Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Richard D. Roth, Chair
Senator Steven M. Glazer
Senator Janet Nguyen
Senator Richard Pan

Wednesday, March 30, 2016
10:30 a.m.
State Capitol - Room 3191

Consultant: Samantha Lui

PART B

PROPOSED FOR VOTE-ONLY

PROPOSED FOR DISCUSSION

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ISSUES PROPOSED FOR VOTE-ONLY

0845 DEPARTMENT OF INSURANCE

Issue 1: Principle-Based Reserving (SB 696) and Budget Bill Language

Budget. The department requests $925,000 (Insurance Fund) in the budget year, and $894,000 (Insurance Fund) ongoing, for five positions to implement workload related to Principle-Based Reserving (PBR). The five positions include:

- One senior life actuary to design the audit plan and oversee audit schedules and timelines.
- One statistical models analyst III to review PBR modeling programs.
- One chief systems actuary.
- One senior programmer analyst to evaluate the software scripts.
- One software systems specialist III to lead actuaries in evaluating data structure, relevance, and organization.

The department also proposes budget bill language, which provides that resources, previously approved for PBR implementation ($41.4 million and nine positions), will be reconsidered if, by June 30, 2017, a super-majority of states that represents 75 percent of the total U.S. premium do not adopt PBR. In addition, the proposed language requires the department to update the Department of Finance and the Legislature on the status of national adoption.

Background. PBR is a stochastic model that requires forecast-based mathematical models, which rely on credible past company experience. The PBR methodology is beneficial to insurers and industry because it allows life insurers to set and hold insurance liabilities reflective of their life insurance past experience. PBR introduces the use of actuarial judgment in allowing insurers to determine life insurance reserves. The stochastic reserve is based on net cash flows projected under multiple economic scenarios based on randomly generated future interest rates and equity return assumptions.

Senate Bill 696 (Roth), Chapter 658, Statutes of 2015, conforms California law to the Standard Valuation Law, adopted by the National Association of Insurance Commissioners (NAIC), and replaces the current method of calculating reserves for most life insurance products with a new method known as PBR applicable to specified contracts.

During the 2014-15 budget, the department received conditional approval to prepare for the implementation of the PBR and was authorized $463,000 in 2015-16, for four new positions (one senior life actuary and three analysts). Currently, none of the four positions are filled. These resources were based on initial estimates and are intended to cover the workload associated with preparing the department to act.

PBR will become operative on January 1 of the year after 42 states that represent at least 75 percent of total U.S. premium adopt the policy. Policies issued prior to the adoption of PBR, or not covered by PBR, will still be covered by the current standard valuation laws.

Staff Comment. Once PBR is operative, the NAIC Valuation Manual allows up to a three-year transition to give insurers time to implement PBR for future sales. This implementation period provides the department additional time to create policies and procedures, recruit and train the necessary staff on insurance stochastic modeling. However, the department notes that it is possible the initial PBR submissions will arrive in March 2017.

As November 13, 2015, 39 states and six territories have adopted PBR, representing an amount just short of the 75 percent required. The department is currently tracking seven other states that are likely to approve PBR by June 30, 2016.

The department may wish to clarify how previously approved resources, if PBR is not adopted by the required number of states, will be "reconsidered."

Staff Recommendation. Approve as requested, including the budget bill language in draft form.

Issue 2: Life and Disability Policies (AB 387)

Budget. The department requests $430,000 (Insurance Fund) in the budget year, and $270,000 (Insurance Fund) ongoing, for two attorney positions to comply with associated workload implementing Assembly Bill 387 (McCarty), Chapter 691, Statutes of 2015.

Background. AB 387 (McCarty) contains the following provisions:

- Extends the period of time for the Insurance Commissioner to review disability insurance policies from 30 to 120 days.
- Requires the Commissioner to request a study comparing California insurance standards with those developed by the Interstate Insurance Product Regulation Compact, and prohibits the use of General Fund or Insurance Fund for the report. The study must be completed by January 1, 2017.
- Authorizes the Commissioner to publish checklists and guidelines for policy form requirements.

Disability and life insurance policies are subject to statutory standards. For some types of insurance, the Insurance Commissioner must affirmatively approve the forms before the insurer issues contracts based on those forms. For other types of insurance, the insurer must submit the form but may issue policies after a waiting period without affirmative approval. In either case, the insurer must stop issuing policies based on that form if the Commissioner subsequently disapproves the form.

Insurers must file forms for disability insurance. If the Commissioner notifies the insurer that the form does not comply with required standards, the insurer must fix the form and get approval before issuing policies. If the Commissioner affirmatively approves the form, or 30 days passes without notice, the insurer may issue policies under that form. Traditionally, the statute has been read so that the Commissioner would have discretion to review a policy or not. The California Court of Appeal, in *Ellena v. Department of Insurance* (2014), held that the Commissioner has a mandatory duty to review each disability insurance policy. That decision has created a substantial new workload in the department's policy review process. AB 387 bill addresses the additional workload by extending the review period to 120 days.

Staff Comment. While this increases the number of days for review, CDI needs additional resources to comply because the department had previously not interpreted the 30 days as a "real" deemer date. The department notes it has "no control over how many filings come in each month and has no control over the size and complexity of those filings, and accordingly, does not have sufficient resources to comply with the new 120 days." During the period of April 1, 2014, to April 1, 2015, the department received an average of 115 new filings each month. Some filings consist of one, three-page document, while others consist of 15, 30-page documents.

Staff Recommendation. Approve as requested.

Issue 3: CDI Menu Modernization Project (CMMP) – Year 3

Budget. The department requests a one-time increase of $2.7 million ($1.8 million Insurance Fund, $962,000 General Fund) in the budget year for four positions and 2.5 temporary help position authority positions. The positions will help complete the third year of implementation of a five-year project to replace the department's legacy Menu and Integrated Database (IDB). Specifically, the requests includes $1.8 million for external contracts for software, project management, and project oversight and $962,000 to support positions.

Background. The CDI Menu Project is a gateway or portal (user interface) that was developed in 1992 using an Oracle Forms and Reports platform. The core of the CDI Menu is the IDB database, the backend database which includes the majority of the CDI Menu's rules and database triggers. Built over 20 years ago, the technology supporting the current IDB is outdated and the vendor will no longer provide support for this technology after June 2017. The CDI Menu provides access to over 90 different functions, reports, studies, and views. For example, the Fraud Integrated Database (FIDB) System provides on-line access, permitting input and/or retrieval of data such as case activity notes, timekeeping, case contacts, suspects, witnesses, case review, case assignment, investigative plans, and management reports. The system's aging technology has created several functionality issues and challenges

To date, the CMMP has received total resources of $4,106,000. The department is requesting year three resources of $2,749,000 to continue the project, which will include the completion of the reengineering of the Fraud Integrated Database (FIDB) system; completion of upgrading systems for Licensing Services Division and Financial Management Division; and begins work for the Rate Regulation Branch (RRB) and Financial Surveillance Branch (FSB) systems.

Staff Comment. The CMMP is a five-year project and this proposal requests funding for year three only. CDI's estimated future resource requirements will be addressed during the annual budget process as seen in the chart below.

Resources	FY 2017-18	FY 2018-19
Positions	5.5	0
Funding	$1.85 million	$278,000

Staff Recommendation. Approve as requested.

Issue 4: Network Switch Replacement

Budget. The department requests a one-time $1.7 million (Insurance Fund) augmentation to replace 95 IT network switches.

Background. CDI’s existing IT infrastructure has been in place for over ten years, with the existing switches purchased in 2008, and has been partially replaced and incrementally upgraded based on security risks, technology needs, and available funding. A central component of CDI's network are 95 IT network switches that serve as an access point to a private cloud that connects the entire organization to the Internet. In July 2016, the 95 IT network switches will reach the end of their life as earmarked by the manufacturer. As the end-of-life approaches for these network switches, the failure rate increases to approximately 25 percent.

The $1.7 million costs include a three-year maintenance and support plan. The switches have a useful life of about six years; therefore, CDI anticipates requesting additional funding in 2019-20 of approximately $325,000 to purchase three more years of maintenance and support.

Staff Comment. The current network switches will reach end-of-life in July 2016 and absent replacing all 95 switches at the same time, CDI may incur more expensive costs as switches are replaced on an emergency basis. Currently, the department’s technology refresh allocation is $700,000 – an amount reserved to refresh the department’s end-of-life desktop and notebook PCs, not to support an entire infrastructure refresh.

Staff Recommendation. Approve as requested.

Issue 5: Resource Redirection

Budget. The department requests to shift $808,000 in the budget year and ongoing from the General Fund Tax Collection and Compliance Program to address workload demands for the following two programs: (1) Regulation of Insurance Companies and Insurance Producers ($461,000), and (2) administration ($347,000).

Background. In 2014-15, the Financial Surveillance Branch (FSB) restructured its Premium Tax Audit Bureau (PTAB) and found inefficiencies with the existing processes, including duplication of work by PTAB's two-level review audit process, lack of coordination of on-site examinations, and not billing companies to recover program costs. When FSB streamlined its review process, staffing needs in PTAB were reduced from 12 to five positions. CDI identified resource needs in its Rate Regulation Branch (RRB) and Administration & Licensing Services Branch - Human Resources Management Division (HRMD).

Staff Comment. The department does not anticipate the reduction of resources for the FSB will impact the department's tax collection activities, which results in approximately $2.4 billion in taxes collected annually for the General Fund. The request does not adversely impact the department’s Insurance Fund.

Staff Recommendation. Approve as requested.

0890 SECRETARY OF STATE

Issue 1: Help America Vote Act (HAVA) Spending Plan

Budget. The Secretary of State (SOS) requests $54.1 million (Federal Trust Fund), including reauthorization of funds not used in prior fiscal years, in the budget year to continue implementing statewide mandates of the Help America Vote Act of 2002 (HAVA) (P.L. 107-252). The request amends a spending plan, which was created to distribute federal grant funds to implement HAVA.

Background. On October 29, 2002, President Bush signed the Help America Vote Act (HAVA), which provides federal funding to the states to implement mandated elections changes, such as uniform and nondiscriminatory election technology and administration requirements, and requirements to ensure that voters receive information about voting rights, provisional voting, and how to use new voting equipment. To date, the state has received $391.3 million in federal funds to implement these mandates; including interest earned, total funds equal $435.9 million. The requirements of HAVA include statewide modernization or replacement of voting equipment, education and training programs for election officials and poll workers, and a statewide voter registration database (VoteCal to be discussed in the next item).

The HAVA Spending Plan for 2016-17 includes the following activities:

September 10, 2015 HAVA Spending Plan for FY 2016-17

Activity	Amount	HAVA Citation
HAVA Activities		
EAID Grants – State Support ($50K)	$ 50,000	HAVA Required – Section 261
Voting System Testing & Approval – Support	$ 380,000	HAVA Required – Section 301
Section 301 – Voting Systems AVVPAT	$ 51,000,000	HAVA Required – Section 301
Interim Solution – Support	$ 450,000	HAVA Required – Section 303
Administration – Support	$ 1,605,000	HAVA Allowable – Sections 101, 251 & 261
Performance Measures – Support	$ 100,000	HAVA Allowable – Section 254
HAVA Activities Total [1]	**$ 3,085,000**	

[1] Funds for the VoteCal project will be secured through a separate BCP

To date, including all rounds of contracts, counties have submitted, and SOS had paid or projected claims in the amount of $144 million, leaving an anticipated unexpended balance of $51 million. Therefore, SOS requests a shift in expenditure authority in 2015-16 in an amount not to exceed $51 million. Allocations previously provided to counties have not been fully expended for a variety of reasons, including:

- Some counties used a phased approach, deploying compliant equipment on an interim basis with the intent to "upgrade" or replace that equipment at a future date.
- Some counties planned on purchasing additional equipment or replacement equipment as systems become more reliable.

- Some counties held funds in "reserve" because of policy changes and potential policy changes at the state and/or federal level that may have affected the continued viability of voting systems as they were configured at the time.

Staff Comment. After implementation of VoteCal in the budget year (see next item), the unexpended HAVA Fund balance, allocated to counties but unspent, is estimated to be $38,893,337. The unexpended balance may be used to support ongoing costs of complying with the federal mandates including maintenance and operation of the VoteCal system and voter registration list maintenance. It cannot be expended without budgetary authorization, and can be used solely for HAVA-related needs.

Staff Recommendation. Approve as requested.

Issue 2: HAVA VoteCal

Budget. The SOS requests $5.3 million (Federal Trust Fund) in spending authority for the budget year to cover the first year of maintenance and operations (M&O) costs of VoteCal, California's new statewide voter registration database. The M&O project costs are as noted in the Special Project Report (SPR) No. 5, which was approved on January 10, 2013, to cover the first year M&O after the implementation of VoteCal.

Background. Section 303 of the Help America Vote Act (HAVA) of 2002 (Public Law 107-22, 107th Congress) mandates that each state implement a uniform, centralized, interactive, computerized voter registration database that is defined, maintained, and administered at the state level. This federal law requires the SOS to deploy a statewide voter registration database (VoteCal System) that is the official statewide voter registration list for all federal elections. This database must contain the name and registration information of every legally-registered active or inactive voter in the state. Each of the 58 counties has a voter registration system, including procedures and practices, that has evolved over decades of use independently of other counties, and generally independent of the state.

The VoteCal Project continues to be executed within the schedule and cost allocation outlined in SPR No. 5 and is anticipated to be the federally-mandated, HAVA compliant, single statewide and centralized voter registration system of record by June 30, 2016. The first year of M&O will begin July 1, 2016, and continue through June 30, 2017. The project is successfully executing completion of the testing activities, pilot rollout activities, training activities, organizational change management, and solution implementation. The request does not include an anticipated $5.3 million ongoing cost.

VoteCal M&O project costs

Categories	
Continuing IT Project Costs	
Staff (Salaries & Benefits)	$1,252,799.00
Hardware Lease/Maintenance	$549,933.00
Software Maintenance/Licenses	$1,246,739.00
Telecommunications	$690,804.00
Contract Services	$307,047.00
Data Center Services	
Agency Facilities	
OE&E	$137,550.00
ICRP & SWCAP	$776,735.00
Other - Training	
Other External Agency Interface Maintenance	$376,457.00
Total Continuing IT Costs	**$5,338,064.00**

Below is a table for VoteCal project milestones:

ACTIVITY/TASKS	FY	ESTIMATED COMPLETION	COMMENTS
Revise spending plan and FSR	05-06	Apr/May 06	Complete
FSR to Leg. and Leg. approval		May/Jun 06	Complete
Hire system contract manager	06-07	July 2006	Complete
Redirected IT staff to maintain existing CalVoter system and interim solutions with counties, DMV, SSA, CCR, DPH		Ongoing	
Bid/Award oversight consultant, project manager, IV&V consultants		Aug 2006	Complete
Bid/Award for consultant to assist SOS with VoteCal bid proposal		Oct 2006	Complete
Begin procurement/develop/issue RFP and bid for integration contractor	07-08	Oct 2007	Complete
Evaluate bids for integration contractor	08-09	May 2009	Complete
Submit SPR for review		June 2009	Complete
Issue contracts for system integrator and other contract services	09-10	Aug/Sept 2009	Complete
Contract with original system integrator terminated May 2010, submit new SPR, develop and issue new RFP	10-11	Aug 2010	Complete
Complete evaluation and selection process for the new system integration contractor	12-13	Oct 12, 2012	Complete
Submit SPR for control agencies review and approval	12-13	Oct 19, 2012	Complete
SPR approved by control agencies	12-13	Jan 10, 2013	Complete
System Integrator contract awarded	12-13	Mar 06, 2013	Complete
EMS Remediation contracts awarded	12-13	April 19, 2013	Complete
Project Kick-Off	12-13	April 19, 2013	Complete
Project Planning	13-14	October 2013	Complete
Design Activities	14-15	Sept 2014	Complete
Development Activities	14-15	June 2015	Complete
Testing Activities	15-16	August 2015	In Progress
VoteCal Pilot	15-16	October 2015	In Progress
VoteCal Deployment	15-16	June 2016	In Progress
VoteCal Maintenance and Operations	16-17	June 2017	In Progress

Staff Comment. The projected launch date for VoteCal is June 30, 2016. As of March 11, 2016, the SOS notes that 58 counties have VoteCal.

Staff Recommendation. Approve as requested.

Issue 3: Secretary of State Headquarters Building Security Improvements

Budget. The SOS requests $226,000 ($172,000 Business Fees Fund and $54,000 General Fund) in the budget year, and $216,000 ($164,000 Business Fees Fund and $52,000 General Fund) ongoing, to fund the following two positions that will coordinate and administer security improvements at the Secretary of State and State Archives Building Complex, based on assessments performed by the Department of General Services (DGS) and the California Highway Patrol (CHP):

- One associate governmental program analyst (AGPA) to assist the Business Operations manager and the Health and Safety Officer with system maintenance and reevaluations, and to develop and maintain emergency protocols and threat mitigation plan.

- One associate information systems analysts (AISA), with CCure 9000 User and Technical certification, to administer, manage, program, configure, operate, and troubleshoot the closed circuit television computer system.

Background. In January 2015, a SOS employee brought a loaded gun, several rounds of ammunition, and two knives (with blades over four inches) to work in a backpack. According to the department, had the employee decided to use the weaponry against co-workers or the public, the employee would have wide access to move throughout the building undetected, undeterred by security cameras or badge card readers. In April 2015, the DGS conducted a Security Assessment Report, which proposes a four-phase project, with a total estimated cost of $2,431,000.

For Phase 1:
- Space planning evaluation $ 13,000
- Card key access $255,623
- Main entry improvements (will add four turnstiles at the main lobby entrance and, voice, and data lines added to the main lobby guard station) $ 96,877

For Phase 2:
- Video camera upgrades $924,100
- Distress call improvements (guard station monitors will be switched to the camera location of the security event) $260,500

For Phase 3: New security doors $127,700
For Phase 4: Physical barriers at public counters $754,000

Staff Comment. In 2014-15, the SOS deposited $2.6 million in its Architectural Revolving Fund (ARF) account. The ARF funding will cover the estimated cost of the four projects above and leave a balance of $168,200. The SOS anticipates making a future funding request for this work once the scope of work and cost estimates are completed.

Staff Recommendation. Approve as requested.

Issue 4: Placement Agent Lobby Registration Workload (AB 1473)

Budget. The SOS requests $79,000 (General Fund), and $74,000 (General Fund) ongoing, for one program technician III to assist with increased lobbying registration workload related to Assembly Bill 1743 (Hernandez), Chapter 668, Statutes of 2010.

Background. Placement agents facilitate investment "partnerships" between public retirement systems and private investors, but are not employees of the private investment firm, investment portfolio managers, or parties to the investment deal. Prompted by public reports about activities of a former California Public Employee Retirement System (CalPERS) board member, who became a placement agent and, reportedly, earned $59 million in placement agent fees, concerns were raised about the role of placement agents in the investment practices of public retirement systems. The investigation led to federal charges that resulted in a guilty plea by the CalPERS CEO to bribery and fraud charges and indictment of the former CalPERS member. In response, AB 1743 was enacted. Among other provisions, AB 1473 requires placement agents to register as lobbyists.

During the three legislative sessions prior to enactment of AB 1743, an average of 1,254 lobbyists and 275 employers registered with the SOS. However, following enactment of AB 1743, an average of 2,237 lobbyists and 659 employers were registered. The SOS attributes this change directly to the enactment of AB 1743. For the 2015-16 legislative session, 1,042 placement agents have registered as lobbyists. Because placement agents have different characteristics and business practices than traditional lobbyists, placement agents’ registration processes are more labor-intensive.

Since 2010, the SOS has experienced a “near doubling of lobbying and tripling of employer registrations, [causing] a persistent backlog in the registration function.” To manage the backlog, SOS has re-directed six different staff members, representing 2,184 hours, adversely impacting other mandated duties, including maintaining the lobbying change log, reviewing campaign and lobbying statements, processing fines for late filing of reports, and monitoring lobbyist participation in mandated ethics courses.

SOS staff project lobbyist and employer registrations to level off in the future, based on the average number of placement agent registrations experienced over three legislative sessions.

Staff Comment. When AB 1473 was first implemented, the department had no statistical information to anticipate future workload. This budget request does not expand or add any new functionality to the program. The Elections Program is authorized for 28 positions, 26.5 of which are filled.

Staff Recommendation. Approve as requested.

Issue 5: Ballot on Demand Systems: Electronic Poll Books (SB 439)

Budget. The SOS requests $93,000 (General Fund) for the budget year and ongoing for one assistant information systems analysis to test and certify of electronic poll books, as required by Senate Bill 439 (Allen), Chapter 734, Statutes of 2015.

Background. An electronic poll book (ePB) is an electronic version of the traditional paper poll book, which contains a list of the registered voters in each precinct or district. An electronic poll book may be on a tablet or laptop computer. Currently, the SOS does not review or approve electronic poll books in California.

SB 439 authorizes county elections officials to use new technology to check-in voters at polling places and other voting sites, and sets up processes and procedures for the review and approval of ePBs for use in California elections. In addition, SB 439 requires the SOS to adopt and publish ePB standards and regulations, and prohibits the use of an uncertified electronic poll book.

Staff Comment. Current SOS staff is unable to absorb additional workload. In the first two months of 2016, the SOS' Office of Voting Systems Technology Assessment, which has two staff, has worked over 100 hours of overtime combined. Further, the requested position cannot be funded with HAVA funds. The federal Election Assistance Commission (EAC), the entity that oversees the administration of HAVA funds, stated in a funding advisory opinion to California, that the certification of ePBs are ineligible for funding to meet Title III compliance.

Staff Recommendation. Approve as requested.

Issue 6: Vote by Mail Ballot Drop-off Location Regulations (SB 365)

Budget. The department requests a one-time $55,000 (General Fund) augmentation for temporary help to assist in promulgating regulations for security measures and procedures related to the security of vote-by-mail ballot drop boxes, such as chain of custody, pick-up times, and proper labeling, that a county elections official may use, if the county elections official establishes one or more vote-by-mail ballot drop-off locations.

Background. As required under Senate Bill 365 (Pavley), Chapter 733, Statutes of 2015, the Secretary of State must promulgate regulations related to vote-by-mail drop boxes by January 1, 2017. The Secretary of State will need to work with county elections officials to identify best practices for security measures. The regulatory process (drafting the regulations and reviewing with agency staff and stakeholders; public notice and publishing of the draft regulations; conducting public hearings; considering comments and drafting potential amendments to the regulations; and final adoption of the regulations) takes approximately six to twelve months. Although SOS has received anecdotal evidence of counties turning to vote-by-mail drop boxes "as a means of providing additional ballot drop-off opportunities," it does not have any specific information as to which counties or how many counties currently offer this option.

Staff Comment. SOS attorneys estimate approximately 650 hours are required to complete regulations. The estimated $55,000 is based on using an hourly rate of $85.27 for 650 work hours ($55,425.50). Although existing staff will be available to assist and review throughout the process, the department provides that staff time must "remain focused on the conduct of the 2016 presidential election."

Staff Recommendation. Approve as requested.

1701 DEPARTMENT OF BUSINESS OVERSIGHT

Overview. The department regulates a variety of financial services, products and professionals, and oversees the operations of state-licensed financial institutions, including: banks, credit unions, money transmitters, issuers of payment instruments and traveler’s checks, and premium finance companies. In addition, the department regulates the offer and sale of securities, franchises and off-exchange commodities.

In 2012, Governor Brown released Government Reorganization Plan No. 2 (GRP 2), which sought to streamline and reorganize state government for efficiency, to the Little Hoover Commission. Effective July 1, 2013, the Department of Corporations (DOC) and the Department of Financial Institutions (DFI) merged to form the Department of Business Oversight, which reports to the Business, Consumer Services and Housing Agency. The former DOC and DFI operate as divisions within the department. All applications, examinations and reports continue to be processed by the attorneys and staff who work for the former departments.

The former DCO (now a division) licenses and regulates securities brokers and dealers, investment advisers and financial planners, consumer and commercial lenders including mortgage lenders, deferred deposit or payday lenders, escrow companies, and certain other fiduciaries. The DOC also regulates the offer and sales of securities, franchises and off-exchange commodities. The former DFI (now a division) oversees the operations of state-licensed financial institutions, including banks, credit unions, and money transmitters.

Budget. The budget includes $92.8 million ($51.9 million State Corporations Fund, $29.1 million Financial Institutions Fund, $10.1 million Credit Union Fund, and other funds) and 571.5 positions to support the department and its services.

Issue 1: Department of Corporations Quality Network System Support

Budget. The budget requests $1.1 million (State Corporations Fund) for the budget year and 2017-18 for seven permanent positions (two staff information systems analyst, one senior information systems analyst, one system software specialist II, one associate programmer analyst, and senior programmer analyst, and one system software specialist I) to provide the time for the knowledge transfer from the contractor to internal staff.

Background. In 2009, the Department of Corporations was approved to develop and implement the Department of Corporations Quality Network (DOCQNET) system. According to the department, due to an administration change, the project was initiated in 2012 with a Special Project Report (SPR 2180-14) and approved Budget Change Proposal (BCP 2180-2); the DOCQNET system was implemented in June 2014. With DOCQNET, the department conducts its regulatory functions, such as revenue collection, enforcement actions, and licensee examinations and licensing. Approximately 99 percent, or 51,165 of the 51,771 licensees, are tracked and managed within DOCQNET.

In July 2013, when DFI and DOC merged to form the Department of Business Oversight (DBO), the information technology workload increased, attempting to consolidate two networks and infrastructures into one. To handle the workload, seven limited-term positions were approved but expired at the end of the 2014-15 fiscal year. Due to the loss of the seven positions, DOCQNET's development contractor continues to absorb nearly 95 percent of all DOCQNET help support, along with efficiency and improvement request activities.

The DOCQNET project originally encompassed only the DOC, not DFI systems. In addition, DOCQNET was not originally designed with the Department of Technology’s updated privacy and security standards, which include guidelines for data encryption and privacy notifications. The Division of Financial Institutions' (DFI) legacy systems encompasses over three dozen databases, spreadsheets, and outdated web systems, including systems for processing applications and licenses, and managing financial institution examinations.

Total cost of the DOCQNET system, to date

2012-13 Actual	***2013-14 Actual***	***2014-15 Actual***	***2015-16 Estimated***	***Total***
223,821	2,094,259	2,355,931	1,636,000	6,310,011

* The DOCQNET project was initiated in 2012-13. Work was not performed until 2013-14.

Justification. The development contractor's service contract expires at the end of fiscal year 2017-18. According to the department, the requested positions will receive training in Microsoft's Dynamic Customer Relations Management (CRM) and SharePoint software solutions. In addition, the permanent positions will allow the DBO to integrate DFI legacy systems into DOCQNET and bring the security of the system up to the latest Department of Technology standards.

Staff Comment. Although the IT workload appears to be ongoing, the request is for two-year funding. The department clarifies that the intent of the proposal is to fund the knowledge transfer from the contractor, Trinity Technology Group, to the state staff. The department currently has the flexibility to fund the permanent staff on an ongoing basis. The department is special-funded through licensing fees and assessments, and the DOCQNET system is both utilized and funded by the State Corporations Fund. There is no impact to the General Fund. No additional fees to the stakeholders are required or are requested with this proposal.

Staff Recommendation. Approve as requested.

Issue 2: Internal Auditing Unit

Budget. The department requests $334,000 ($196,000 in State Corporations Fund, $106,000 in Financial Institutions Fund, $30,000 in Credit Union Fund, and $2,000 in Local Agency Deposit Security Fund), and $321,000 ($188,000 in State Corporations Fund, $102,000 in Financial Institutions Fund, $29,000 in Credit Union Fund, and $2,000 in Local Agency Deposit Security Fund) ongoing, for one senior management auditor and one associate management auditor, to establish an internal auditing unit. This unit will provide ongoing, independent, evaluation, and assessments of internal controls.

Background. Senate Bill 1452 (Speier), Chapter 452, Statutes of 2006, requires state and local agencies that spend an aggregate of $50 million or more annually to consider establishing an ongoing audit function. Prior to GRP 2, the Department of Corporations and Department of Financial Institutions' annual appropriation was less than $50 million. However, following GRP 2, the department now exceeds the $50 million threshold. Since 2013, the department has attempted to meet this audit requirement by moving vertically through the management process, if any issues arise.

The proposed unit will assess: (1) the consolidation efforts following GRP 2; (2) the implementation of its strategic plan (currently under development by a departmental task force); and (3) internal controls of each division.

Staff Comment. The request to establish an internal audit unit complies with existing law and best practices. As a nascent department, the request for two additional staff appears adequate to cover the department's needs at this time. The internal audit will follow the International Standards for the Professional Practice of Internal Auditing and Generally Accepted Government Auditing Standards.

Staff Recommendation. Approve as requested.

PROPOSED FOR DISCUSSION/VOTE

0845 DEPARTMENT OF INSURANCE

Overview. The California Department of Insurance (CDI) was created in 1868 as part of a national system of state-based insurance regulation. The state's publicly-elected Insurance Commissioner regulates the sixth largest insurance economy in the world, collecting more than $259 billion in premium annually. CDE licenses approximately 1,300 insurance companies and more than 385,000 insurance agents, brokers, adjusters, and bail agents.

Annually, the department receives and investigates around 250,000 complaints, performs examinations to ensure the financial solvency of companies, and receives approximately 33,000 suspected fraudulent claim referrals annually.

Budget. The budget includes $269.4 million ($262.4 million Insurance Fund, $5.6 million General Fund, $1.1 million Federal Trust Fund, and $250,000 in reimbursements) and 1,266.8 positions to support the department and its programs.

In addition, the department requests three budget proposals related to legislative implementation and two pertaining to automation functions.

Issue 1: Outpatient Prescription Drugs (AB 339)

Budget. The department requests $242,000 (Insurance Fund) in the budget year, and $235,000 (Insurance Fund) ongoing, to implement Assembly Bill 339 (Gordon), Chapter 619, Statutes of 2015. Specifically, the request includes funding for:

- One attorney position to provide legal guidance in market conduct examinations and to annually review compliance.

- A contract with a pharmacist ($100,000 in budget year and ongoing) to confirm review formularies and advise the Health Policy Approval Bureau (HPAB) attorneys regarding insurer formularies, how to formulate appropriate legal objections, and assist with negotiations for insure compliance.

Background. Assembly Bill 339 requires health plans and health insurers that provide coverage for outpatient prescription drugs to have formularies that do not discourage the enrollment of individuals with certain health conditions. Among many provisions, the bill requires, commencing January 1, 2017, a plan or insurer to maintain a pharmacy and therapeutics (P&T) committee to develop, maintain, and oversee any drug formulary list, and establish requirements associated with the P&T committee that are substantially similar to federal regulations. In addition, the Commissioner, as part of the market conduct examination, must review the performance of an insurer that provides prescription drug benefits.

The HPAB must confirm that formularies are accessible and searchable on an insurer's website. These formularies will also need to be reviewed for compliance and non-discriminatory practices. According to the department, current legal staff does not have the medical expertise to review the formularies or understand the various medical conditions treated by prescription drugs. Further, the HPAB needs to promulgate regulations to define, interpret, and develop specific requirements for formulary design, formulary submission requirements.

Staff Comment. According to the Senate Appropriations Committee analysis, AB 339 was estimated to incur one-time costs of about $750,000 (Insurance Fund), and ongoing costs of about $400,000 per year, for the department to adopt policies and regulations, review plan filings, and enforce the requirements of this bill.

Staff Recommendation. Approve as requested.

0890 SECRETARY OF STATE

Overview. The Secretary of State (SOS) is the chief elections officer and administers and enforces election laws. The SOS also administers and enforces laws related to corporations, limited liability companies, partnerships, limited partnerships, unincorporated associations, and bonds and perfecting security agreements. The Secretary is the filing officer for lobbying and campaign documents under the Political Reform Act, and operates the Safe At Home program.

Budget. The budget includes $140.6 million ($59.4 million Federal Trust Fund, $50.5 million Secretary of State Business Fees Fund, $29 million General Fund, and $1.7 million other special funds) and 495.9 positions.

Issue 1: Business Programs Division Filings Processing

Budget. The SOS requests $5.5 million (Business Fees Fund) for the budget year and 2017-18, for 52 temporary help positions (appointments of retired annuitants, permanent intermittent, seasonal) to assist in processing business filings and statements of information until California Business Connect (CalBusiness Connect) is implemented in 2020.

Overview of CalBusiness Connect. The CalBusiness Connect project is envisioned to automate paper-based processes, allowing business to file and request copies of records online and to process fee payments within one business day. Currently, the Uniform Commercial Code and Statement of Information filings are on paper, manually sorted, tracked on different automation systems, including a system on three inch by five inch index cards. The SOS received its feasibility study report (FSR) approval for the project on April 1, 2011; and a contract was awarded on January 10, 2014. On April 10, 2015, the SOS and its system integrator, Bodhtree Solutions Inc., mutually terminated the contract for $8.9 million.

On December 28, 2015, the SOS submitted a Special Project Report (SPR) to the California Technology Department (CalTech) which proposed: (1) changing the project scope to focus on the largest annual volume filings and reducing the complexity of the project; (2) changing the schedule to a phased implementation approach; and (3) changing the project's budget. At the time of this publication, the SPR is still under review. The department shared the following projected milestones:

Item	Estimated timeframe
Planning	Present until January 1, 2017
Procurement for vendor	Until August 2018
Award contract	September 2018
Phase 1 (LLCs, limited partnerships)	August 2019
Phase 2 (Corporations)	February/March 2020
Phase 3 (Uniform Corporations Code)	August/September 2020
Phase 4 (Trademarks)	January/February 2021
Maintenance and Operations (one-year)	2022

The department acknowledges certain lessons learned from the previous contract, including improving initial requirements, improving vendor procurement processes, and to have a focus on the code rather than plans.

Background on SOS filings. The Budget Act of 2013 provided $7.8 million in combined funding and 56 limited-term positions to reduce processing times to an average of five business days. The five business day average was achieved in October 2013. In 2014-15 and the current year, the spending authority was reduced to an annual allocation of $6.2 million and 54 limited-term positions to maintain the average five business day turnaround times for both business formations and statements of information. Below is a table that demonstrates the historical backlogs for both business formations and statements of information.

Backlog History

Fiscal Year	Year-End **Formations** in Process	**Formations** Processing Times during FY (low and high)	Year-End **Statements of Information** in Process	**Statements of Information** Processing Times during FY (low and high)
FY 2010-11	11,681	21-45 days	120,288	48-84 days
FY 2011-12	5,631	19-53 days	100,279	71-95 days
FY 2012-13	7,788	9-45 days	67,221	30-74 days
FY 2013-14	2,848	4-13 days	10,164	3-38 days
FY 2014-15	3,982	4-5 days	10,878	3-5 days

	1/31/2016 **Formations** in Process	**Formations** Processing Times during 1/2016 (low and high)	1/31/2016 **Statements of Information** in Process	**Statements of Information** Processing Times during 1/2016 (low and high)
End of 1/2016*	4,329	5-7 days	12,905	5-8 days

*These numbers reflect the documents in process at the end of January 2016. January is a peak processing month; therefore, January work in process is higher than is typical at fiscal year-end in June.

Workload History

Workload Measure	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16*
Documents Processed**	1,738,908	1,933,954	2,089,718	2,150,622	2,214,796	2,200,000
Name Reservations	41,860	43,075	44,623	35,784	34,910	34,000
Telephone Calls	352,415	376,563	318,473	303,607	330,649	330,000
Copies Issued	391,427	332,972	405,447	552,137	628,966	628,000
Certificates Issued	446,629	451,246	473,403	476,199	496,495	496,000
Annual Volume	2,971,239	3,137,810	3,331,264	3,518,349	3,705,816	3,688,000

*Projected; ** Includes corporation, limited liability company, limited partnership, statement of information, regional office, UCC, trademark and special filing documents.

Currently, the SOS is authorized for 326.8 positions in this division and has 19 vacancies.

Staff Comment. There are no statutorily required timelines for processing business filings or statements of information. However, Assembly Bill 113 (Committee on Budget), Chapter 3, Statutes of 2013, increased the Secretary of State appropriation by $1.6 million to reduce processing time for business formations and statements of information. According to the SOS, the SOS and the Legislature agreed the reduction sought would be to reach an average five business day turnaround for both business formation filings and statements of information.

At the time of this publication, the SPR is not available for public review, as it is still under review with CalTech. Staff notes that these 52 temporary help position requests are intended to maintain the current processing turnaround for business filings and statements of information – processes that were intended to be automated by the suspended CalBusiness Connect project. A general estimate is that the project's first phase (limited liability corporations and limited partnerships) will not be launched until 2019. The subcommittee may wish to ask how the department intends to use temporary help for an ongoing need while CalBusiness Connect is being phased-in.

Staff Recommendation. Hold open.