.9
Other Retirement Funds	42.9	57.3	61.0	3.7	6.5
Total Expenditure	$10,509.3	$11,546.9	$12,571.8	1,024.9	8.9
Positions	826.0	885.5	904.4	18.9	2.1

General Fund contributions to the retirement fund costs for 2012-13 is budgeted to be slightly less than $1.358 billion: $584 million for purchasing power protection (also called "Supplemental Benefit Maintenance"); and $717 million for the base 2.017 percent contribution. The proposed funding in 2012-13 would be an increase over the $1.316 billion funding in 2011-12. These "non-add" General Fund payments are not reflected in the figure above.

ISSUE 1: INVESTIGATION AND PREVENTION OF PENSION SPIKING

The Budget proposes $746,000 (special funds) permanent funding and seven positions to create a special unit within CalSTRS to identify and prevent pension spiking. The request includes funding for staff counsel, program analysts, as well as funding for attorney general services. Pension spiking is the illegal payment of compensation intended to enhance a benefit when the compensation increase is not reflective of prior compensation level. CalSTRS notes that an individual administrator, who receives 10 percent salary increases in the last two years of service, would receive approximately an additional $500,000 in retirement benefits, assuming normal life expectancies for the member and option beneficiary. CalSTRS indicates that a conservative estimate for ongoing benefit reduction is $2,000 per year per spiking case. Based on 820 spiking adjustments per year, the annual overpayment avoidance would be over $1.6 million

Due to the absence of prior systematic efforts to identify and prevent spiking, CalSTRS does not have benefit/cost data for the spiking prevention program. Rather, it has derived the resource request from the workload requirements. The anti-spiking efforts would include both active and retired members.

The cohorts that will be the focus of these efforts include those members where:

- Final compensation exceeds $150,000;
- Annual retirement benefits exceed $100,000;
- Salary increases in final compensation years exceed twice the average; and,
- Salary increases were in excess of $15,000 or 15 percent or more of base.

STAFF COMMENT / QUESTIONS

Anti-spiking efforts are a valuable contribution to the administration of CalSTRS and for the benefit of its members. CalPERS has had similar efforts in place for a number of years. The absence of firm measurement metrics is somewhat problematic, in that the absence of these leaves the agency with no guidance over the appropriate level of resources to devote to such efforts. Absent estimates on benefit/cost ratios for the undertaking, the agency is left with somewhat arbitrary workload-driven resource needs. The tax agencies, for example, are able to derive benefit/cost estimates that are driven by data from past years and incorporate behavioral changes among taxpayers. In addition, the tax agencies typically incorporate an education campaign as part of the process. A similar approach by CalSTRS with respect to its member agencies may warrant consideration in the future. Given the lack of firm results estimates, a report to the Legislature may be warranted, after the program is up and running and has some results compiled. A report to the Legislature by December of 2013 would provide sufficient time for the program to be established and commence full operation.

ISSUE 2: TECHNOLOGY MAINTENANCE AND SUPPORT SERVICES

CalSTRS is continuing to improve systems and production and has requested permanent funding augmentation of $2.5 million (special funds) for the acquisition of system production support services for Systems Analysis and Program (SAP) development for the Corporate Accounting and Resource Management (CARM) and Penalties and Interest (P&I) systems. These systems will provide help desk support, problem management, upgrades, enhancements and business process support The new data information systems require system production support services to ensure that they operate according to design. CalSTRS has proposed contracting with an outside provider for such necessary support services.

The agency has indicated that the cost of the required support services using in-house resources is much higher than the use of contract services. It estimates that using in-house services would cost approximately $4.5 million annually versus the cost indicated in this request. It also indicates that current knowledge of system analysis and program development (SAP) is limited in the state environment, the cost of training is high and given prevailing salaries in the area, retention of qualified personnel would be difficult. CalSTRS also indicates that a pay-as-you-go approach (contracting as needed) would be even higher at $5.1 million annually. Contracting with the State Controller's office (SCO) for these services does not appear feasible due to differences in maintenance and support requirements. Once the system is fully implemented in 3-5 years, CalSTRS indicates that cost savings will be about $1.9 million annually.

BACKGROUND

Like many other state agencies, CalSTRS has run up again the limitations of many of its technology and data systems. CalSTRS identifies numerous inefficiencies, restrictions, and costs associated with its outmoded systems. The CARM and P&I systems, approved by the agency in 2010, have been underway over the ensuing period. The P&I system was completed in 2011. The CARM system's initial release is expected in October 2012 and a second release in July 2013. The system support services will be consolidated starting in fiscal year 2012-13. The system is expected to eliminate the use of numerous and various types of existing programs, including Fundware, CALSTARS, many Excel Spreadsheets, as well as labor-intensive manual processes.

STAFF COMMENT / QUESTIONS

In general, creating expertise within an agency is preferable to retaining outside consultants for services. However, technology services have been particularly problematic for a number of different reasons. Two of the most important issues that work against in-house expertise is the velocity at which technology changes and the prevailing salaries in the industry. The first of these makes it difficult and expensive for the state to remain current with respect to these changes. The later presents barriers to hiring personnel with the expertise in the area and retaining staff once they acquire such expertise. The approach of CalSTRS to contract for these services is appropriate when it can benefit from the larger economies of scale available to firms that provide specialized support services to a host of public and private entities—including the state. This approach seems prudent in supporting and maintaining SAP-type software in specialized applications such as CARM and P&I.

ISSUE 3: SYSTEM OPERATIONS SUPPORT

CalSTRS reports that it currently has a backlog from years of absorbing new application support responsibilities within existing levels of resources. The proposal is for an augmentation of $304,000 from the Teachers' Retirement Fund and the redirection of $324,000 currently used for contract services. This will fund six permanent positions designed to enhance member services, including tracking service credit, retirement contributions, and payments to retirees and beneficiaries. The proposal indicates that augmentation and redirection is necessary to respond to system problems, change requests, and maintenance.

CalSTRS has enhanced the current system based on legislation and new services to members. Over the years, a number of applications were developed and implemented without a corresponding increase in resources to sustain support, maintenance and change requests, resulting in processing backlogs. For example, program expenditures increased modestly between 2007-08 and 2011-12 from $23.6 million to $25.5 million, an increase of approximately 8 percent. The workload history provided by the agency indicates that incidents increased from 1,014 to 1,752—approximately 73 percent—over the same period. This has resulted in a backlog of issues of 170 as of July 1, 2011 and a similar backlog of issues of 166 is expected by July 1, 2012. The augmentation and enhancement is estimated to result in a steady decrease in the backlog from 11 percent to 18 percent annually.

STAFF COMMENT / QUESTIONS

Given that the augmentation and redirection will result in a steady whittling-down of the current backlog of issues, the question arises why these should be permanent positions. CalSTRS indicates that continued absorption will result in backlogs in other areas, but does not directly address the issue of permanent versus limited-term positions, and the Committee may want some clarity on this issue. In general, creating expertise within an agency is preferable to retaining outside consultants for technology support, as we noted in the item above. This program is different, because it is less specialized and the expertise appears to be more abundant, thus easing hiring, training, and retention concerns. CalSTRS should address the distinction between this item and the prior issue. Finally, given increases in technological effectiveness and efficiencies, it should not be expected that resources would necessarily keep pace with workload demands. Instead, it is more appropriate that system capabilities keep pace with workload demands. The Committee may want to CalSTRS to distinguish between workload demand absorbed into more effective programs and workload necessitating resource increases.

ISSUE 4: TECHNOLOGY MAINTENANCE AND LICENSING COSTS

CalSTRS is requesting $1.8 million in permanent funding from Teachers' Retirement Fund for uncovered projected obligations associated with ongoing technology maintenance and licensing contracts. CalSTRS has implemented a number of large and complex automation projects. As part of these projects, CalSTRS retains services and contracts with a number of state and private entities, including California Technology Agency (CTA), Office of Technology Services (Otech), and LexisNexis. The request is driven based on expanded services and increased membership demand. Since 2007-08, expenditures for the program have actually declined from $15.7 million to $13.9 million. Staff has increased moderately over the same period from 101 positions to 120 positions

CalSTRS reports that the expenses that can no longer be absorbed in the agency budget are the following:

- OTech—data center changes related to increased processing and billing changes (37 percent of total).

- Infrastructure and Maintenance Charges—increase in contract fess due to imaging, headquarters facility, member service centers, P&I, and CARM (34 percent of total).

- Telecommunication Contracts—growth in demand related to projects noted above (19 percent of total).

- LexisNexis—contract fees related to member services (11 percent).

Estimated costs for 2012-13 are outlined below:

Total Cost Increases	FY 2012-13
OTech	$661,767
Subtotal	**$661,767**
Maintenance and Service	
• Compucom • Hewlett-Packard-EVA • Verizon-Cisco • Whitlock-Audio Visual • Comm Vault • Citrix • NetQos • VMware	$88,040 98,975 226,520 40,710 39,890 16,620 14,425 96,645
Subtotal	**$622,125**
Telecommunications	$336,332
Subtotal	**$336,362**
LexisNexis	$191,500
Subtotal	**$191,500**
Total	**$1,811,754**

STAFF COMMENT / QUESTIONS

CalSTRS has been operating under the current situation for some years, yet the need for additional funding has not been requested. There does not appear to be an event that has caused a sudden demand for increased technology resources at this point. There may a critical threshold that is reached with respect to these systems that the Committee may wish to clarify. The agency indicates that developing new procurement is not an attractive alternative due to the multiplicity of contracts, uncertainty regarding the response and the resource intensiveness of such an endeavor.

ISSUE 5: BAY AREA MEMBER SERVICE CENTER

CalSTRS will be replacing its contracted member services with a staffed services center in the Bay Area. The request also calls for transitioning contract services to CalSTRS positions in San Bernardino. The CalSTRS-staffed member service center will require an augmentation of $1.8 million (special funds) and seven full-time permanent positions. Of the request, $1.4 million will be one-time with $389,000 as an on-going augmentation. In place of contracted services, employees will provide required staff, allowing for the redirection of $545,000 to the project. The new office will largely replace the current system of contract counseling services with County Offices of Education (COE) and local school districts in the Bay Area.

The Bay Area service center will serve Alameda, San Francisco, Marin, and Contra Costa counties and be staffed by one manager, four counselors, and one support staff. This support level is calculated based on experience from other member service centers (MSCs) and the demographics of the Bay Area. The Bay Area MSC will replace the existing Hayward, San Francisco, and Contra Costa County offices. The San Francisco and Contra Costa contracts will be terminated and counselors in Hayward will be transferred to the Bay Area MSC. The savings from terminated contracted services will be used to fund the project in part.

BACKGROUND

The establishment of a Bay Area service center is in response to an overall trend in delivering services to members. During the last few years, several contract offices have closed, modified their contractual arrangements, or requested CalSTRS to replace contract counselors with CalSTRS employees. Retirements, vacancies, and office closures have occurred in San Francisco, Alameda, Contra Costa, and Sonoma counties. CalSTRS contacted other offices in the Bay Area to take over management but was met with a poor response. CalSTRS is thus moving in the direction if providing its own services. The request is designed to respond to the uncertainty in contract services and ensures the consistency of services to members.

STAFF COMMENT / QUESTIONS

Cal STRS provides several lower cost alternatives, one of which involves the use of executive suite space in the Bay Area as opposed to a new, leased facility. Although not the preferred option, it is substantially less expensive. Some of the objections to this alternative (e.g. space in the ideal local may not be available) apply equally to the preferred alternative. The Committee may want to query CalSTRS on the suitability of testing the market with respect to this option.

ISSUE 6: INFORMATION TECHNOLOGY PROJECT FUNDING BUDGET LANGUAGE

CalSTRS has requested the establishment of a new budget item and associated language to address funding continuation issues associated with some of its major technology projects. The proposal would allow additional flexibility to address situations where projects entail complex and multi-year commitment of funds. It would allow three years for funds to be encumbered and 2 years for funds to be liquidated. Currently, the period of time for these two actions to occur is one year and two years. There is no new funding associated with this proposal.

Each year, CalSTRS allocates $20 million for the support of technology projects, as selected by Enterprise Program Investment Council (EPIC), which involve major commitments that further CalSTRS' strategic goals. The $20 million includes funding for EPIC staff salaries and wages, operating expenses, and various technology projects. The proposal will only shift the funds used for direct major technology projects, totaling $18.5 million. The chart provided below indicates the duration of the projects that have been funded from this source.

According to CalSTRS, this funding change would allow the agency to use already appropriated funding for a longer period of time and thus the need to request additional resources in future years would be minimized or, in some cases, eliminated. The amendment would increase the timeliness and organizational flexibility to allocate project funding, allowing projects to be initiated and implemented earlier than is currently the case. CalSTRS anticipates that the number of projects will decrease in future years, but the existing planned projects are substantial in nature and with a complexity that may require the additional time proposed. To complete the loop, CalSTRS anticipates submitting reappropriation language for consideration in the future.

CalSTRS Large Enterprise Projects

Project Name	Purpose	2006-07	2007-08	2008-09	2009-10	2010-11
Accounting Reengineering Project	The Accounting Reengineering Project will modify and enhance CalSTRS corporate database to improve financial internal controls, accuracy and completeness.	x	x	x		
Actuarial Valuation	The Actuarial Valuation project will provide CalSTRS with verification of the actuarial valuation processes, improve the current valuation process through the use of both technology and process improvement, and create detailed Actuarial Resources procedures.			x	x	x
Additional Earnings & Annuity Credit	The Additional Earnings & Annuity Credit Project will distribute payments and credits to eligible members.		x	x	x	
Board Elections	The Board Election project will facilitate, coordinate and conduct the CalSTRS 2012 Board Election as required under the Teachers' Retirement Law. The elected candidates will serve a four-year term beginning January 1, 2012.					x
BusinessRenew Corporate Accounting & Resource Management	The Renew Corporate Accounting and Resource Management (CARM) project will reduce risk, provide accurate and timely financial services information, and modernize CalSTRS financial services, systems and ways of doing business through enhanced business procedures.					x
BusinessRenew Pension Discovery	The Renew Pension Discovery will acquire the services of a Pension System Expert to assist CalSTRS in planning for a new pension solution, refining estimates for costs, schedule and resources.					x
CalSTRS Address Redesign & Enhancement Project	Improve the accuracy of client addresses by revising the current business process; enhancing the CalSTRS corporate database address maintenance process; cleansing existing address data; and locating missing addresses.	x				
Community College - Part-time and Adult Education Benefit Calculation (AB 1586 legislation) Project	The Community College – Part-time and Adult Education Benefit Calculation (AB 1586 Legislation) Project allows CalSTRS to provide for the recalculation of service credit and final compensation for part-time community college instructors.	x	x			
Continuous Improvement Team 'Proof of Concept' Project	The Continuous Improvement Team 'Proof of Concept' Project – an effort to implement an enterprise business process improvement methodology and a continuous improvement program staffing plan.	x	x	x	x	
Data Integrity Project	The Data Integrity Project will improve the integrity of data in the CalSTRS corporate database by correcting identified program and data issues, and implementing solutions to prevent additional errors.	x	x	x		
Employer Reporting Project	The Employer Reporting Project will improve the employer reporting process and provide technologies in order to gain ongoing efficiencies and to increase the quality of member account data.	x	x	x	x	
Enterpriise Process Management	CalSTRS initiated the Enterprise Process Management (EPM) Project to provide coordinated management of the Annual Update, Board Election and Cost Effectiveness Measurement (CEM) Defined Benefit (DB) Administration Survey Processes.	x	x	x		
Future State Architecture	The Future State Architecture Project will deliver the Solutions Framework and Implementation Roadmap to assist the organization in moving forward to its Future State as defined in the CalSTRS Strategic Plans.		x	x	x	x
Headquarter Facility Project	The Headquarter Facility Project has completed a multiple year planning and construction effort to physically relocate its headquarters facility from a three building campus in Sacramento to a mid-rise office building in West Sacramento. The building move and related technology is complete. The new Hosted Contact Center system is now reporting under its own project.	x	x	x	x	
Human Resource Management Information Systems	The Human Resources Management Information Systems Project will provide CalSTRS with the foundation for implementing Human Resources strategic vision, program development and technology based on industry leading best practices.		x	x	x	
Investment Accounting	The Investment Accounting Project will enhance the current accounting procedures and processes as they relate to accounting for CalSTRS' investment portfolio.				x	x
Member Information Center (MIC) Project	Provide Customer Service Representatives with a tailored system interface to the CalSTRS corporate database data and other systems through a user-friendly Web interface.	x				
myCalSTRS Online Services for Teachers (MOST)	The MOST project will enhance member online services by updating the secure access and providing a variety of new online services including the ability to complete the retirement application and register for direct deposit online.				x	x
Option Simplification Project	Simplify and reduce the complexity in selection of Defined Benefit and Defined Benefit Supplemental options by members. Modify and enhance the CalSTRS corporate database processing to align with the option simplification.	x				
Penalties and Interest	The Penalties and Interest project will implement SAP, a commercial off-the-shelf (COTS) solution, to automate the calculation, billing, monitoring, collection and dispute process of penalties and interest assessed to Employers for late remittances, late reporting and late adjustments of contributions.				x	x
Pension Accounting Initiative	The Pension Accounting Initiative will improve internal controls by addressing gaps between current and best practices in accounting policy, planning, treatment, chart of accounts, analysis, availability of financial information, use of the general ledger, communication of fiscal impacts, and training for pension administration business events.		x	x	x	x
Reduce Files	The Reduce Files project will convert non-member paper, microfilm and microfiche files to electronic format to reduce storage space requirements. This will decrease the number of filing cabinets throughout CalSTRS and contribute to the New Headquarters facility's LEED Gold Certification for sustainable "green" construction. The project also includes implementing a Records Management Program to ensure proper ongoing record maintenance.			x	x	x

STAFF COMMENT / QUESTIONS

The request to extend the length of time to encumber and expend funds for technology projects is a reasonable one. In addition, the reappropriation authority has been used in the past with respect to technology projects, including California Child Support Automation System (Department of Child Support Services), Unemployment Insurance Modernization Project (Employment Development Department), and Automatic License Data System (Department of Fish and Game). One issue that is worth considering is the ability of the Committee to monitor ongoing projects of the agency and make fiscal adjustments as necessary. The Committee may want to address this issue of whether lengthening the period of time for commitment can result in a greater uncertainty or lack of clarity for the Committee regarding technology projects, and if so, how this might be addressed. The Committee may also want to query the agency regarding the approach used by other state agencies to address issues raised by multi-year technology projects.

8380 DEPARTMENT OF HUMAN RESOURCES/DEPARTMENT OF PERSONNEL ADMINISTRATION

The Department of Personnel Administration (DPA) is responsible for managing the state personnel functions and represents the Governor as the employer in all matters concerning state employee-employer relations. DPA is responsible for issue relating to recruitment, selection, salaries, benefits, position classification, and provides a variety of training and consultation services to state departments and local agencies. DPA is funded through General Fund and special funds support. For the budget year, DPA will be budgeted $94.1 million and have 292.4 positions. This represents a significant increase over the current year budget, of $79.6 million largely due to rolling-in the administrative and operational functions of State Personnel Board (SPB). DPA will become the Department of Human Resources (DHR) as a result of the reorganization. The new department will be placed in the new Governmental Operations Agency (GOA). The process was initiated last year but did not go through the budget process.

2012-13 Governor's Budget

Fund Source (millions)	2010-11 Actual	2011-12 Projected	2012-13 Proposed	BY to CY Change	% Change
General Fund	$7.4	$6.4	$8.2	$1.8	28.1
Special Funds and Reimbursements	64.3	73.2	86.0	12.8	17.5
Total Expenditure	$71.7	$79.6	$94.1	14.5	18.2
Positions	206.7	218.0	292.4	74.4	34.1

ISSUE 1: GOVERNOR'S REORGANIZATION PLAN—CONSOLIDATED HUMAN RESOURCES

As part of the Governor's reorganization plan, the new DHR will be established, rolling together DPA and administrative functions of SPB effective July 1, 2012. This would be consistent with the Governor's Reorganization Plan Number 1 of 2011 (GRP 1—2011). All the constitutional functions and authority vested with SPD would remain with that agency. The goal of the reorganization is in the words of the plan "end duplicative and disjointed processes which are neither efficient nor cost effective." This item requests the transfer of budgetary authority from DPA and SPB to DHR effective July 1, 2012.

Under Government Code Section 12080.1, the Governor is required from time to time to examine the organization of all agencies and determine what changes are necessary to accomplish one or more of several goals including:

- Promote the better execution of the laws, the more effective management of the executive and administrative branch of the state government and of its agencies and functions and the expeditious administration of the public business;

- Reduce expenditures and promote economy to the fullest extent practicable consistent with the efficient operation of the state government;

- Increase the efficiency of the operation of the state government to the fullest extent practicable;

- Group, consolidate and coordinate agencies and functions thereof as nearly as possible according to major purposes;

- Reduce the number of agencies by consolidating those having similar functions under a single head and to abolish such agencies or functions thereof as may not be necessary for the efficient operation of the state government;

- Eliminate overlapping and duplication of effort.

A number of studies and commissions and reports have recommended the rationalization of the state's human resources functions. In 1995, the Little Hoover Commission made recommendations to streamline and improve the state personnel functions by eliminating the overlap and redundancy between DPA and SPB and consolidating activities in one agency. In the same year, the Legislative Analyst's Office made recommendations related to a fundamental restructuring of the agencies. In 1997, the California Research Bureau issued a report that noted the overlapping responsibilities' of SPB and DPA. In 2005, the Little Hoover Commission again weighed in and urged changes in the system.

The Administration has provided a timeline that involves a consolidation timeline over the remainder of 2011-12 and during 2012-13. The consolidation would be fully in place for 2013-14. DOF indicates that there will be savings from the consolidation, in addition to increases in efficiency and effectiveness. Once the revamp has been implemented, DOF projects annual savings stemming largely from staffing reductions and result in savings of $8.6 million ($3.7 million General Fund).

The areas of duplication between DPA and SPB that are being combined under the proposal are:

- **Administrative Functions.** All administrative functions of DPA and SPB would be consolidated, including budgeting, procurement, personnel, contract management, business services, and information technology.

- **Training**. Training units would be combined to provide training online or classroom training where needed. State training would be centralized and standardized state training courses aligned to state law, regulation, and policies, with training consistency among state agencies.

- **Appointments.** The merger would simplify the appointment processing procedures. Human resource staff will no longer need to go to two different departments for appointment processing.

- **Career Executive Assignments (CEA).** The consolidation will eliminate the duplicative review process that requires both DPA and SPB to review and approve CEAs. DHR staff would establish the position and ultimately adopt it without SPB Board review.

- **Establishing, Abolishing, and Revising Classes.** A class specification is the summary of duties and responsibilities of positions within that class. The current process would be simplified by consolidating review and negotiation in DHR prior to adoption by SPB.

- **Special Consultants.** Special Consultant is for temporary appointments to meet short-term needs. Departments must now submit a justification to DPA, subject to SPB approval, if there is an exception to guidelines. Under the reorganization, all this would be conducted by DHR.

- **Legislation.** One legislative unit would provide legislative support to both DHR and the SPB, eliminating duplication of bill tracking and monitoring, researching, writing, and coordinating legislative proposals, and analyzing legislative proposals and bills.

- **Communications**. One communications unit would provide communication support to both DHR and SPB, eliminating duplication of effort with respect to personnel related media inquiries, policy changes, human resource announcements, and other state personnel functions.

- **Alternate Salary Ranges.** Alternate salary ranges are based on working conditions and/or possession of a specified license or degree. DHR would integrate the establishment of alternate ranges and pay differentials in the new Personnel Management Unit.

STAFF COMMENT / QUESTIONS

The Administration has provided limited detail on how the consolidation of the two agencies will occur. In addition—and more importantly—greater efficiency and effectiveness have been put forth as an argument for reorganization, but there is little by way of example as to how this would occur. If the outcome is intended to be a more rational and function department, there should be some demonstration of this in practical terms. In addition, the new organizational structure may have an impact on labor relations with represented and non-represented employees. The committee may ask the administration how these function would work under the new organization plan. Finally, the Committee may want to request that the department or Department of Finance walk-through some of the enhanced aspects of the new organizational arrangement, including the proposed Governmental Operations Agency.