AGENDA

ASSEMBLY BUDGET SUBCOMMITTEE NO. 4 ON STATE ADMINISTRATION

ASSEMBLYMEMBER JOAN BUCHANAN, CHAIR

WEDNESDAY, MAY 23, 2012
1:30 P.M. - STATE CAPITOL ROOM 437

VOTE-ONLY CALENDAR

ITEMS TO BE HEARD

VOTE-ONLY

1760 DEPARTMENT OF GENERAL SERVICES

ISSUE 1: PROGRAM REDUCTIONS

May Revision. The Governor's May Revise includes a request to schedule a portion of the unallocated reductions that were identified in the Governor's Budget for the Department of General Services (DGS). The request has identified a total of $33.39 million dollars and 45.5 positions that can be reduced in the 2012-13 budget due to program reductions and operational efficiencies.

BACKGROUND

The Governor's January Budget identified $59.08 million dollars in reductions to DGS due to efficiencies and program changes. The May Revise identifies some of the specific solutions related to the reduction. DGS has identified $33.39 million dollars in reductions that can be made in the 2012-13 budget. The reductions include the following:

- $15.4 million and seven positions from the Office of State Publishing. Utilization of increased technology and automation will allow the Office of State Publishing to offset some of reductions.
- $6.7 million and 28.5 positions in various Real Estate Services Division programs by reprioritizing workload, reducing travel by increasing use of videoconference capabilities, and other operational measures will be utilized to offset these reductions.
- $6.3 million and 3.0 positions in various Building Regulations programs. Reductions will be achieved by greater use of operational efficiencies and reductions in consulting and contracting costs.
- $5 million and 7.0 positions within the administrative support will be achieved by streamlining processes, and enhancing operational efficiencies.

DGS notes that they plan on achieving the balance of the reduction, $25.68 million, through future, undetermined efficiencies.

Staff Recommendation: Approve the May Revise request

ISSUE 2: STATEWIDE CONSOLIDATION OF UNDERUTILIZED OFFICE SPACE

May Revision. The Governor's May Revise requests amended Budget Bill Language to expand the use of the Service Revolving Fund, Tenant Improvement Reserve Account relating to efforts to improving state office space utilization.

BACKGROUND

This request is to amend current Budget Bill Language in order to better utilize office space owned by the state. The provisional language related to this request (Item 1760-001-0666) is amended as follows:

"The Director of Finance is authorized to increase this item for purposes of funding ~~tenant improvement projects to facilitate~~ the backfill of vacant space, <u>necessary restack studies, and other required building improvements</u> within Department of General Services (DGS) office buildings <u>related to the Governor's Office Space Utilization Initiative</u>. This provision shall only be used to augment expenditure authority for DGS office buildings where a $0.03 tenant improvement surcharge for DGS Individual Rate Buildings or a $0.02 tenant improvement surcharge for DGS Building Rental Account Buildings has been approved by the Director of Finance and is included in the monthly rental rate. Director of Finance approval is contingent upon justification for the proposed tenant improvement projects to be provided by the DGS including an analysis of cost impacts and how the tenant improvements will improve the state's utilization of the facility. Any augmentation made in accordance with this provision shall not result in an increase in any rate charged to other departments for services without the prior written consent of the Director of Finance. Any augmentation made pursuant to this provision may be authorized not sooner than 30 days after notification in writing to the chairpersons of the fiscal committees of each house of the Legislature and the Chairperson of the Joint Legislative Budget Committee."

Staff Recommendation: Approve the May Revision request

ISSUE 3: OFFICE OF ADMINISTRATIVE HEARINGS

May Revision. The Governor's May Revise requests an increase in expenditure authority of $961,000 (Reimbursements) for the Office of Administrative Hearings to implement AB 366 (Allen, Achadjian), Chapter 624, Statutes of 2011. The office states the new law could lead to as many as 1,000 administrative hearings per year.

BACKGROUND

AB 366 (Allen, Achadjian) Chapter 654, Statutes of 2011, revised the procedures governing the involuntary administration of antipsychotic medication to state hospital patients. The Office of Administrative Hearings has reached an Interagency Agreement with the Department of Mental Health to facilitate the hearing process for the involuntary medication of individuals incompetent to stand trial.

Currently, the Office of Administrative Hearings lacks the requisite expenditure authority to handle the estimated 1,000 administrative hearings per year that this new law will generate. The provisions of law impacting the Office of Administrative Hearing in AB 366 will take effect on July 1, 2012.

The Office of Administrative Hearings has determined that it will require a Staff Counsel III; an Associate Governmental Program Analyst, and two Senior Legal Typists. Additionally, the Office of Administrative Hearings will require an increase to its OE & E expenditure authority to support these positions and to permit the Office of Administrative Hearing to enter into personal service contracts for Pro Tem Administrative Law Judges (ALJ) and counsel for patients.

As the law was enacted, if the defendant originally consented to antipsychotic medication but subsequently withdraws his or her consent, or if involuntary antipsychotic medication was not ordered and the treating psychiatrist determines the medication has become medically necessary and appropriate, the treating physician will certify whether the defendant lacks capacity to consent, an assessment of the current mental status of the defendant and the opinion of the treating psychiatrist that involuntary antipsychotic medication has become medically necessary and appropriate.

Within 72 hours of the certification, the law requires a medication review hearing before an ALJ to be conducted at the facility where the defendant is receiving treatment. The defendant is entitled to representation by an attorney or patient's rights advocate. If the ALJ determines the defendant meets specific criteria, the antipsychotic medication may be administered to the defendant for 21 days. Any medication beyond 21 days requires a court order.

STAFF COMMENT

The request is less than the potential costs described in the August 25, 2011 Assembly Appropriations Committee analysis of the bill, which suggested costs of $1.2 million in 2012-13 for ALJ hearings.

Staff Recommendation: Approve the May Revision request

ISSUE 4: REDUCE EXCESS AUTHORITY FOR THE NATURAL GAS SERVICES PROGRAM

May Revision. The May Revise includes a request to reduce the Natural Gas Services Program by $75 million in order to align the program with actual natural gas costs, which have dropped in recent years.

BACKGROUND

The Natural Gas Program, which is within the Energy Contract Services division of Department of General Services (DGS), was originally developed to purchase natural gas needed to operate state and other public facilities at a more economical price. The program was started when changing state and federal regulations gave rise to the option for large gas users, such as the state, to purchase gas directly from the supplier versus purchasing from the local gas utility companies (e.g., Pacific Gas & Electric, Southern California Gas). The program serves as the state interface between public agencies and the gas suppliers, ensuring that the state and other public sector facilities get the best rate available based on economies of scale and in-depth knowledge of the opportunities available from the natural gas market.

In Fiscal Year 2008-09 an augmentation of $75 million was authorized for the purchase of natural gas. Currently, natural gas prices are substantially lower than the previous four fiscal years, allowing for a reduction of $75 million, leaving a total budget of $287.98 million.

Staff Recommendation: Approve the May Revision request

ISSUE 5: CAPITAL AREA DEVELOPMENT AUTHORITY PROPERTY DISPOSITION

May Revision. The May Revise requests Trailer Bill Language to sell seven state-owned, Capital Area Development Authority-managed properties with no state programmatic use.

BACKGROUND

The proposed Trailer Bill Language specifies seven parcels of state-owned land located within the Capital Area Development Authority that could be dispensed with. The Capital Area Development Authority managed properties are located at:

- 1510 14th Street (.14 acres)
- 1530 N Street and 1412 16th Street (.22 acres)
- 1416 17th Street and 1631 O Street (.15 acres)
- 1609 O Street (.59 acres)
- 1612 14th Street (.07 acres)
- 1616,1622,1626 14th Street and 1325 and 1331 Q Street (.30 acres)

Proceeds of any moneys received from the disposition of any the parcels listed above would be deposited in either the General Fund or the Deficit Recovery Bond Fund as determined by the Department of Finance.

Staff Recommendation: Approve the Trailer Bill Language

8955 DEPARTMENT OF VETERANS AFFAIRS

ISSUE 1: REAPPROPRIATION AUTHORITY FOR CAPITAL OUTLAY FUNDS

Spring Finance Letter. A Spring Finance Letter requests the reappropriation of funds for construction projects at the Veterans Home of California – Yountville and the California Central Coast State Veterans Cemetery. The funds - $350,000 for Yountville and $1.1 million for the California Central Coast State Veterans Cemetery – were appropriated in the Budget Act of 2006 and the Budget Act of 2011, respectively.

BACKGROUND

The Department of Veterans Affairs (CalVet) has completed the construction project at the Veterans Home of California – Yountville that renovated the Member Services Building to address fire safety and Americans with Disabilities Act deficiencies. The project cost $13.8 million in state lease-revenue bonds and federal funds. While the project is complete, CalVet requests reappropriation of $350,000 from the project to purchase equipment in 2012-13.

CalVet also seeks reappropriation authority of $1.1 million for a cemetery project at the former Fort Ord Army base. The funds will be used for the preliminary plan phase of the cemetery and to allow CalVet to apply for a federal grant to design and construct the facility.

Staff Recommendation: Approve the Spring Finance Letter

ISSUE 2: ADJUSTMENT TO FEDERAL PER DIEM FOR VETERANS HOMES

Spring Finance Letter. A Spring Finance Letter requests an adjustment to reflect $15,000 in additional federal funding for the state's veterans homes.

BACKGROUND

The federal government pays a per diem rate to the state for every resident that is housed in the state's veterans homes. This $15,000 change reflects a decrease in the projected number of veterans home residents in 2012-13 and an increase in the per diem rate.

Staff Recommendation: Approve the Spring Finance Letter

ISSUE 3: SKILLED NURSING FACILITY ACTIVATION SLIP

Spring Finance Letter. A Spring Finance Letter requests a decrease of $3 million for the Department of Veterans Affairs (CalVet) to reflect a delay in the opening of the Skilled Nursing Facility at the West Los Angeles veterans home. The delay reduces staffing needs by 42 positions in FY 2012-13.

BACKGROUND

CalVet had intended to open a Skilled Nursing Facility at the Veterans Home in West Los Angeles in February 2012. The department now intends to open the facility in Summer 2012.

The delay is caused by the termination of a food sharing agreement with the U.S. Department of Veterans Affairs. The federal department had been providing food services to the West Los Angeles home, but the federal government has requested ending all service sharing agreements with the state due to accounting difficulties that have arisen because the state and federal governments operate on differing fiscal-year calendars.

The cancelled contract required the state to seek a private vendor for food services. This has caused a delay in opening the Skilled Nursing Facility because the new processes for food delivery to the facility are under review by the Department of Public Health, which must issue a license for the facility before it can open.

The delay in opening reduces the need for 42 positions in 2012-13, as the facility will have fewer patients in 2012-13 than originally estimated. This reduction in personnel needs allows for CalVet to reduce General Fund costs by $3 million.

CalVet estimates it will have 84 residents in the facility by the end of the 2012-13 fiscal year.

Staff Recommendation: Approve the Spring Finance Letter

1900 CALIFORNIA PUBLIC EMPLOYEES RETIREMENT SYSTEM

ISSUE 1: CALPERS ADMINISTRATIVE BUDGET ADJUSTMENTS

May Revision. The May Revision proposes adjustments to eight items in the California Public Employees Retirement System's (CalPERS) administrative budget based on the 2012-13 CalPERS budget approved during the April 18, 2012 board meeting. CalPERS has continuous appropriations authority, so these changes are to ensure display items in the budget are accurate. The items and changes are described below:

- Item 1900-003-830, CalPERS board administration costs paid by the Public Employees Retirement Fund, increased by $164.5 million;
- Item 1900-015-0815, CalPERS board administration costs paid by the Judges' Retirement Fund, decreased by $42,000;
- Item 1900-015-0820, CalPERS board administration costs paid by the Legislators' Retirement Fund, decreased by $70,000;
- Item 1900-015-0822, CalPERS board administration costs paid by the Public Employees Health Care Fund, increased by $5.2 million;
- Item 1900-015-0830, CalPERS board administration costs paid by the Public Employees Retirement Fund, increased by $18.3 million;
- Item 1900-015-0833, CalPERS board administration costs paid by the Annuitants' Health Care Coverage Fund, increased by $409,000;
- Item 1900-015-0849, CalPERS board administration costs paid by the Replacement Benefit Custodial System, increased by $2,000;
- Item 1900-015-0884, CalPERS board administration costs paid by the Judges Retirement System II, decreased by $10,000.
- Reimbursements decreased by $116,000.

Staff Recommendation: Approve the May Revise request

9650 HEALTH AND DENTAL BENEFITS FOR ANNUITANTS

ISSUE 1: HEALTH AND DENTAL BENEFITS COST ADJUSTMENT

May Revision. The May Revision requests an increase in costs for health and dental benefits due to rising premiums. The Governor's Budget proposed $1.7 billion for health and dental benefits for annuitants, which was based on a projected increase in premiums of 8.5 percent over 2012 rates. A revised projection suggests premiums will be 10 percent more than 2012 rates, requiring an increase of $13.1 million to Item 9650-001-0001.

Staff has no issues with this proposal.

Staff Recommendation: Approve the May Revise request

1920 CALIFORNIA STATE TEACHERS RETIREMENT SYSTEM

ISSUE 1: REVISED CREDITABLE COMPENSATION

May Revision. The May Revision proposes a technical correction regarding the amount of General Fund contribution to CalSTRs based on a revision of creditable compensation as reported for 2010-11. The true-up is a percentage-driven calculation and is the result of a lag in reporting of actual compensation. The Governor's Budget estimated 2012-13 contributions of $1.4 billion, based on October 2011 report of prior-year teacher payroll by CalSTRs. The actual amount is based on the submission by CalSTRs in April 2012 of an update to the prior-year teacher payroll.

The revision in the creditable compensation results in an increase in funding of $1.4 million. This increase consists of $545,000 in the defined benefit level, $157,000 in the pre-1990 defined benefit level, and $675,000 for supplemental benefit maintenance account.

Staff has no issues with this proposal.

Staff Recommendation: Approve the May Revise request

8380 DEPARTMENT OF HUMAN RESOURCES

ISSUE 1: ARBITRATION FUNDING FOR THE TRIBAL LABOR PANEL

May Revision. The May Revision requests $100,000 from the Indian Gaming Special Distribution Fund for disbursement to the Tribal Labor Panel to support its arbitration duties and other responsibilities.

BACKGROUND

Under current law, the California Department of Human Resources (CalHR) is responsible to provide necessary funding for disbursement to the Tribal Labor Panel. The fund source is the Indian Gaming Special Distribution Fund (IGSDF), which is money received by the state from Indian tribes as specified by the terms of the tribal-state compacts.

CalHR (formerly Department of Personnel administration first received $400,000 in funding from the IGSDF in the 2000 Budget Act. Since that time, and through 2010-11, these funds were used to contract with an outside entity to provide arbitration services per current law. Not all of the funds were used each year, leading to some funds disencumbering and reverting to the state. Additionally, these funds were reappropriated several times; the last reappropriation was in 2010-11. By this request, the administration proposes to start fresh in 2012-13 and provide $100,000 from the IGSDF. In essence, CalHR requires the appropriation so it can secure the contract; under the terms of the Budget Act, CalHR has one year to encumber the funds and two years to spend.

Staff Recommendation: Approve the May Revision request

ITEMS TO BE HEARD

REDEVELOPMENT

The May Revision includes a trailer bill proposal that creates a framework for successor agencies to transfer cash assets not obligated or reserved for other purposes to cities, counties, special districts and local schools, consistent with the state Constitution.

RESPONSE PANEL

- Mayor David Glass
  City of Petaluma

- Dan Carrigg,
  Legislative Director, League of California Cities
  Mayor David Glass, City of Petaluma

- Deborah Collins
  Managing Attorney
  The Public Interest Law Project

- Phillip Kilbridge
  Executive Director
  Habitat for Humanity Greater San Francisco

Given the complexity of the May Revision proposal and the large amount of public interest, this issue will have a reaction panel that is intended to allow for an expanded reaction from invited key stakeholders.

BACKGROUND

As a result of legislation adopted last year, AB 26 X1 (Blumenfield), Chapter 5, Statutes 2011 and subsequent decisions by the State Supreme Court, Redevelopment Agencies (RDAs) were dissolved as of February 1, 2012. Between when the Governor proposed the elimination of RDAs as part of his 2011-12 Governor's Budget, RDAs engaged in activities including the transfer of assets. Former RDAs maintained substantial resources and assets that have been conveyed to the Successor Agencies, usually the city that established them, even though the RDAs were under a freeze. The purpose of the legislation was to redirect property taxes to local governments and convey assets in a manner to maximize the value for purposes of schools, counties, cities and special districts. The administration has proposed trailer bill language that attempts to address the asset transfers that have occurred counter to law. In addition, the language clarifies some aspects of the original RDA legislation.

In his January budget, the Governor assumed that approximately $2.1 billion of additional property taxes (formerly tax increment flowing to RDAs) would be available for K-12 education. For the May Revision, the estimates of the amount over the two-year period has been lowered to about $1.8 billion. This due to "enforceable obligations" paid for out of property taxes, coming in higher than expected.

In addition, the May Revision reflects the sweep existing unencumbered cash and cash equivalent assets from former RDAs held in the Capital Projects Fund, the Debt Service Fund, the Low-Mod Housing Fund, and other funds, which occurs under existing law. This results in an additional $1.4 billion in 2012-13 (and an additional $600 million in 2013-14). The Low Mod Housing Funds comprise only $485 million of the $1.4 billion. These funds would also go to K-14 education.

MAY REVISION TRAILER BILL

The proposed draft trailer bill language proposes a framework for successor agencies to transfer cash assets not obligated or reserved for other purposes to cities, counties, special districts and local schools, consistent with the state Constitution. As part of this, the language addresses remedies for inappropriate transfers of assets and incorrect obligation paid from property taxes, clarifies parts of the original RDA legislation, and corrects inconsistencies and cleans-up ambiguities.

- **Remedies for Bad Actions.** For General Fund purposes, the most important aspects of the proposed language allows county auditor-controllers, Department of Finance and the State Controller to require the return of funds improperly spent or transferred to a public entity. If the funds are not returned in a timely fashion, they can be recovered through an offset of sales tax and use taxes or property taxes. In addition, the language allows payments on improperly claimed enforceable obligations to be recovered from future property tax allocations.

- **Clarifications of Law.** The proposed language also makes clarifications of certain aspects of current law and adds additional detail for purposes of clarity. Among the most important of these are: clarification regarding the issuance and refinancing bonds and the maintenance of reserves, definition of enforceable obligations to exclude vague plans or commitments, definition of housing assets that would be transferred to the entity that assumes housing activities, treatment of pass-through payments to local governments, constitution and actions of oversight boards, and disposition of assets identified for public use.

- **Corrections and Clean-Up.** The original RDA legislation was extremely complex and detailed. As a result, there were certain areas where additional language to rectify inconsistencies or inaccuracies. The most important areas relate to scheduling of payment schedule for enforceable obligations, definition of administrative costs, definition of property taxes, actions of successor agencies, and the timing of certain deposits.

The state has been informed by various local governments regarding inappropriate and unauthorized transfer of assets by successor agencies. In addition, the Controller, in its on-going audits of RDA funds and assets has also uncovered instances of asset transfers and the use of funds that are not allowed under the law. With respect to enforceable obligations, the Department of Finance has continued to reject claims that it has determined are not truly legal obligations that should be paid from property taxes. The trailer bill language would provide the tools to begin to address these situations.

STAFF COMMENT

The proposed trailer bill would enhance the Department of Finance's powers to identify and collect local tax funds from successor agencies. The language does not provide a venue for dispute resolution or appeal outside of the court system. The Subcommittee may wish to consider whether providing local governments and successor agencies with a venue for dispute resolution might hasten the transfer of assets and improve the likelihood that funds assumed in the budget materialize in the budget year.

Staff Recommendation: Hold Open

9210 LOCAL GOVERNMENT FINANCE

ISSUE 1: Reimbursements to Amador County

The Governor's budget requests $1.5 million for Amador County to remedy an adverse impact from a shift of local tax funds.

BACKGROUND

In the January Budget, the Governor proposed a new General Fund subvention of $4.4 million to backfill Mono and Amador counties due to unique circumstances that reduced property tax directed to those county governments and cities within those counties in 2010-11. In an April 1 Finance Letter, the Governor rescinded the funding for Mono County indicated that updated dated suggested the problem did not existing in that county for 2010-11. The Governor maintains the funding request of $1.5 million for Amador County. The revenue loss is understood to also have occurred in 2011-12 and will continue into 2012-13 and likely beyond, but the administration indicates it is undetermined at this time whether its proposal is one-time or ongoing.

Legislation enacted early in the Schwarzenegger administration shifted local property tax from schools to cities and counties to accommodate two State fiscal initiatives. Schools were then backfilled with State funds. Overall, the fiscal changes resulted in a large net revenue gain for cities and counties as the replacement revenue streams have grown faster than the relinquished revenue streams. However, for Amador County, unique circumstances reportedly reversed this outcome in 2010-11 and it is possible this outcome could occur for a few additional counties in the future.

- **Financing Economic Recovery Bonds (ERBs):** In the 2004 primary election, voters approved Proposition 58, which allowed the State to sell ERBs to pay its accumulated budget deficit. The local sales tax for cities and counties was reduced by one-quarter cent and the State sales tax was increased by one-quarter cent to create a dedicated funding source to repay the ERBs. Property tax was redirected from schools to cities and counties, and the State backfilled schools via the Proposition 98 funding guarantee. This financing mechanism is sometimes called the "triple flip," and was anticipated to hold local governments harmless. When the ERBs are repaid in 2016-17 (or earlier), the local sales tax rate is restored.
- **Backfilling for the Vehicle License Fee (VLF) Tax Cut**: Also in 2004, the Legislature enacted the "VLF Swap" to provide a more reliable funding mechanism to backfill cities and counties for the local revenue cut by the State when the VLF tax on motor vehicles was reduced from 2.0 percent of a vehicle's value to 0.65 percent of a vehicle's value. Here again, the state redirected property tax from schools to cities and counties and backfilled schools with State funds.
- **Problem for Amador**: The funding mechanism stopped fully working for Mono and Amador counties reportedly in 2010-11 due to all the schools in those counties becoming "basic aid" schools. Basic aid schools receive sufficient local property tax to fully fund the per-student amounts required by the Proposition 98 guarantee and therefore the State's funding is minimal. Due to this "basic aid" situation, current law would not backfill schools for any property tax shifted to cities and counties and county auditors have reportedly reduced or discontinued the "AB 8" shift of property tax from

schools to those cities and counties. The estimated loss for the two counties in 2010-11 is $4.4 million. Conversely, in a non-"Test 1" Proposition 98 year, the State would realize a savings from not having to backfill schools – but 2012-13 appears to be a Test 1 year.

STAFF COMMENT

The Subcommittee heard this issue on March 20, when the administration was requesting $4.4 million for Amador and Mono counties. The issue was left open. The administration has reduced the request in an April 1 Finance Letter and is currently requesting only $1.5 million for Amador County, indicating that Mono County did not lose fund in 2010-11.

The financing shifts and educational financing provisions are complex, and perhaps not entirely relevant to making a determination on this budget request. The Subcommittee may instead want to focus on some broader ideas and issues:

- **Revenue growth uncertainty:** The funding shifts did include uncertainty and risk, as the relative growth of various revenue streams over many years was unknown. On a statewide basis, data suggests most counties – perhaps as many as 56 of 58 counties - have received a net benefit from the shifts. Since 2010-11, reportedly Amador has not seen net benefits. Individual county estimates of benefits or costs are not currently available, but Amador County has estimated the isolated effect of the property tax shift at $1.5 million.
- **No backfill guaranteed in the original legislation, but the Amador outcome was not anticipated:** The enacting legislation did not include provisions for the State to backfill locals with new subventions if the baseline funding mechanism proved to be insufficient to maintain city and county funds. At the time of the legislation, stakeholders were likely aware of the risk of variable levels of growth for different revenue streams, but may not have anticipated this outcome of all schools within the county becoming "basic aid." Since this outcome may not have been foreseen by the State or local governments at the time of bill enactment, does the State have a responsibility to backfill for this revenue loss?
- **Budget challenges in most cities and counties:** Since many cities and counties are continuing to experience budget shortfalls, should the Legislature consider the fiscal condition of the two counties relative to other counties as a factor in the determination. For example, has the decline in revenue for these counties since 2007-08 exceeded the statewide average?
- **Timing of the subvention:** If the Legislature determines a subvention is appropriate, should the Legislature appropriate for revenue loss through 2012-13 (maybe funding at a level of $13.2 million), or conversely decide to fund, but defer reimbursement to later in the fiscal year.

Staff Recommendation: Adopt April Fiscal Letter

8885 COMMISSION ON STATE MANDATES

ISSUE 1: COMMISSION ON STATE MANDATES MAY REVISION ADJUSTMENT

As part of his May Revision, the Governor has requested the authorize reappropriation of $79,000 to fund unanticipated costs of the commission. The costs are related to the accrued leave payout of a commission staff member who is retiring in 2012.

BACKGROUND

The Commission on State Mandates (COSM) is charged with the duties of examining claims and determining if local agencies and school districts are entitled to reimbursement for increased costs for carrying out activities mandated by the State. The Legislature created the seven-member commission in 1984 as a quasi-judicial body and instructed it to act deliberatively in resolving the complex legal questions associated with determinations of state mandated costs. COSM is made up of the Director of Finance, the State Controller, the State Treasurer, the Director of the Office of Planning and Research, a public member with experience in public finance, and two additional members of local public bodies appointed by the Governor and approved by the Senate.

This budget item appropriates the funding for staff and operations costs of COSM. (The item also includes appropriations for non-education mandate payments to local governments addressed later in the agenda.) State operations and administrative costs are approximately $1.6 million and the number of personnel years would remain stable, compared to the current year, at 11.0.

MAY REVISION

As part of his May Revision, the Governor has requested the authorize reappropriation of $79,000 to fund unanticipated costs of the commission. The costs are related to the accrued leave payout of a commission staff member who is retiring in 2012.

Staff Recommendation: Adopt both May Revision Fiscal Letters

0502 CALIFORNIA TECHNOLOGY AGENCY

ISSUE 1: MAY REVISION FISCAL LETTER

The May Revision contains a proposal for $670,000 and five positions, plus trailer bill language, to provide technology project oversight.

BACKGROUND

The May Revision contains a proposal for $670,000 and five positions to offer additional project oversight. The intent of this proposal is to minimize the reliance on contractors for project oversight. The California Technology Agency expects that the reduction of reliance on outside contractors will result in savings to state information technology projects, which will be captured through Budget Control Section 4.05.

The proposal also includes trailer bill that requires California Technology Agency approval to procure project oversight services.

STAFF COMMENT

This request mirrors discussions by this Subcommittee in 2011 regarding enhancing the CTA's role in standardizing and improving oversight of state IT projects.

Staff Recommendation: Adopt May Revision Fiscal Letter and placeholder Trailer Bill.

8880 FI$CAL

ISSUE 1: FI$CAL MAY REVISION FUNDING PLAN UPDATE

The May Revision contains a proposal to change the funding proposed mechanism for the Fi$Cal project to reduce General Fund Cost.

BACKGROUND

The Subcommittee heard this issue on May 1, 2012 and directed the Fi$Cal project to return by May 15, 2012 with a plan for implementing Fi$Cal with less of a General Fund Cost in 2012-13. The administration has submitted a revised funding plan in the May Revision that complies with this direction. The new proposal defers all General Fund expenditures to future project years. As a result, $53.5 million in General Fund costs are avoided in 2012-13 by accelerating the use of special funds for the project. This both allows the General Fund costs of the project to be avoided, but also avoids borrowing costs associate with other options to reduce the project's exposure to General Fund in 2012-13.

The Financial Information System for California (Fi$Cal), is an Enterprise Resource Planning (ERP) information technology (IT) project intended to create and implement a new statewide financial system which will encompass the areas of budgeting, accounting, procurement, cash management, financial management, financial reporting, cost accounting, asset accounting, project accounting, and grant accounting. As an ERP system, Fi$Cal will be a set of software applications that will integrate and streamline the aforementioned business processes, and, in so doing, replace aging legacy systems, inefficient “shadow” systems, and duplicate processes throughout the state’s departments and agencies.

The Fi$Cal system evolved from an effort by the Department of Finance to create a new the Budget Information System (BIS). The project evolved and was increased in size into what is now known as the Fi$Cal project into a full ERP system to replace the State Controller’s Systems and the California State Accounting and Reporting Systems (CALSTARS).

FI$CAL CONTRACT

After a two-year procurement process, Accenture was awarded the contract to create and implement FI$CAL. The total contract is expected to be 213 million and last five years.

The project used a two-step procurement strategy (similar to the one used on the 21st Century project) that included an open procurement for a Firm Fixed Price fit-gap analysis to three top bidders (in FY 2010-11), followed by the actual fit-gap analysis in which the bidders had nine months to review potential gaps between their software and the state’s business requirements. Each bidder receives a fixed price for production of a detailed implementation plan. At the end of the process, the state had three entirely viable FI$CAL proposals from which to choose. Through the procurement evaluation process, Accenture was deemed the winning bidder.

The fit-gap analysis is often referred to as a "bake-off" because the final vendor is selected from a pool of vendors that have developed tangible prototypes for evaluations before the final awards are made.

FUNDING PLAN

The FI$CAL project intends to use a "pay-as-you-go" funding mechanism for the expected $616.8 million project costs, of which $331.5 million is expected to be General Fund. Most of the project costs are one-time. The project is expecting to complete implementation in 2016-17, with its first year of maintenance and operations in 2017-18. As expected the total project costs have been reduced from the early estimates of $1.6 billion project costs projected in earlier analysis of the project. Funds have already been appropriated and spent for $94.6 million ($17.7 million General Fund) of the project costs. The project would recapture federal funds upon final completion of the project.

The chart below illustrates the proposed funding plan for the project:

Year	**Total Project Cost**	**General Fund**
Expenditures 2005-06 to 2011-12	$94,593.8	$17,668.6
2012-13	88,978.0	53,475.8
2013-14	84,596.6	50,842.6
2014-15	101,909.0	61,247.3
2015-16	130,014.6	78,138.8
2016-17	84,194.3	50,600.8
2017-18	32,519.3	19,544.1
Total	**$616,805.6**	**$331,518.0**

SPRING FISCAL LETTER REQUEST AND JAN 10 BCP

The Governor's budget includes $130.6 million ($64.9 million General Fund) for the FI$CAL project. The January Budget includes $39.1 million ($26.7 million General Fund) appropriated for development of the system, including 79 positions. In addition the budget assumed a $91.5 million ($38.2 million General Fund) project cost for the FI$CAL contract that was not appropriated, but was assumed in the overall budget scoring.

The Spring Fiscal Letter reflects the lower anticipated cost of the project now that the contract has been awarded. The new cost for 2012-13 is anticipated to be $89 million ($53.5 million General Fund), $41.6 million less than anticipated in the budget. The Spring Fiscal Letter also changes the project positions requests 89 new positions, including 72 new positions at the FI$CAL project and 17 new partner agency positions for implementations.

Overall, the project is requesting 247 positions (235.73 PYs) for various FI$CAL functions as detailed below:

Function	Total PY's	Total Positions
Administration	32.26	36
Business Team	77.00	80
Change Management Office	29.00	32
Project Management Office	18.00	18
Technology Team	63.47	65
Executive	16.00	16
Total	**235.73**	**247**

MAY REVISION

The May Revision makes three adjustments to the Spring Fiscal letter:

- Changes the funding sources for the 2012-13 fiscal year project activities to accelerate the use of special fund, thus avoiding $53.5 million of General Fund costs in the budget.
- Adds provisional language to allow the Department of Finance, with JLBC notification, to seek an augmentation if special funds are unavailable for the project.
- Makes technical changes to conform to the Budget Letter 12-03 regarding position control and salary savings.

The May Revision letter makes changes to the April Letter, so both letters would need to be adopted for the administration's proposal to be adopted.

PRIOR ACTION

On May 1, 2012, the Subcommittee took the following actions:

- Direct the administration to provide an alternative funding plan for FI$CAL that results in less General Fund cost in 2012-13 by May 15, 2012.
- Adopt Placeholder Trailer Bill Language to implement reporting requirements.

STAFF COMMENT

The administration has complied with the direction of the Subcommittee in the May Revision and thus both fiscal letters should be adopted.

Staff Recommendation: Adopt both Spring and May Revision Fiscal Letters

9620 CASH MANAGEMENT AND BUDGETARY LOANS

ISSUE 1: CASH MANAGEMENT AND BUDGETARY LOANS

The May Revision calls for a decrease in this budget item as a result of paying off fewer budgetary loan amounts.

BACKGROUND

This budget item appropriates funds to pay interest costs on General Fund borrowing used to overcome cash flow imbalances during the fiscal year. Because receipts and disbursements occur unevenly throughout the fiscal year, the General Fund borrows in most years, even though each budget is balanced when enacted and funds are repaid within the fiscal year.

The January Governor's Budget includes $39 million for interest costs on budgetary borrowing from the General Fund in 2012-13. The May Revision calls for a decrease in this budget item as a result of paying off fewer budgetary loan amounts. The decrease is $21 million for a revised total of $18 million. The costs for 2011-12 will also decline, from the January figure of $52 million to $35 million. The two-year savings will be $48 million.

STAFF COMMENT

The administration has complied with the direction of the Subcommittee in the May Revision and thus both fiscal letters should be adopted.

Staff Recommendation: Adopt May Revision Fiscal Letter

0950 STATE TREASURER'S OFFICE

ISSUE 1: SCHOLARSHARE

The May Revision includes a provision to revert $63.1 million to the General Fund of funds previously set aside for the Governor's ScholarShare program.

BACKGROUND

As part of the Governor's May Revision, the administration proposes trailer bill language (TBL) to revert $63.1 million to the General Fund of moneys previously set aside for the Governor's Scholarship Program. The funds for contracts are allocated to TIAA-CREF for management and disbursement of approximately $85 million in funds, most of which will eventually be reverted to the General Fund. The $85 million represents unused funds from scholarship grants provided to high school students for performance on standardized tests in 2000 through 2002. This proposal will result in $20 million remaining in the reserve to assure funding for participants. A three percent discount rate is paid by the state to TIAA-CREF to continue with account administration and to offset the early reversion of funds.

The Governor's Scholarship Program was established in 2000 and included two components: a $1,000 scholarship to students who demonstrated high academic achievement on the Standardized Testing and Reporting (STAR) program in the 9th, 10th, or 11th grades; and a $2,500 scholarship to students who demonstrated high academic achievement specifically in math and science on the Advanced Placement (AP) test and other specified exams. Scholarships were awarded without regard to financial need. Due to budget difficulties, the program was repealed in 2003; however, the State continued to honor program obligations for tests taken in 2000-2002. A total of about $313 million was provided from the General Fund for the creation of individual scholarship accounts for each recipient with the funds transferred outside the state treasury and managed by a private financial firm. Awardees can receive disbursements for qualified college expenses, and the funds are transferred directly to the college. Recipients have access to disbursement through age 30, after which time their funds revert to the state General Fund.

The majority of awarded funds have been disbursed for qualified college expenses, but about $85 million remains. Based on program activity, it appears that most awardees have either completed college, or entered the workforce without claiming a disbursement of their award. Under current law, the unused portion of the $85 million will revert to the General Fund over the next seven or eight years as recipients turn age 30. Alternatively, as proposed by the administration, statue could be amended to revert the funds sooner for General Fund relief.

STAFF COMMENT

Given the condition of the General Fund, this proposal makes sense.

The Subcommittee should consider reverting all or most of the roughly $20 million remaining in the ScholarShare account in 2012-13. If the Subcommittee wished to consider this option, a mechanism would need to be developed to insure the State honored its prior obligations.

Staff Recommendation: Adopt May Revision Fiscal Letter

1730 FRANCHISE TAX BOARD

ISSUE 1: TAX COMPLIANCE POLICY CHANGES

The May Revision contains two policy changes that would increase compliance with income tax law and enhance the ability of the tax agency to collect outstanding tax liabilities.

BACKGROUND

The Governor has proposed two policy changes that would result in increased compliance with the state's income tax law and enhance the ability of the tax agency to collect outstanding tax liabilities. The two proposals relate to the ability of earning withhold where the tax liability has not been paid and the establishment of a penalty for the fraudulent filing of a claim for a tax refund. The issues are described more fully below:

1. **Earnings Withhold.** Under current law, the state is authorized to issue a withholding order for taxes to collect an outstanding state tax liability, including any penalties, accrued interest, and costs in accordance with state law and regulation. Currently, "state tax liability" is defined to mean an amount for which the state has a state tax lien created pursuant to specified provisions. The proposal from the administration would streamline and reduce the costs associated with the earnings withhold process. Under the proposal, the term "state tax liability" would be expanded to include any liability under the Personal Income Tax Law, Corporation Tax Law, or specified franchise and income tax provisions that is due and payable and that remains unpaid. The proposal would save the administrative cost associated with recording a lien. It would also allow the tax agency to collect tax liabilities that are over 10 years old. (Tax debts over 10 years old expire unless renewed by recording a lien.) The change is expected to result in additional General Fund revenues of $11 million in the current year and $27 million in 2012-13.

2. **Fraudulent Refund Claim.** Under existing law, the Franchise Tax Board (FTB) imposes certain penalties in connection with tax avoidance and partially conforms to federal law in this respect. The administration proposes that state law be changed to additionally conform to federal law and impose a penalty for filing a fraudulent claim for refund. The corresponding federal treatment imposes a penalty if a claim for refund is made for an excessive amount unless there is a reasonable basis for the claim. The penalty is equal to 20 percent of the excessive amount. The new policy is intended to be further restrict the potential use of abusive tax transactions and tax avoidance schemes. The estimated revenue impact is $1 million in the 2011-12 and $3 in 2012-13.

STAFF COMMENT

The trailer bill proposals from the administration are reasonable efforts to make inroads in the state's existing income tax gap of an estimated $10 billion, while maintaining taxpayer rights. While a tax lien would still be an option for the agency (if for example, wage withholding was not feasible) the proposal would streamline the ability to satisfy established tax liabilities and reduce time and costs. It would also avoid having to place a tax lien on a taxpayer's property. The additional penalty proposed represents conformity with the federal treatment in this area.

Staff Recommendation: Adopt May Revision proposed Trailer Bill Language

0840 STATE CONTROLLER'S OFFICE

ISSUE 1: 21ST CENTURY PROJECT

The 21st Century Project is an extensive revamp of the state's entire payroll processing and related services such as employment history, position management and leave accounting. The State Controller's Office (SCO) is responsible for paying approximately 294,000 state employees through its existing legacy system. This employee population includes state civil service employees, as well as elected officials, judicial council members, judges and the California State University System (CSUS) employees. To support the state's ongoing needs, the Legislature in 2004 authorized the development and purchase of a new system that would provide a technically-advanced solution and create the functions required to support future growth and increased complexities in state government.

This request is for 181 one-year limited term positions and $81.4 million, for additional costs of the program. The funding request is composed of $46.9 million General Fund, $33.5 million special funds, and $1.0 million reimbursement authority. Of the 181 positions, 111 are a continuation of positions approved in a 2011-12 BCP. An additional 70 positions will address new project workload identified in Special Project Report (SPR) 5. These positions are be distributed to those areas (described below) as follows: 16 position in project management, 41 positions in business operations, 49 positions in technical operations, 50 positions in organizational change management, 10 positions in business transition, and 15 positions in other administrative functions. The SCO has indicated that these positions will likely be revised downward, with a corresponding budget request decrease, based on input from California technology Agency (CTA).

MAY REVISION REQUEST

The May Revision adjusts the 21st Century project's budget to reflect expected costs from Special Projects Report 5, resulting in a $1.6 million. With this change, the project would be funded at $79.7 million total cost for 2012-13, with $45.3 million from the General Fund. The May revision also updates Control Section to appropriate the $34.4 million of special funds and reimbursements for the project.

BACKGROUND

Project Governance

Project Governance activities are designed to provide strategic leadership, funding and support while assuring a culture of accountability, transparency and oversight. The Project Governance bodies include a Steering Committee, Business Transformation Council and Configuration Standardization Committee.

- **Steering Committee**. The most senior group in the project governance structure is the Project Steering Committee. This group represents an executive body within the State of California that has a stake in the project. The Steering Committee supports the project by making required statewide decisions on processes and policies. To effectively enable change and manage issues that cross departments, the Steering Committee is responsible for the strategies required for a State government implementation. The

Committee's responsibilities are that business objectives are achieved, that an effective structure exists to consider the interests of stakeholders, that the state/vendor relationship is optimized, and that the project remains under control.

- **Business Transformation Council**. The Business Transformation Council is an advisory group for key business-related issues that affect the way the State operates as it transitions to the project. Its focus is primarily on the adoption by the end-user organizations' HRMS/Payroll functions. The Council may recommend changes to State business regulations and processes to ensure that department interests are represented in system design and reflect uniform best practices. The council examines issues that meet certain criteria and can submit change requests for the project.

- **Configuration Standardization Committee.** The Configuration Standardization Committee is an advisory group that deals with issues that directly affect the configuration of the project. The committee provides guidance and recommendations to the project teams and interface partners regarding potential opportunities for standardizing business practices. The goal of the committee is to meet stakeholder business requirements while limiting enhancements to the project to minimize future costs.

Project Management

The Project Management Office is composed of teams with the objective of moving the project toward successful implementation. The PMO's day-to-day activities and direction to staff include administrative support with budgets, funding and contracts as well as ensuring control agency reporting and compliance. In addition, Project risks, issues, costs and status reporting are developed, monitored and controlled by the office. A quality assurance team performs its duties using methodologies designed to measure the accuracy and success of the project implementation. Advisors with expertise in large-scale IT projects are on hand to provide additional guidance.

Business Operations

The Business Operations team provides expertise in all functional areas of project. These areas include benefits administration, leave accounting, organizational management, payroll processing, personnel administration, and time management. Business operations also conducts the unit and Integration testing of the project system as it is developed. Business operations conducts the analysis of human resources management and payroll processes to validate and document business process design. In addition, business operations configuration activities will align SAP system programs with the State's business processes and identify customization of SAP functions.

Technology Operations

The Technology Operations team provides expertise for all technical requirements for the project. Technology operations is responsible for implementation and operation of project software and hardware, security configuration and validation activities, business warehouse, portal, user roles/authorizations, extraction of legacy data for loading to SAP, development of workflow, and the full development life-cycle activities for reporting, interfaces, enhancements, of SAP programs to ensure the State's business process are met.

Organizational Change Management

Preparing for change is essential for a successful transition of people to new technology and business processes. The organizational change management team provides expertise in preparing the State workforce for the implementation of the project. It works in partnership with the departments through the areas of communications, workforce transition, deployment and end user training to ensure that people receive training and support to be successful in their new environment.

STAFF COMMENTS/QUESTIONS

The 21st Century Project has experienced considerable problems in the past—some related to the magnitude and complexity of the project and some related to the consultants hired to work on the project. Following the termination of a contract with a vendor (BearingPoint) in January 2009 for failure to meet contractual obligations, the SCO awarded a new contract to SAP in December 2009, which was approved in February 2010. After some delay in the execution of the contract, an update to the SPR 4 allowed for certain limited go-live activities to occur in September 2011.

Delays have again been encountered, and SCO proposes for this phase of the project to be implemented June 2012. This is a nine-month delay from the amended SPR 4 and 12-month delay from the approved SPR 4. The most recent SPR 5, submitted in November 2011, incorporates these dates. SCO reports that it could accelerate the total go-live, roll-out, but this would substantially increase the system risks. SCO reports that this acceleration would result in "substantial resource over-allocation, particularly from the functional team." In other words, this plan may be too much, too soon.

In 2005, the Legislature approved the project with an estimated total cost of $130 million. Total project costs provided in SPR 4 were $305 million, largely based on program additions. This estimate had increased to $370 million by the date of SPR 5. The increase is comprised of $23.2 million in personal services and $43.9 million in OE&E (the increase in consulting and professional services component of OE&E was $29.0 million). The chart below indicates actual costs to date and project costs in the future (shaded). According to the pro-formas presented below (estimated costs in shaded area), 2012-13 will be the high cost year at $81.4 million, as reflected in this BCP.

21st Century Project Costs and Funding ($ millions)

Year	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	Total
Project Costs	1.4	4.9	11.6	35.8	19.1	19.6	31.4	65.6	64.0	81.4	33.2	5.1	370.2
General Fund	0.0	0.0	0.0	18.1	9.9	11.8	16.2	30.3	34.5	46.9	6.5	0	174.2

Subsequent to the preparation of the BCP, the CTA reviewed the project as compiled by SCO and in conjunction with the SCO reduced the request by $1.6 million and reduced the proposed number of new positions by 29. Once the revise proposal is reviewed by DOF, it will be provided to the Legislature for action. Staff recommends this item be left open pending the decision by DOF on cost revisions for the proposal.

Staff Recommendation: Adopt May Revision Proposal

ISSUE 2: MYCALPERS

The May Revision requests $1.5 million in 2012-13 and 15 two year limited-term positions for workload associated with the temporary data incompatibility between the SCO and PERS computer systems.

BACKGROUND

When CalPERS implemented its MyCalPERs system in 2009, the new system recorded tens of thousands of "fallout records" errors that needed to be reviewed manually. A "fallout record" occurs when the data received from the Controller does not match the data in the CalPERS computer records. These "fallout errors" are expected to continue until the Controller implements the 21st Century Project. CalPERS also reports that it is working on automation fixes in the hopes to reduce the number of these errors.

The May Revision requests $1.5 million and 15 two-year limited term positions to address these fallout records. The Controller's office says that it reassigned staff from other SCO areas to cover this workload, but it has started to accrue backlogs in these other areas as a result of this redirection and thus believes dedicated resources should be identified to address this problem. The May Revision proposal includes budget bill language to allow the Department of Finance to reduce the staffing levels if this workload diminishes.

STAFF COMMENT

Staff believes that while the data incompatibility should have been foreseeable during the implementation of the MyCalPERs system by CalPERS, the Controller's Office does not have any remedy to avoid absorbing this temporary workload.
Staff recommends that the Subcommittee approve half of the proposal on a two-year limited term basis to address this backlog.

Staff Recommendation: Adopt 7 positions on a two-year limited term basis

ISSUE 3: COMPUTER ASSOCIATES INTEGRATED DATA MANAGEMENT SYSTEM (CA-IDMS) COST ADJUSTMENT

The May Revision includes a revised support costs for CA-IDMS costs.

BACKGROUND

The May Revision updates costs for O-Tech to support the CA-IDMS system at the Data Center. The update results in additional costs of $201,000 ($47,000 General Fund) in 2011-12 and $902,000 ($207,000 General Fund) in 2012-13.

STAFF COMMENTS

This request is a result of O-Tech rates being adjusted to reflect actual costs at the California Technology Agency.

Staff Recommendation: Adopt May Revision Letter

ISSUE 4: INDEPENDENT REVIEW OF AIRPORT FACILITY FEE AUDITS

On May 9, 2012, the Subcommittee took action to continue the State Controller's role in the auditing of airport fee collection. This issue revisits that action.

BACKGROUND

The Governor's Budget proposes trailer bill language (TBL) that would eliminate the requirement that the Controller's Office independently review and report to the Legislature regarding the results of audits required to be conducted by airports with respect to the collection of fees to fund consolidated rental car and other transportation facilities. Under SB 1192 (Oropeza), Chapter 642, Statutes of 2010, the Legislature expanded the definition of customer facility charge to include a fee to be collected for the purpose of financing common-use transportation facilities and thus allowed the collection of an alternative fee, if necessary, for funding purposes. The bill also requires that airports that collect the fee to report certain information to the Legislature and complete a specified independent audit at particular intervals. The Controllers' Office is to independently examine the audits and substantiate the necessity for the customer facility charge. The Controller is to report the finding to the Legislature and expenses of the review are paid by the airports.

The authority to collect the customer facility fee began in 1999 with special approval for such collection granted to international airports at San Jose, San Francisco and San Diego. The legislature expanded this to other public airports in 2001 and 2007. Under the program, each airport is required to complete an independent audit to ensure the aggregate amount of fee revenue does not exceed the reasonable costs paid by the airport to finance the design and construction of consolidated car rental facilities and common-use transportation systems. In 2010, the Legislature required that SCO review the audits and independently examine and substantiate the necessity of the customer facility fee. Thus, the audits will ensure that the fee (not to exceed $10 per contract) charged to airport car renters is not excessive.

One two-year, limited term position was funded, resulting in $140,000 in reimbursement authority for 2010-11 and $134,000 for 2011-12 to conduct mandated independent reviews of the audits. The limited-term position expires at the end of this fiscal year. The SCO proposed to continue the funding in order to fulfill the independent review required by statute. The administration has proposed TBL to eliminate the review requirement.

To date, the SCO has conducted an independent review of three independent CPA audits of the charges. The reviews reviewed undercharges and overcharges. For the Burbank-Glen date-Pasadena Airport Authority Audit, the review revealed that the Authority could have charged $4.4 million more than it actually did. Two other reviews—San Jose Intonation Airport and Fresno-Yosemite International Airport—reveal overcharges of $19.5 million and $7.0 million, respectively. The overcharges were the result of unrecognized income and overstated costs.

STAFF COMMENTS/QUESTIONS

The Subcommittee took action to reject this proposal and continue the authority and positions on May 5, 2012. This was in part due to the results of the SCO's independent review of the independent audits indicates the presence of discrepancies between justifiable charges and fees actually collected.

Since that time, representatives from the airports have come forward to suggest that the SCO audits had serious flaws and that the airports were concerned that expanding this authority would be disruptive. Given the feedback from the airports, staff recommends rescinding the prior action and adopting the administration's proposal. This action would eliminate $80,000 in reimbursement authority and 0.5 positions as well as Trailer Bill Language that would eliminate this auditing requirement prospectively.

Staff Recommendation: Rescind Prior Action and Adopt Governor's Budget proposal to reduce .5 staff and corresponding Trailer Bill

ISSUE 5: FRAUDULENT CLAIMS DETECTION AND PREVENTION PROGRAM

The Governor's Budget includes a proposal for a new Fraud Claims Detection and Prevention Program for the Unclaimed Property Fund.

BACKGROUND

The SCO has requested $2.3 million in permanent funding from the Unclaimed Property Fund and 17.9 permanent positions to establish a fraud detection unit within the Unclaimed Property and Information Systems Divisions. The fraud detection approach will include database application changes and enhancements to implement upfront authentication activities, contracted services that would perform independent verification for certain claims, and a fraud unit of analysts who would develop and implement protocols for fraud detection. The committee heard this issue at its March 20 hearing and held it open at that time.

According to SCO statistics, fraudulent claims show a very erratic pattern over the last fours, ranging from two in 2007-8 to 1,017 in 2010-11. The dollar amount of theses fraudulent claims was $122,470 and $3.3 million for each of those years, respectively. On the other hand, the SCO was successful in detecting a good number of these claims, since its data indicates that only $2.9 million was paid out in fraudulent claims between 2000 and 2011. SCO has conducted an analysis of fraud in other industries and has reviewed efforts in other states. Based on the application of these data, SCO estimates that the actual number of fraudulent claims would be on the order of 7 percent, or $17.5 million of about $250 million in annual claims.

STAFF COMMENTS/QUESTIONS

It is not clear that the data used for various industries (health care and property insurance) are applicable in the context of unclaimed property. In addition, SCO data indicates that only $2.9 million in fraudulent claims were paid between 2000 and 2011, out of $6.2 million fraudulent claims filed. Understanding that estimation is difficult in this context, the SCO may find a better means of looking at past data and claims to get a sense of the actual number and value of fraudulent claims.

At its March 20 hearing, concerns were expressed regarding initiating a full-scale program without first establishing a trial or pilot program on a smaller scale. Once the scope of the problem is identified, the creation of models that would lead more fruitful auditing and detection of claims could be initiated. This approach is generally used in the tax field in order to detect ineligibility for tax credits, excessive deductions, and transfer-pricing abuses. The committee may want to explore whether a smaller pilot should be established to help define the problem more thoroughly and develop a systematic approach. A program half the size with limited term positions and a report to the Legislature would be one approach.

Staff Recommendation: Recommend SCO establish a pilot program with two year limited-term positions and SRL to the Legislature after a full year of operation.

0860 BOARD OF EQUALIZATION

ISSUE 1: CENTRALIZED REVENUE OPPORTUNITY SYSTEM (CROS)

The May Revision proposes $23.8 million ($14.6 million General Fund) and 156.7 positions in 2012-13 and $29.1 million $18.1 million General Fund) and 242.1 positions in 2013-14 for the beginning stages of a new centralized data and tax collection system.

BACKGROUND

The May Revision proposes $23.8 million ($14.6 million General Fund) and 156.7 positions in 2012-13 and $29.1 million $18.1 million General Fund) and 242.1 positions in 2013-14 for the beginning stages of a new centralized data and tax collection system. The initial stage of the project would largely address the beginning implementation stage of the project, maintain the existing legacy systems, address data conversion issues, address external interface issues and engage in certain tax compliance and enforcement activities. While the initial phase of the project relates to preparatory work, the final product will result in combining several of the department's existing systems and provide a centralized and unified tax collection and data system. The project is designed to generate revenue during its implementation and will be structured based on "alternative procurement" in that it will be benefits-funded. During the initial two years, the project would result in additional revenue of $38.8 million in 2012-13 and $66.5 million in 2013-14

BOE's current automation systems were developed in the 1990s. The hardware and software which supports these systems is dated and more costly to maintain than newer technologies. Additionally, because BOE's systems have required continuous modifications over the last ten years, there has also been a significant, and steady, increase to the costs, staffing resources and time involved to make changes, enhancements or maintain these systems. The programming language is outdated and it is becoming increasingly difficult to find staff, or contractors, to maintain the systems. The current systems are antiquated, do not have the capability to easily adapt to new or expanding requirements, and cannot adapt or take advantage of emerging technologies.

As the systems have become more dated, workload has increased. Over the recent past, BOE has been directed to implement several new tax and fee programs or other proposed statutory changes. Each of these statutory changes or new programs requires significant programming hours to modify the existing automation systems. Any new implemented tax program uses the same computer components as our existing tax programs while in use by BOE's multiple tax programs. Multiple programming changes are difficult to accomplish since programming components are tightly integrated and changes to the components disrupt existing tax program activities. Implementing a new tax and fee programs can take as long as ten months to complete with existing systems. In addition, the department is increasingly experiencing frequent and recurring requests for statistical data or quantitative information.

BOE has developed a number of ad hoc methods and ancillary systems to respond to these information requests. Extracts from the department's principal systems--Integrated Revenue Information System (IRIS) and Automated Compliance Management System (ACMS) are stored with data received from external agencies in data marts and reports are created utilizing desktop applications. The difficulty in accessing BOE internal data and the ability to only perform one-source data matching is cumbersome and often detrimental in responding timely to requests and performing program analysis. Requests still require programming expertise and are expensive and time consuming to perform. BOE does not have the business intelligence tools required to provide the requestor or client access to the information that is required to complete necessary business processes in a timely and cost effective manner.

To address this, BOE proposes a significant automation project which will ultimately replace IRIS and ACMS, its two current automation systems. In addition, the project will expand online taxpayer services and provide an enterprise data warehouse. This project will impact virtually all processing areas within the organization. The new technologies and tools will provide increased efficiency and will augment revenue production while incorporating "best practices" to reengineer how work is performed. Replacement of the legacy systems should improve the BOE's performance. Additionally, the integration of a data warehouse would provide a single enterprise repository of BOE internal data and external data.

MAY REVISION PROPOSAL

The May Revision proposes $23.8 million ($14.6 million General Fund) and 156.7 positions in 2012-13 and $29.1 million $18.1 million General Fund) and 242.1 positions in 2013-14 for the beginning stages of a new centralized data and tax collection system For the budget year 2012-13, roughly $12.3 million will constitute personnel services with the balance ($11.5 million) used for operating expenses and equipment (OE&E). A large portion of the OE&E—slightly less than $5 million—is for consulting services and data center services. About a third of the personnel will be directly involved in the CROS project, which in this phase is concentrated on project direction and generally relate to data cleansing and preparing for conversion to the new system. The positions, in addition to administrative project-direction positions--include software specialists, programmers, and system analysts. Performing much of this work in-house, as opposed to by the vendor--is expected to reduce overall project costs.

At the same time the activities related to the implementation of the CROS are occurring, other personnel will be addressing the accumulated backlog of activities that need to be addressed in preparation for the new integrated system. Significant backlogs have been identified in the areas of audits, collections, Statewide Compliance and Outreach Program (a BOE tax gap program), offers in compromise, and settlements. Addressing the backlogs in these areas generates the revenues identified in the proposal. In addition, addressing the backlogs also makes the project itself more feasible by improving the quality of the data prior to system implementation.

STAFF COMMENT

The department's current proposal is much improved from earlier draft versions. Technology and data system improvements at BOE are overdue. Its technology systems are clearly dated and expensive, and the current proposal is a reasonable start in the process of modernization. The department has pursued benefits-funded approach that has been recommended in the past and has also reviewed the plan with other agencies in order to benefit from lessons learned. In particular, the department has consulted with the Franchise Tax Board, which has been generally successful with its various technology modernization projects. The short-term benefit/cost ratio does not meet historical standards, but the project is based not on short-term returns, but rather longer-term benefits. In addition, the benefit/cost ratio is generally in keeping with FTB's similar technology upgrades. Staff recommends an interim report for this project that would allow the Legislature to evaluate progress in conjunction with subsequent budget requests the department indicates will be forthcoming. The proposal may also benefit from additional vetting of the estimated revenue generated by the project. This could be incorporated as part of the reporting language.

ALTERNATIVE IMPLEMENTATION PLAN

At the request of Senate staff, the BOE has provided an alternative proposal to delay starting the CROS automation component until 2013-14 but begin work on the revenue aspect and backlog in 2012-13. This adjustment would not reduce the overall project implementation timeline. Under this revised timeline, BOE would reduce the proposal by 28 percent or 43.7 positions. A majority of these positions are under the CROS proper component, including the subject matter experts (SMEs) that will be drawn from the program. BOE believes it can delay starting the SMEs portion of this project until the second year and still achieve the desired revenue of $38.8 million in the 2012-13 and $66.5 million in 2013-14.

According to BOE, through the use of cleaner, synthesized data and additional revenue sources identified through the early initiatives in CROS proper, BOE will be able to improve their audit selection and collection modeling. These improvements will result in identifying productive cases to work for the additional staff in SUTD – generating the $38.8 million in FY 2012-13 and $66.5 million in FY 2013-14.

Staff Recommendation: Adopt Alternative Implementation Plan

2240 DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT
0820 DEPARTMENT OF JUSTICE
1700 DEPARTMENT OF FAIR EMPLOYMENT AND HOUSING

ISSUE 1: NATIONAL MORTGAGE SETTLEMENT PROCEEDS

May Revision. The May Revision proposes to use $292.2 million in discretionary funds received by the state in the National Mortgage Settlement to pay for programs in FY 2011-12 and FY 2012-13 that benefit California homeowners affected by the mortgage and foreclosure crisis and other consumers. Specifically, the proposal would use $41.1 million for the Unfair Competition Law Fund to offset Department of Justice (DOJ) programs, $44.9 million to support the DOJ's Public Rights and Law Enforcement programs, $8.2 million for the Department of Fair Employment and Housing's efforts to address housing discrimination, and $198 million to cover housing bond debt service in Department of Housing and Community Development bond programs that assist homeowners. The administration states it will propose to use another $118.4 million in 2013-14 in a similar manner.

BACKGROUND

California, 48 other states and the federal government reached a settlement on February 9, 2012 with five major mortgage lenders that provides $25 billion for relief for distressed homeowners in the form of modifications, mortgage loan servicing reforms, increased compliance monitoring and enforcement. The settlement could bring as much as $18 billion in support for California homeowners. In addition, the state will receive about $411 million in 2011–12.

Language included in the settlement gives considerable latitude to the state in how it can use the $411 million:

"The payment to the California Attorney General's Office shall be used as follows: a) Ten percent of the payment shall be paid as a civil penalty and deposited in the Unfair Competition Law Fund; b) The remainder shall be paid and deposited into a Special Deposit Fund created for the following purposes: for the administration of the terms of this Consent Judgment; monitoring compliance with the terms of this Consent Judgment and enforcing the terms of this Consent Judgment; assisting in the implementation of the relief programs and servicing standards as described in this Consent Judgment; supporting the Attorney General's continuing investigation into misconduct in the origination, servicing, and securitization of residential mortgage loans; to fund consumer fraud education, investigation, enforcement operations, litigation, public protection and/or local consumer aid; to provide borrower relief; to fund grant programs to assist housing counselors or other legal aid agencies that represent homeowners, former homeowners, or renters in housing-related matters; to fund other matters, including grant programs, for the benefit of California homeowners affected by the mortgage/foreclosure crisis; or to engage and pay for third parties to develop or administer any of the programs or efforts described above."

The administration states that it is targeting the funding to departments and programs that assist homeowners. For example, the administration determined that 26 percent of the work done by the Department of Fair Employment and Housing's relates to its efforts to prevent and eliminate unlawful discrimination in housing and prosecution of housing violations under the Fair

Employment and Housing Act. Thus, 26 percent of the department's expenditures will be offset by the settlement funding.

Similarly, settlement money used to pay debt service on housing bonds is being used only in bond programs associated with home ownership, such as the CalHOME program, which provides grants to local public agencies to assist households through deferred-payment loans.

The Department of Justice program proposed for mortgage settlement funding includes work the department does on mortgage fraud investigation and enforcement.

All funds would offset General Fund expenses. Below is a table showing the department and program, and proposed funding through 2013-14:

Department/Program	**2011-12 Proposed Funding**	**2012-13 Proposed Funding**	**2013-14 Proposed Funding**
Administrative Fee (10% of amount available to state)	$41.1 million	$0	$0
DOJ, Program 20.30 Public Rights	$12.4 million	$18.8 million	$18.8 million
DOJ, Program 50.15 Office of the Director	$7.7 million	$0	$0
DOJ, Program 50.25 Bureau of State Investigations	$0	$6 million	$6 million
Dept of Fair Employment and Housing	$4 million	$4.2 million	$4.2 million
Proposition 1C and Proposition 46	$106 million	$92 million	$89.5 million
Totals	**$171.2 million**	**$121 million**	**$118.5 million**

STAFF COMMENT

States involved in the settlement have used payments in varied ways, according to a report by the National Conference on State Legislatures. Some examples:

- Georgia is using $99 million for economic development efforts.
- Utah is using $1.8 million for homeless shelters and services, $2 million for mortgage fraud investigations, and $18.2 million was directed to the state's General Fund.
- Indiana used $28.8 million for its Low Income Home Energy Assistance Program and another $15 million for efforts to prevent mortgage foreclosure.

LAO Comments. The LAO provided the following comment on this issue in its analysis of the May Revision: "Given the state's current fiscal situation and the magnitude of General Fund savings achieved, we find that the Governor's proposal merits legislative consideration. However, some of the proposed expenditures could fall outside the intent of the settlement agreement to the extent that they do not directly relate to consumer fraud, borrower relief, services for homeowners, or other permitted uses. For example, the administration proposes to fully supplant General Fund support for DOJ's Division of Law Enforcement, which conducts investigations into organized crime, gangs, and drug trafficking. The Legislature will want to consider any potential legal risks associated with using the settlement proceeds for the proposed purposes."

Trailer Bill Language implementing this proposal has not yet been released by the administration. The Subcommittee may wish to hold this item open until more details are available.

Staff Recommendation: Hold Open

CONTROL SECTION 3.90 EMPLOYEE COMPENSATION

ISSUE 1: REDUCTION OF EMPLOYEE COMPENSATION

May Revision. The May Revision proposes a decrease of $839.1 million ($401.7 million General Fund) in employee compensation, equivalent to about a 5 percent reduction in pay. The proposal seeks Budget Bill Language allowing the administration to achieve the savings through collective bargaining or other means.

BACKGROUND

The total number of state employees is 341,783, resulting in a salary cost of $24.8 billion (including all funds). This tally includes employment at the Executive Branch, Judicial Branch, University of California (UC) and California State University System (CSUS), and elected members of the Legislature. Roughly, two-thirds of total state employment is in the Executive Branch. Of this proportion, about one-third of Executive Branch employment is in the California Department of Corrections (CDCR).

Compensation for salaries and benefits accounts for approximately 11 percent of General Fund costs, and includes $7 billion in salary expense and $3.3 billion in benefit costs. Employees of CDCR account for approximately two-thirds (64%) of General Fund salary costs.

Recent administrations have addressed budgetary savings through reductions in employee compensation. To date, savings in employee compensation has been achieved through unpaid leave days (furlough days and the personal leave program (PLP), retirement changes (increased employee contributions and a new formula for new state employees). Other measures adopted as part of collective bargaining, which could increase expected out-year costs, include annual floating paid leave days, future pay increases for top step employees in the future, and continuous appropriation of salaries during late budgets.

The administration states in the May Revision summary that it intends to work with labor organizations in the coming weeks to achieve the proposed savings. It also states that it will work "to avoid furloughs and to mitigate layoffs," and to propose a four-day, 38-hour workweek for many state employees. In addition, changes in employee and retiree health coverage to offset rising state health care costs will be pursued.

STAFF COMMENT

LAO Comments. The LAO states concerns with the proposed four-day workweek, noting that it could increase unpaid leave balances and hinder services. It also notes that bargaining necessitates concerns and could produce offsetting costs, layoffs take months to achieve and impact states services, furloughs and leave programs add future costs, and the administration's proposed Budget Bill Language could impact state employees without undergoing collective bargaining.

Because this is a complex issue with potentially large impacts on the state and the state's 21 bargaining units, the Subcommittee may wish to defer action until a more vigorous discussion can occur.

Staff Recommendation: Hold open

CONTROL SECTION 31.10 BUDGET DISPLAY ADJUSTMENT

ISSUE 1: POSITION, COST ADJUSTMENTS, CREATION OF CONTROL SECTION 31.10

May Revision. The May Revision proposes to eliminate more than 11,000 historically vacant positions and make other changes to more accurately reflect departments' spending and improve state government transparency. These changes are cost-neutral.

BACKGROUND

According to the Legislative Analyst's Office, when a position is vacant or filled by an employee at a pay level lower than the department's budget assumes—the department captures "salary savings." Since the early 1940s, the state budget has assumed that most departments have "normal salary savings" — historically, assuming vacancies equal to about five percent of authorized personnel—and reduces departments' personnel budgets accordingly. Excess salary savings —savings from vacant positions in excess of normal salary savings — typically can be used for personnel or operations expenditures but are displayed in a department's personnel budget.

This can result in departments' budget displays inaccurately showing higher personnel costs and lower operational costs.

A department-by-department review of historic staffing vacancies identified 11,709.2 positions that the administration proposes to eliminate. According to the LAO, vacancy rates for many state departments have risen during the past several years for a number of factors, including:

- Unallocated Cuts. The Legislature has approved many unallocated cuts, especially to General Fund departments. When implementing unallocated cuts, the administration chooses how to achieve the reduction. We understand that it is common for departments to hold positions vacant to absorb unallocated cuts. As a result, departments largely funded by the General Fund have noticeably higher vacancy rates than special fund departments.

- Leave Cash Outs. The number of state retirements has increased as employees of the baby boom generation reach retirement age. Upon retirement, the state must compensate (or cash out) an employee for certain unused leave days. Generally, departments do not receive supplemental appropriations to cover these costs. Some departments cannot absorb these costs without holding positions vacant.

- Overtime Costs. Some departments, especially those with 24–hour institutions, consistently incur high overtime costs. Like leave cash outs, departments sometimes do not receive supplemental appropriations for these costs. Departments with high overtime costs often have high vacancy rates to generate excess salary savings.

Instead of continuing these practices, which result in less transparency in how the state spends money, the administration seeks to eliminate vacant positions and improve the accuracy of budget displays by eliminating normal salary savings and showing where that money is actually spent. The result of this would:

- Eliminate 11,709.2 authorized positions and $1.1 billion in displayed salary costs;
- Increase 669.4 temporary help positions and $137.2 million in temporary help funding;
- Increase $62.6 million in overtime funding;
- Increase $6 million in staff benefit costs;
- Decrease $55 million in operating expenses and equipment;
- And, increase $909.9 million to reflect the elimination of salary savings.

The administration also seeks to revise Control Section 29.00 to reflect a new method of displaying position information in the budget, and to create Control Section 31.10, to allow the Director of Finance the authority to adjust positions further if subsequent adjustments to department's position elimination totals are necessary.

STAFF COMMENT

LAO Concerns. The LAO states that this proposal has merit, but recommends rejecting it because it would be impossible for the Legislature in the next few weeks to review every position slated for elimination.

According to the administration, every position proposed for elimination was determined to have been historically vacant, suggesting departments have determined ways to perform department missions without the position. In addition, this proposal would mark a major improvement in state government transparency.

Staff Recommendation: Approve the May Revise request to eliminate historically vacant positions, revise Control Section 29.00 and create Control Section 31.10

CONTROL SECTION 3.60 CONTRIBUTIONS TO PUBLIC EMPLOYEES' RETIREMENT

ISSUE 1: INVESTMENT AND RETIREMENT RATE ADJUSTMENTS

May Revision. The May Revision proposes a General Fund increase of $202.1 million, special funds increase of $101.6 million, and nongovernmental cost funds increase of $51.1 million for retirement rate adjustments.

BACKGROUND

Control Section 3.60 sets the employer rate of contributions for retirement benefits. The proposed increases are due to the following two factors:

- **Investment Rates.** On March 14, 2012, the CalPERS Board voted to adopt a decrease in the assumed investment rate of return from 7.75 percent to 7.5 percent. This adjustment accounts for most of the proposed General Fund increase - $173 million.

- **Retirement Rates.** Employee retirement rates are above those assumed earlier in the year and result in an increase of $29.1 million General Fund.

As a result of $202.1 million General Fund adjustment, the fourth quarter payment to CalPERS that is deferred from 2012-13 to 2013-14 will increase by $50.5 million. The adjustment less the $50.5 million deferral results in a total net increase of $151.5 million to the General Fund in 2012-13 under the administration's proposal.

This request also includes amendments to Control Section 3.61, which was proposed in the Governor’s January budget to stop making base adjustments to reflect changing retirement costs at California State University (CSU) and instead shift added costs to CSU's unrestricted base budget. However, both Assembly Budget Subcommittees No. 2 and this Subcommittee rejected the proposal, given that CSU has little control over benefit structures in the short term.

STAFF COMMENT

The CalPERS Board voted on May 16, 2012, to set the state’s required 2012-13 employer contribution at a level over January budget that necessitates an increase of $124.2 million General Fund (and $93.6 million other special funds and nongovernmental cost funds).

This level reflects a CalPERS Board action to phase-in the impact of the lessened investment rate of return by amortizing the increase over a 20-year period. Under the phase-in, the payment in year one is roughly 55 percent of the payment that would have been required without the phase-in. This will result in increased costs of $145.9 General Fund million during the next 20 years. The CalPERS Board indicates the phase-in was adopted to provide employers with more time to adjust to the higher contribution rates.
Under the phase-in approach, the fourth quarter payment to CalPERS (which was deferred to 2013-14) will increase by $31.1 million.

Per the CalPERS board vote, the state will contribute $124.2 million General Fund for employee retirement costs instead of the $202.1 million the Governor proposed in the May Revise.

Staff recommends approving the phase-in approach to cut General Fund costs in 2012-13. In addition, to conform with previous actions taken by Assembly Budget Subcommittee No. 2 and this Subcommittee, the Subcommittee should direct the Department of Finance to include adjustments to CSU retirement costs in Control Section 3.60.

Staff Recommendation: Approve an increase of $124.2 million General Fund ($93.6 million other funds) over the January budget level in order to fund the state's required employer contribution to CalPERS in 2012-13 with Budget Bill Changes to Conform to Prior Subcommittee Actions.

1900 CALIFORNIA PUBLIC EMPLOYEES RETIREMENT SYSTEM

ISSUE 1: CALPERS HEALTH BENEFITS PROGRAM

May Revision. The May Revision proposes to eliminate Control Section 4.21 and increase General Fund expenditures by $45.4 million, special fund expenditures by $15 million and other nongovernmental costs funds by $7.4 million to reflect the final outcome of implementing Control Section 4.21.

BACKGROUND

This item was first discussed at the Subcommittee's March 7, 2012 hearing.

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.*

Through notifications to the Joint Legislative Budget Committee, CalPERS has reported that it has achieved savings based on this Control Section, but not in the amounts proscribed. Savings appear to be $34.7 million General Fund and $13.3 million in special funds and other nongovernmental costs. The administration's request notes savings were not achieved due to significant year-over-year increases in anticipated premium rates for 2013.

Staff Recommendation: Approve the May Revise request

9800 AUGMENTATION FOR EMPLOYEE COMPENSATION

ISSUE 1: AUGMENTATIONS, BARGAINING AGREEMENTS AND CAPS ADJUSTMENT

May Revision. The May Revision proposes increases in employee compensation resulting from updated health care enrollment figures, projected health care premium increases, and updated salary surveys affecting the California Association of Highway Patrolmen (Bargaining Unit 6) and judges. The administration also is seeking legislative authorization of addenda to extend the contract with Bargaining Units 12, 16, 18 and 19.

The Subcommittee also can consider approving a new budget bill control section to appropriate funds to adjust salaries for 14 supervisory scientist classifications per Government Code 19826.

BACKGROUND

Item 9800 in the budget allows for adjustments in departmental budgets to account for changes in employee compensation, including salaries, health and retirement benefits.

This proposal would increase Item 9800-001-0001 by $10.9 million to reflect increases to General Fund costs, Item 9800-001-0494 by $4.1 million to reflect increases in special fund costs, Item 9800-001-0988 by $2 million to reflect increases to nongovernmental cost funds. The increases are due to updated health care enrollment figures, projected health care premium increases, and updates salary surveys impacting the CHP and judges. In addition, health care premium costs are being adjusted to reflect adjustments to Bargaining Units 12 and 18 based on agreements with the administration.

The administration also is seeking legislative ratification of addenda to contracts with Bargaining Unit 12, craft and maintenance, Bargaining Unit 16, physicians, dentists and podiatrists, Bargaining Unit 18, psychiatric technicians, and Bargaining Unit 19, health and social service professionals. The addenda would extend the contracts through July 1, 2013.

Additionally, the Subcommittee can consider a "like pay-like work" salary adjustment for 14 supervisory scientist classifications. Beginning in 2006, the supervisory division of the California Association of Professional Scientists has argued their members were performing similar work as certain engineering supervisors and should be paid similar salaries. The Department of Personnel Administration (DPA) held a hearing on the issue and on April 28, 2008 recommended salary increases for the supervisory scientist classifications.

Despite this ruling, the classifications have never received an increase. This salary adjustment has never been included in a Governor's January budget proposal. If the adjustment were made for Fiscal Year 2012-13, it would add $10.6 million in costs, with only $1.6 million coming from the General Fund.

STAFF COMMENT

Staff has no concerns with the administration's proposals.

With regard to the supervisory scientist classifications, litigation involving CAPS and the state over this issue led to a state Court of Appeals decision in May 2011. The court found that the Department of Finance has no obligation to fund DPA-approved budget changes, but that Government Code Section 13337 states that the information should be provided to the Legislature to allow it to make additional appropriations to fund proposed salary changes. On June 20, 2011, DPA asked the Department of Finance to provide the salary change in the budget and provide information to the Legislature. That has not yet occurred.

To address the DPA ruling that is now more than four years old, staff recommends creating a new budget bill control section to allow the salary changes.

Staff Recommendation: Approve the proposed compensation adjustments and language authorizing the addenda to contracts with Bargaining Units 12, 16, 18 and 19. In addition, approve a new budget bill control section to appropriate the funds necessary to adjust salaries for the 14 supervisory scientist classifications.