

SUBCOMMITTEE NO. 5

Agenda

Senator Nancy Skinner, Chair
Senator Joel Anderson
Senator Jim Beall



Thursday, March 30, 2017
9:30 a.m. or upon adjournment of Session
State Capitol - Room 113
Consultant: Anita Lee

Vote Only Items

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Pursuant to the Americans with Disabilities Act, individuals who, because of a disability, need special assistance to attend or participate in a Senate Committee hearing, or in connection with other Senate services, may request assistance at the Senate Rules Committee, 1020 N Street, Suite 255 or by calling (916) 651-1505. Requests should be made one week in advance whenever possible.

ITEMS TO BE HEARD VOTE ONLY

0559 SECRETARY FOR LABOR AND WORKFORCE DEVELOPMENT AGENCY

Issue 1: Associate Secretary for Farmworker and Immigrant Services

Governor's Budget Proposal. The Governor proposes to make the 2015-16 limited-term agency secretary position permanent, by providing the agency an increase of \$205,000 (reimbursement authority) and one position to identify and prevent abuses in the recruitment of H-2A temporary workers and to coordinate the programs within the Agency that are responsible for serving farmworkers and immigrants.

Background. The U.S. Department of Labor's H-2A temporary agricultural worker program allows agricultural employers who anticipate a shortage of domestic workers to bring nonimmigrant foreign workers, typically from Mexico, to the U.S. to perform agricultural labor of a temporary or seasonal nature that lasts no longer than one year. Employers must pay all travel costs and provide these workers with a copy of their contract, free housing, and three low-cost meals per day. To secure H-2A workers, employers typically rely on recruitment agencies to find and contract the workers on their behalf. Under the federal program, it is unlawful for recruiters or recruitment agencies to charge recruitment fees to H-2A workers. California's usage of the program has more than doubled since 2011-2012. In 2011-12 there were 58 job orders, accounting for 3,337 requested workers, of which 3,174 were certified; in the current program year 2015-16 there have been 261 job orders, accounting for 9,606 requested workers, of which 8,179 have been certified. In July 2014, Governor Brown signed a letter of intent to cooperate with Mexico's Secretary of Labor and Social Welfare to protect the rights of Mexican H-2A temporary workers in California.

The 2015-16 budget provided the agency a two-year limited-term funding to hire the agency secretary for Farmworker and Immigrant Services to design and implement a voluntary pilot program in the Salinas and Santa Maria areas to improve transparency and accountability in the recruitment chain of these workers, to reduce exploitation, and prevent labor violations among this vulnerable workforce. Upon being hired, the agency secretary engaged stakeholders from the advocate community, agricultural industry, bi-national worker advocates, the Mexican government and internal state entities to develop a survey instrument that best captures the demographic and compliance information necessary to identify bad actors and make policy recommendations.

The agency secretary is also responsible for implementing and overseeing the directives of the Director of Immigrant Integration within the agency and coordinating agency programs and resources that can be used to assist California's immigrant population in obtaining employment, labor rights protections, and accessing employment training resources. There are multiple programs within the agency serve farmworkers, including: 1) The Agricultural Services Unit, and the Monitor Advocate Office at the Employment Development; 2) The Division of Labor Standards Enforcement, and the Division of Occupational Safety and Health at the Department

of Industrial Relations, 3) the Workforce Development Board, and 4) the Employment Training Panel.

In February 2017, the agency secretary is launching the first intra-agency farmworker cross-training effort. This training will include a discussion on outreach best practices, engaging with indigenous farm workers, and best practices in collaboration and areas where these departments can collaborate more effectively. This initial training will also set the stage for regularly scheduled quarterly farmworker coordination meetings that will follow. The quarterly meetings will provide an opportunity for ongoing training for staff and coordination amongst departments interfacing with farm workers, paying particular attention for opportunities for multiple remedies across departments when it comes to farm worker protections.

The agency secretary will work with the state's workforce partners to identify gaps in services and programs, develop solutions and identify, promote, and implement best practices to expand access to workforce programs for the immigrant population. This position will also actively engage with immigrant rights stakeholders, and workforce partners to ensure collaboration in development and implementation of programs. The agency secretary will also be responsible for crafting and implementing a workforce navigator program which will be piloted in 2017-18. This pilot will help fund two to three locations where local boards can increase their staff capacity to hire "navigators" that can help increase the participation of immigrant and LEP participants in workforce programs. This pilot project will be implemented in targeted locations of the state that have a high density of LEP and Immigrant workers and will include a comprehensive program evaluation component to enable the agency secretary to evaluate and identify which practices are most effective at serving the target population. The goal for the pilot project is to ensure that navigators are the liaison for the LEP and immigrants enrolled in their programs, and that the navigator is properly trained to recruit, engage and support immigrant and English language learner participants through the workforce system and increase enrollment and completion by this population. One key component of the navigator program will be the ability to connect program participants with wrap around services, including transportation, housing, and other supportive services to ensure the participant has the tools needed to succeed and complete the training program.

Staff Recommendation. Approve as budgeted.

7501 DEPARTMENT OF HUMAN RESOURCES**Issue 2: Employee Outreach**

Summary. The Administration requests \$135,000 in reimbursement authority for 2017-18 and ongoing, to continue implementing a Statewide Employee Engagement Survey program that began in 2015.

Background. In 2015, the state hired a consultant to implement the first statewide employee engagement survey. The Governmental Operations Agency paid \$48,000 for the survey, and included 5,000 randomly selected employees. This survey provided a broad perspective on the level of engagement in California's workforce. The state must build on this first engagement effort by greatly expanding on the survey's ability to deliver more agency and department specific results on a reoccurring basis. The state does not currently provide department with their own workforce employee engagement data, or the tools and guidance needed to improve engagement, departments either expend resources to create their own surveys or don't seek to improve performance through engagement. Without comprehensive engagement data, CalHR notes that departments cannot benchmark their results with other organizations.

The reimbursement authority will allow CalHR to create and implement an ongoing program to survey the state's workforce on key engagement indicators. Additionally, CalHR will provide recommendations for standardized tools, resources and guidance to support individual departments efforts to improve employee performance through engagement. The primary short-term outcome of the requested resources is to develop a consistent state-wide survey for measuring employee engagement, along with a repeatable process for administering the survey in all state organizations. The long-term expected outcome includes improvement of employees and organizational performance as a result of organizations having and acting on employee engagement.

CalHR anticipates that by April 2017, they will develop and release a request for proposal for a statewide engagement survey, and have a vendor in place by July 2017, to support CalHR's engagement services.

Staff Recommendation. Approve as budgeted.

Issue 3: Statewide Training Center

Summary. The Governor's budget includes \$2.82 million in reimbursement authority and three positions in 2017-18, and \$2.79 million in reimbursement authority in 2018-19, and ongoing, to continue expanding the Statewide Training Center (STC) to accommodate increasing enrollment.

Background

In 2006, the original STC closed due to budget cuts. In 2012, the STC reopened, however training functions became decentralized as departments built their own training programs and established vendor contracts for outsourcing employee development services. The decentralized model resulted in system-wide inefficiencies, redundancy and inconsistencies in how the state develops the competencies of California's civil service workforce.

The STC's mission is to provide the state civil service workforce with low cost, relevant and appropriate soft skills, leadership and human resource technical training. The Administration notes that most departments do not have resource to conduct their own training programs. While these departments do not have staff to provide training, they do have funding available to send their staff to training. The STC offers training on a reimbursable basis. The new business model proposed by CSI will provide CalHR with greater leadership over statewide training curriculum in order to supply training. Under the Governor's proposal, the STC will develop centralized training models and content to address statewide needs as determined by CalHR statewide workforce planning data and training needs assessments. The STC will offer state-taught classes that will complement, or in some cases replace, existing vendor training. The STC will continue to partner with vendors to deliver requested training beyond CalHR's capacity, but the content will be owned by CalHR leadership and oversight.

The chart below displays participants at STC.

	2012-2013 Actual	2013-2014 Actual	2014-2015 Actual	2015-2016 Actual	2016-2017 Actual (July - January)
Participants	3,099	6,790	7,780	10,465	10,965

CalHR has developed the following multi-year phased approach to successfully perform its statewide mission:

- **Phase I - 2012-2017.** Offer state employees a wide variety of vendor supported STC training classes.
- The STC has been successful during Phase I. A 2016 CSI training initiative has helped expand STC training to four new regions across the state, creating greater demand for vendor supported STC classes.
- **Phase II – 2016-17.** Create statewide leadership, staff training and development

programs in order to analyze civil service training needs, oversee training curriculum design and evaluation, and facilitate sharing and collaboration on employee development solutions.

- **Phase III – 2017-18.** Offer a variety of leadership and staff development training classes through the STC taught by state employees.

CalHR is requesting three Training Officer II position to provide leadership and staff training through STC. Currently, the STC has no dedicated trainers to deliver revenue-producing state-taught classes. CalHR estimates that these three positions will provide about 2,400 hours in 2017-18 in training classes. The Administration notes that of the \$2.8 million in reimbursement authority, about 85 percent is for training.

Staff Recommendation. Approve as Budgeted.

Issue 4: Blanket Position Conversion for CalCareer Services

Summary. The Administration is proposing to convert three positions from limited-term to permanent to address recruitment and retention issues within CalCareer Services unit. The Administration is requesting position authority only, and the costs will be absorbed by the department.

Background. The CalCareer Services unit is responsible for providing the public with assistance with walk-in career search inquiries in the Job Center and providing proctoring services and administrative support to the in Testing Center. CalCareer Services is the first line of support to help applicants navigate the California State Jobs website. Specifically, CalCareer Services is responsible for answering and responding to state-wide incoming calls and emails regarding general questions on the civil service examination process, CalCareer account profiles, Limited Examination Appointment Process (LEAP), and Veterans' Preference program.

The CalCareer Services unit has had recruitment and retention challenges. Many applicants accept permanent intermittent or limited-term employment within CalCareer Services as a means to gain initial state employment and experience, but continue to seek full-time employment. Since January 2014, 11 staff has left CalCareer Services for full-time employment. Turnover is costly due to the onboarding process, and the resources it takes to train and develop staff that ultimately leave for full-time employment elsewhere. Currently, CalCareer Services has three permanent full-time positions, and three limited-term positions to provide statewide assistance to departments and the public. This combination of staffing has been insufficient to provide the high level of customer services expected from CalHR. CalHR notes that the average wait time for calls in 2016 was 26 minutes, and the goal is to reduce the wait times and complete calls in 10 minutes or less. Additionally, CalHR notes that in 2016, an average of 93 calls a month are dropped or abandoned.

Staff Recommendation. Approve as Budgeted.

Issue 5: Dependent Re-Verification Process.

Summary. The Governor's budget includes one position and \$175,000 in reimbursement authority for 2017-18, \$118,000 and in 2018-19, and ongoing, to perform the new workload to develop, implement and administer the dependent re-verification process.

Background. In January 2011, CalPERS Board of Administration endorsed the Health Benefits Purchasing Review (HBPR) project to develop strategies and initiatives to ensure the continuation and sustainability of the CalPERS Health Benefits Program. The HBPR resulted in the development of 21 initiatives, including dependent eligibility verification designed to influence health care delivery, improve health outcomes, and delivery sustainable programs. The purpose of the dependent eligibility verification project was to ensure all dependents enrolled in a CalPERS health plan met CalPERS' eligibility criteria and to prevent members and employers from having to pay health care costs for those who do not qualify. During verification, each subscriber with at least one dependent enrolled on their health plan was required to provide specific supporting documentation based on dependent type (e.g., spouse, domestic partner, child, parent-child relationship). The 2013-15 CalPERS Dependent Eligibility Verification project disenrolled 8,379 ineligible state employee dependents from the CalPERS health plans for a savings of over \$60 million.

Senate Bill 98, (Committee on Budget and Fiscal Review), Chapter 28, Statutes of 2015 designates CalHR to establish standards for the employing office of the state employee to conduct health dependent eligibility at least once every three years for spouses, domestic partners, children, stepchildren, and domestic partner children; and at least once annually for other children enrolled as dependents under parent-child relationship. Eligibility is the same for dental benefits as it is for health benefits.

CalHR is requesting funding to perform project management and other duties to administer dependent re-verification process and workload associated with oversight to ensure that departments are removing ineligible dependents from health and dental benefits. CalHR will hire a full-time staff personnel program analyst (SPPA), a classification that is responsible for the most complex and difficult personnel management assignments at the statewide human resources leadership level. The SPPA will conduct biweekly project meetings with CalPERS and departmental HR representatives, creating policy memos, training and procedural manuals, user guidance, and assisting state departments with re-verification process issues. On a continuing basis the SPPA will analyze enrollment data, monitor departmental compliance with health and dental dependent enrollments, train department HR staff on eligibility rules and enrollment, verification and termination procedures.

CalHR notes that on August 2017, the SPPA will begin monitoring departments to ensure that they are removing ineligible dependents from dental benefits, and develop a procedural manual to for the re-verification process, and conduct multi-departmental trainings. From 2018 onward, the SPPA will begin the re-verification process, among other duties described above.

Staff Recommendation: Approve as budgeted.

7300 AGRICULTURAL LABOR RELATIONS BOARD**Issue 6: Funding for Agricultural Labor Relations Board**

Governor's Budget proposal. The Agricultural Labor Relations Board (ALRB) requests the the current limited term funding of \$573,000 General Fund for limited-term positions: 1.5 hearing officer II positions and one Attorney IV position be made permanent. The workload for these positions has not decreased and is projected to increase as new satellite offices are fully opened and education and outreach efforts are increased.

Background. In 2015-16, ALRB received a temporary budget augmentation for three positions: two full-time hearing officer positions to address the backlog and ongoing caseload and one full-time attorney IV position to address the increased state and federal court litigation. These positions were authorized as limited-term for two years.

ALRB is requesting permanent augmentation for 1.5 hearing officer II positions, which would bring the ALRB's total permanent hearing officer staffing to three hearing officer positions. The hearing officer is the presiding administrative law judge and every case that comes before a hearing officer is fact-specific and unique in the complexity of the law involved. Hearing officer decisions are multifaceted and complex as cases can involve thousands of employees, resulting in numerous legal questions within a single case.

The ALRB notes that three permanent full-time hearing officer positions will allow them to timely schedule, preside over, and provide a final decision all in support of the protection of rights of California farmworkers. Moreover, ALRB recently opened a Santa Rosa sub-regional office, and is planning to open another office in the Indio sub-region, and notes that these additional offices will likely generate additional unfair labor practice filings, and increased workload through their presence in the area, as well as increased outreach to communities. Prior to the 2015-16 budget, it took 200 to 600 days to schedule a hearing. However, with the additional limited-term positions, hearings were scheduled within a 60 to 90 day time frame, which provided greater assurances to farmworkers will be available to participate in a hearing.

ALRB is also requesting permanent augmentation for the attorney IV position. In January 2014, to address the ALRB's increased state and federal court litigation workload, the Labor and Workforce Development Agency (LWDA) temporarily redirected resources to provide a limited-term Attorney IV position to the board to oversee, coordinate, and assist board counsel and attorneys assigned from the Office of the Attorney General to handle litigation. The 2015-16 budget provided a two year limited term attorney IV position for the ALRB, which expires in July. The primary responsibility of the attorney IV is appellate work where the position works with the three board vounsel positions to represent the ALRB in the most sensitive and complex matters.

Staff Recommendation. Approve as budgeted

7350 DEPARTMENT OF INDUSTRIAL RELATIONS**ISSUE 7: ENHANCED ENFORCEMENT COMPLIANCE AND APPRENTICESHIP SERVICES**

Summary. The Department of Industrial Relations requests 11 positions and \$1.7 million special funds in 2017-18, 25 positions and \$3.4 million special funds in 2018-19, with 19 positions and \$2.6 million special funds ongoing, to fulfill the provisions of recently chaptered legislation including:

- Assembly Bill 1066 (Gonzalez), Chapter 313, Statutes of 2016: Phase-In Overtime for Agriculture Workers
- Assembly Bill 1978 (Gonzalez), Chapter 373, Statutes of 2016: Property Service Workers
- Senate Bill 693 (Hueso), Chapter 774, Statutes of 2016: Workforce Expansion
- Senate Bill 1001 (Mitchell), Chapter 782, Statutes of 2016: Immigrant Workers Document Protections
- Senate Bill 1063 (Hall), Chapter 866, Statutes of 2016: Equal Pay – Race and Ethnicity
- Senate Bill 1167 (Mendoza), Chapter 839, Statutes of 2016: Indoor Heat Regulations

Background.

Assembly Bill 1066 (Gonzalez). AB 1066 removes an exemption for agricultural employees regarding hours, meal breaks, and other working conditions. The bill includes specific wage requirements, bringing farmworkers in line with the majority of employees in California who are protected by the existing mandate that any hours worked in excess of eight hours per day or 40 hours per week be paid at 1.5 times the regular pay. The bill provides for a phase-in approach for overtime requirements that gradually implement the eight hour workday for farmworkers over a four-year period.

The department requests \$40,000 for outreach in 2017-18, and two positions and \$308,000 in 2018-19, with \$267,000 ongoing to support its Division of Labor Standards Enforcement (DLSE) for increased workload created by the passage of AB 1066.

Assembly Bill 1978 (Gonzalez). AB 1978 establishes specific standards and protections for property service workers (otherwise known as janitors). The intent of the new law is to combat wage theft, ensure compliance with existing labor laws, and also lower instances of sexual harassment, sexual violence, and human trafficking in the property services industry, where it is particularly prevalent. The bill requires biennial in-person sexual violence and harassment training requirement for employees and employers, as well as requiring the registration of janitorial contractors with DIR.

The department requests an augmentation of three positions and \$442,000 in 2017-18, nine positions and \$1 million in 2018-19, with nine positions and \$967,000 ongoing. These positions will support DLSE in implementing the requirements under AB 1978.

Senate Bill 693 (Hueso). The Division of Apprenticeship Standards (DAS) promotes and develops apprenticeship training and enforces minimum apprenticeship standards. Among other mandates, DAS is the division within DIR responsible for approving new apprenticeships programs, ensuring that programs are adhering to its approved training standards, registering apprentices in approved programs, investigating apprentice complaints against programs, and issuing State certificates of completion to graduates of programs.

Because only registered apprentices may be paid a lower prevailing wage on publicly-funded “public works” projects, DAS regularly receives inquiries from the public to verify that a worker is a registered apprentice. Employers also contact DAS when they wish to confirm that worker has completed an apprenticeship and has graduated into a journey person. SB 693 allows a public entity to require a bidder, contractor, or other entity to use a skilled and trained workforce to complete a contract or project. DIR notes that the additional resources will allow the department to respond to inquiries and verification regarding DAS approved programs.

The Department requests one position and \$123,000 in 2017-18, (\$116,000) to provide resources for DAS to address additional workload as a result of SB 693.

Senate Bill 1001 (Mitchell). SB 1001 created a new protection that makes document abuse a strict liability violation regardless of intent. Specifically, this bill expands protection to immigrant applicants seeking employment by explicitly stating that it is unlawful to request more or different documents than required by federal law as a prerequisite to employment. The bill provides that an applicant for employment or an employee who believes their rights have been violated under this law may file a complaint with DLSE for equitable relief and penalties not to exceed \$10,000 per violation.

The department requests three positions and \$437,000 in 2017-18 and 2018-19 as a two-year limited-term funding, to support its DLSE for increased workload created by SB 1001.

Senate Bill 1063 (Hall). Existing law prohibits payment of a wage less than the wage rate paid to employees of the opposite sex for substantially similar work, when viewed as a composite of skill, effort, and responsibility, and performed under similar working conditions. SB 1063 adds a new and discrete equal pay protection to the existing protection for gender-based disparity to also include a prohibition against paying lesser wage to an employee based on race or ethnicity. The amendments made by SB 1063 are an individual worker protection that will be enforced by the DLSE’s Retaliation Complaint Investigation unit within DIR.

The department requests three positions and limited-term augmentation of \$415,000 in 2017-18 and \$392,000 in 2018-19, to implement the requirements of SB 1063 that will expand equal pay protections to include a prohibition against paying a lesser wage to an employee based on race or ethnicity.

Senate Bill 1167 (Mendoza). The Division of Occupational Safety and Health (DOSH) is the sole agency responsible for protecting workers from health and safety hazards on the job. DOSH protects workers in almost every workplace in California through its enforcement, research, and standards, and consultation programs. SB 1167 requires DOSH to develop a new heat-illness

prevention standard for indoor workers which would specify necessary measures to control indoor exposures to heat and would make compliance and enforcement easier and more effective. The new standard completed by this bill could prompt engineering and administrative changes to reduce risks of heat stress for indoor employees.

The Department requests one position and \$212,000 for 2017-18 and seven positions and \$1.1 million in 2018-19, with \$1.3 million ongoing, to provide resources for DOSH to address the new activity of indoor heat exposure inspections to protect California workers as required by SB 1167.

Staff Recommendation. Approve as budgeted.

Issue 8: Division of Apprenticeship Standards Federal Apprenticeship Grant Funding

Summary. The Department of Industrial Relations (DIR) requests six positions and \$923,000 one-time for 2017-18 from the Federal Trust Fund for the Division of Apprenticeship Standards (DAS) to expand the number of opportunities for Californians to gain employable lifetime skills and provide employers with a highly skilled and experienced workforce. Through focused outreach and education, DAS aims to register 6,000 new apprentices, including women and underrepresented apprentices; and engage 100 non-traditional industry sponsors from advanced manufacturing, information technology, healthcare and transportation for potential apprenticeship program development.

Background.

As part of the California workforce development system, the primary responsibility of DAS is to promote and develop employment based apprenticeship training programs, to improve apprentices' working conditions, and to advance profitable employment opportunities for apprentices. DAS accomplishes these objectives by providing consultative services to apprenticeship program sponsors, employers, employee organizations, and education providers.

DIR and its key partners, such as the Labor and Workforce Development Agency (LWDA) and the Employment Development Department (EDD), are responding to the state's workforce need by developing a strategy to enhance current apprenticeship programs and develop new programs that will help address the need for workers in high-demand sectors, and from under-served populations and/or geographic areas of the state.

The Employment and Training Administration (ETA) and the U.S. Department of Labor (DOL) announced the availability of approximately \$50.5 million to fund an estimated 33 quality grant applications competitively awarded to states through grant funds authorized by the Consolidated Appropriations Act of 2016 for Apprenticeship USA State Expansion Grants. The grant was designed to provide states with an opportunity to further align resources to innovate, expand, and diversify registered apprenticeship to better respond to industry workforce demands. California was awarded \$1.8 million over 18 months from the ApprenticeshipUSA State Expansion Grant.

On October 5, 2011, Governor Jerry Brown signed into law Assembly Bill 554 (Atkins) Chapter 499, Statutes of 2011, which requires the Workforce Development Board (WDB) to partner with apprenticeship programs, creating a smoother training pathway that broadens access to apprenticeships. In addition, in 2014 the federal government reauthorized the old Workforce Investment Act (WIA) with the Workforce Investment and Opportunity Act (WIOA). As a result, DAS staff has been collaborating with WIA and WIOA partners, namely the WDB and community colleges, to provide training through pre-apprenticeship as well as apprenticeship offered by approved apprenticeship programs and to create new on the job training and apprenticeship programs. DAS has been working with the Community Colleges' Sector Navigators to broaden opportunities for apprenticeship by recreating existing program curricula and developing apprenticeship programs for new industries. DAS also continues to work with multiple private and public entities that received Accelerator Grants from the California Community College Chancellor's Office in 2014, helping them to set up new apprenticeship

programs.

Apprenticeship Program Expansion in Non-Traditional Industries. High-growth industries in California that are best suited for potential apprenticeship programs have been identified. The EDD Regional Economic Analysis Profile details projected growth in specific geographical areas where it is expected that apprenticeship expansion in these industry clusters will stimulate economic market growth and boost employment opportunities statewide. Four of these industries (healthcare services, information and communication technologies, transportation and logistics, and advanced manufacturing), will be targeted for apprenticeship expansion based on the need for workforce and education programs. California is in its second grant application cycle for creation of innovative new apprenticeship demonstration projects, as part of its “California Apprenticeship Initiatives.” The first round of state grants, which included a \$15 million grant program, awarded eight pre-apprenticeship grants, 14 apprenticeship grants, and one grant for technical assistance and evaluation. These grants provided innovative approaches to new kinds of apprenticeship programs in a wide range of non-traditional industries and occupations ranging from registered nurses, and early childhood educators.

Training. This proposal also will help facilitate an educational campaign directed to California employers and their associations, informing them of their benefits of registered apprenticeship. DAS will provide a two-day training session for front-line staff in regional DAS offices to provide ongoing technical assistance, consultation and oversight to all program sponsors to ensure continuous compliance with apprenticeship law and regulation.

DAS will continue to work with and engage the California Apprenticeship Council (CAC) to focus on expanding and improving the overall quality of apprenticeship programs. The CAC meetings provide an ideal setting for training the CAC and the public on ways to promote new programs, utilizing its partnerships with local communities involving parents, educators, and businesses to better educate each other on apprenticeship principles and providing policy advice to attract new apprenticeship sponsors and increase apprenticeship registration.

Increased Apprentice Participation in Underrepresented Populations. This proposal builds on the success of existing pre-apprenticeship and apprenticeship pilot programs, and will begin expanding opportunities to low-income areas with training and high quality job opportunities. Women represent 50.3 percent of the population (U.S. Census Bureau, 2016) in California but only six percent of registered apprentices in the state. A blue ribbon panel met to address this issue and produced a set of recommendations focused on enhanced recruitment through outreach, retention strategies to increase graduation rates, and leadership pathways to train, support, and motivate women to enter positions of leadership. These recommendations are central to the current strategic plan to engage and successfully graduate more women apprentices in California.

Staff Recommendation. Approve as budgeted.

7920 CALIFORNIA STATE TEACHERS' RETIREMENT SYSTEM**Issue 9: CalSTRS Budget Proposals**

The following CalSTRS proposals are recommended for vote only.

1. **Enterprise Risk, Compliance and Cyber Security:** \$1.39 million special funds to establish 11 positions to address an increasing need in enterprise wide risk management, security, and compliance. Of these positions: (1) Four positions to support organization wide risk management and enhance internal controls; (2) Two positions in the Office of General Counsel and Procurement Management to support organization wide compliance and management; (3) Five positions for the Information Security Office in the Office of General Counsel to deploy enhanced cyber security and information management controls. A major data breach at CalSTRS could cost an estimated \$190 million and could impact the delivery of member benefits.
2. **Member Service Center Resources.** The Governor's budget includes 13 positions and \$1.3 million to support member benefit education efforts, communication regarding supplemental retirement savings, and other member and employer outreach activities requested by the Teachers' Retirement Board (TRB). The positions will address staffing needs in the Glendale, Riverside, and San Diego Member Service Centers (MSC). These centers have been operating for about four years.
 - One pension program manager and five associate pension program analysts (Glendale)
 - Three associate pension program analysts (San Diego)
 - Three associate pension program analysts (Riverside)
 - One associate governmental program analyst (HQ).

Staff Recommendation. Approve as budgeted.

Issue 10: Investment Portfolio Budget Change Proposal

Summary. The Governor's budget includes \$3.23 million for 16 positions to reduce risk and increase efficiencies in the management of the investment portfolio. Thirteen of these positions will address critical investments branch resource needs, as a result of increased size and complexity of the portfolio.

The Investment Branch's workload is driven and authorized by the Investment Committee. The Investment Committee is composed of the full Teachers' Retirement Board and adopts strategic asset allocation targets that are implemented over the long term. The Branch is organized into asset classes and sub-units of those classes. These classes are currently working at full capacity, and will be facing challenges caused by bringing more of the fund under internal management. This move is designed to benefit the fund as a result of the reduced costs and increased control that it can provide. The requested positions are proposed to be allocated to the various classes and units.

Two positions will support Financial Services to provide investment accounting, operating cash management, program allocation, and financial reporting for the portfolio. The last position will provide software support to both Financial Services and Investment Branch users of CalSTRS' enterprise resource planning software. The additional staff will allow each unit within the Investment Branch to implement asset allocation. The CalSTRS Investment Branch 10-Year Comprehensive Financial Plan forecasts that the portfolio's total assets will grow by \$49 billion from fiscal year 2016-17 to 2017-18, with external management costs increasing by \$25.4 million. CalSTRS states that for each staff added to support the internal management of portfolios, CalSTRS saves about \$1.2 million in external management fees per year.

Staff Recommendation: Approve as budgeted.

ITEMS FOR DISCUSSION AND VOTE

7501 DEPARTMENT OF HUMAN RESOURCES

Issue 11: Civil Service Improvement Trailer Bill Language

Summary. The Governor’s budget proposes trailer bill language to continue advancing the Administration’s Civil Service Improvement efforts.

Background. According to the Government Operations Agency (GovOps), which oversees various departments, including CalHR, the goal of the Civil Service Improvement initiative is to produce a modern human resource system that will allow state departments to find and quickly hire the best candidates through a fair and merit-based process. Departments will be able to determine their workforce needs and will be equipped to train and develop their employees to maximize their potential to serve the department’s mission. An improved civil service system will produce a capable and engaged state workforce.

The 2015-16 budget act adopted various civil service improvements, including (1) consolidating various hiring eligibility list requirements into a single process, under the “Rule of Three Ranks,” which would allow hiring managers to consider all eligible persons whose examination scores result in them being in the top three ranks; (2) Expanding the pool of candidates eligible to compete for a career executive assignment CEA position to include individuals from the private sector; and (3) Reconciling department budgets to help promote greater transparency in how departments develop their support budgets, which include vacant positions, personal services and operating expenses and equipment.

The 2016-17 Budget Act provided CalHR with 16 positions in 2016-17, and 17 positions in 2017-18 to implement civil service improvements. Additionally, the Legislature adopted trailer bill language to simplify the exempt appointee reinstatement guidelines, remove the probationary period for individuals who successfully complete the Limited Examination and Appointment Program job examination period and are appointed to a position, among others.

Governor’s Budget

The Administration proposes trailer bill language to do the following:

1. **Probationary periods.** Extends the maximum probationary period from up to six months to up to 2 years, and requires probation periods between ranges of a classification. The Administration notes that this provides department’s sufficient opportunity to review the performance of probationary employees, particularly in classifications where certain key duties and functions are cyclical, like budgets.
2. **Employee Eligibility Lists.** Removes current requirements for when a department may refresh open and promotional eligible lists. Existing law allows departments to remove names from lists after one year. If a list has less than three names, a department may remove the list prior to the one year timeline. The Administration notes that TBL allows

departments the flexibility to recruit qualified candidates to take civil service exams. Also removes outdated wording concerning when departments can fix clerical errors on an eligibility list.

3. **Job Announcements.** Removes current requirements of information that must be included in an examination announcement. Currently, departments are required to notice the time and location of the examination, minimum qualifications and general scope of examination, among others. The Administration notes this change will promote uniformity in job announcements, making it easier for job seekers to review the announcements.
4. **Promotional Exams.** Clarifies that policies established by departments which employees can take promotional examination must be consistent with State Personnel Board rules. The Administration notes that this change promotes uniformity, fairness, and consistency for employees taking promotional exams.
5. **Exam Demonstration Projects.** Adds “methods of examination”, which will allow the state to explore different exam methodologies through a demonstration project.
6. **Employee Transfers.** To promote a qualified civil service working force, the requirement that the employee seeking transfer must meet the minimum qualifications of the “to” class has been added.
7. **Reemployment Lists / Top Three Rankings.** Allows departments to establish more or less than three rankings for eligibility lists. Removes certain procedures regarding eligibility lists as a result of the changes being made to Government Code Section 19054.
8. **Certifying Candidates.** Removes language regarding certifying eligible for an employee list. The Administration notes that this process is cumbersome, costly, rigid, and often arbitrary. Instead, the employee list will be certified per SPB rules. Order of preference to apply to reemployment lists only.
9. **Definition of an employee class/ class consolidation.** Amends the definition of employee class to also mean consolidation of similar classes in the same occupational area based on broader duties and responsibilities. The Administration notes that this reduces the costs associated with promotional examinations and encouraging retention of a qualified state workforce. Promotes upward mobility by creating better career ladders.
10. **Employee transfers.** Allowing a CalHR or an appointing power to determine when minimum qualifications should be met through exam, to avoid inconsistent outcomes with SPB rules.
11. **Alternate Employee Lists.** Specifies that the statute is concerning “alternate employee lists” to avoid confusion with the employee lists as specified in Government Code Section 19054.

12. **Gender Equity.** Replaces the outdated phrase “female dominated jobs” with “jobs that employ a higher proportion of females than males.”
13. **Supervisor Training.** Amends existing requirement for supervisor to be provided a minimum of 20 hours of training from a biannual basis to a biennial basis.
14. **Various topics.** Technical changes, such as replacing a reference to “Department of Personnel Administration” with “Department of Human Resources” to reflect departmental duties pursuant to GRP 1. Clarifies that SPB has authority over “appointments”, which is already outlined in the constitution.
15. **State Personnel Board Authority.** Specifies that references to the word “rules” is equivalent to “board rules” and “rules of the board”, as used in this part of the Government Code. This is consistent with the Civil Service Act and allows SPB “to make rules concerning the subject matter” in the statute.

Staff Comments.

In 2015-16 and 2016-17, the Administration proposed civil service improvement reforms through the budget process. In the past, members of the subcommittee noted these proposals may have been better discussed through the policy committee process. This trailer bill is 45 pages long, and proposes significant policy changes to the civil service process. Similar to previous years, staff questions whether proposed trailer bill language has a budget nexus, and that the proposal may be better suited for a policy committee discussion, or in the collective bargaining process.

The trailer bill proposes to extend the maximum probationary period from up to six months to up to two years, and requires probation periods between ranges of a classification, however the Administration has not provided justification for why this is necessary, and what deficiencies are with the current probationary period is. Additionally, it is unclear why a probation period between ranges of a classification is necessary. Staff is concerned that this could lead to unintended consequences where an employee to be on probation for a substantial portion of their career.

Moreover, it is unclear why the Administration seeks to eliminate basic information, such as time, location, and minimum qualifications for a position, from an examination announcement. This information may help individuals seeking state employment, and should this information be eliminated, the public may lack basic transparent information on how to gain employment.

Staff Recommendation. Hold Open.

Issue 12: Judges Salaries Trailer Bill Language

Summary: The Governor's budget proposes trailer bill language to clarify the statutory methodology used to calculate annual salary adjustment for state judges and justices, which is based on the average salary growth of civil service state employees.

Background.

The 2016-17 budget included trailer bill, Senate Bill 848 (Committee on Budget and Fiscal Review) Chapter 848, Statutes of 2016, which clarifies the statutory methodology used to calculate the annual salary adjustment for state judges and justices to include both salary increases and decreases for state employees to be considered when calculating the average state wage growth for purposes of adjusting salaries of judges and justices. Prior to the enactment of SB 848, the calculation only considered the average salary increase of state employees in the calculation.

Currently, CalHR captures the scheduled salary increases to be provided to state employees during the next fiscal year, and applies those raises to judges on July 1 of the same fiscal year.

The Administration notes that the proposed trailer bill modifies the methodology in cases where the state reaches a labor agreement after July 1, that includes salary increases during that fiscal year. Specifically, the trailer bill requires that salary increases made after July 1 that have been provided retroactively to state workers on July 1, will be included in the judges' calculation during that same fiscal period to ensure they receive the same level of salary increase.

As a result of this new methodology, judges will receive a one-time retroactive payment equivalent to a 0.16 percent salary increase. Item 9800 includes \$1 million General Fund to cover the cost of this retroactive payment.

On July 1, 2016, only four bargaining units had ratified agreements (BUs 5, 6, 9, and 10) with scheduled salary increases that are effective July 1, 2016. These were used to calculate the judicial salary increase of 1.36 percent for 2016-17. The next judicial salary calculation will be made on July 1, 2017, and will include any general salary increases (GSIs) for employees in the remaining bargaining units that are ratified and become effective during the 2016–2017 fiscal year.

Under the current methodology, if there are bargaining units that reach a ratified agreement after July 1, 2016, on or before July 1, 2017, 2016-17 salary increases will be included in the calculation for the judicial salary increase effective July 1, 2017, not retroactively. While most new contracts include GSIs that are effective midway through 2016-17 or July 1, 2017, recently negotiated contracts with BUs 7 and 18 included GSIs retroactive to July 1, 2016. Absent this trailer bill language, these increases for BUs 7 and 18 would not be included as part of the judges calculation until July 1, 2017, nor would they be retroactive.

Staff Recommendation: Hold Open.

7100 EMPLOYMENT DEVELOPMENT DEPARTMENT**Issue 13: Tax Appeal Program Stabilization**

Summary. The California Unemployment Insurance Appeals Board (CUIAB) requests an augmentation of \$791,000 General Fund, \$791,000 Disability Insurance/Paid Family Leave (DI/PFL) funds and 12.5 positions (5.4 temporary position equivalents and 7.1 permanent position equivalents) in 2017-18 and 2018-19, and \$407,000 General Fund, \$407,000 DI/PFL funds, and 7.1 permanent position equivalents in 2019-20 and ongoing, to conduct mandated Tax Appeal Program functions in order to keep up with the incoming workload, reduce the high level of pending appeal caseload, and provide timely due process for California's employers who appeal their payroll tax liabilities and reserve account charges as assessed by EDD.

Background.

California Unemployment Insurance Appeals Board. The California Unemployment Insurance Appeals Board (CUIAB) was created by the Legislature in 1943, and is a quasi-judicial agency whose primary purpose is to conduct impartial hearings and issue prompt decisions to resolve disputed unemployment and disability determinations, and Employment Development Department (EDD) tax liability assessments. The Appeals Board consists of five members, three of which are appointed by the Governor and one each by the Senate Rules Committee and the Speaker of the Assembly.

If a party appeals an EDD decision, an Administrative Law Judge (ALJ) will review EDD's original decision. The ALJ can overturn, agree with, or modify EDD's decision. The losing party can appeal the ALJ's decision to CUIAB's board. The Board's decision is CUIAB's final decision. Workers and employers who disagree with CUIAB's final decision may appeal to the California Superior Court system, which is outside of CUIAB.

CUIAB's services are free to the participants, and do not require an attorney. The proceedings are funded almost completely by federal dollars, with state special funds paying for costs related to disability and paid family leave cases, and the state General Fund paying for less than one-half of one percent of the costs. In addition to reviewing judge's decisions, the Board issues precedent decisions and oversees CUIAB operations and its hearing facilities in twelve field offices and 43 satellite facilities around the state.

The EDD's tax program is a federal-state program that primarily collects and enforces payroll taxes from about one million California employers. When employers dispute EDD tax audits, tax liability statements, unemployment insurance (UI) reserve accounts and benefit charges, or other tax liabilities, they may file appeals with the CUIAB. Tax appeals make up about one percent of the total appeal caseload at the CUIAB, but take about three to four times the staff time to process as compared to benefit appeals.

The CUIAB has a high number of pending tax appeal and tax ruling appeal cases. As of July 31, 2016, the liabilities associated with CUIAB's current open balance of pending tax appeals total approximately \$339.5 million. This represents the tax liabilities at the time of the appeal, and then captured in CUIAB's appeal tracking system. When the EDD collects the upheld tax liabilities, the recovered monies are distributed among several funds.

According to the Administration, Each year, the CUIAB receives more tax appeals than it can process with the staff levels supported by available funding. This results in a growing number of pending tax appeals, delayed due process for employers, and delays in the State’s collection of upheld tax liabilities. For cases closed in SFY 2015-16, employers had waited 26 months on average, from the date the appeal was filed to the date the CUIAB decision was mailed, for resolution to their tax appeals. This also delays EDD’s collection of the tax liabilities upheld by CUIAB decisions. The Administration notes that the proposed additional resources will reduce the wait time from 26 months to about 9 months.

At the end of SFY 2015-16, the CUIAB had 4,800 pending first-level tax appeal cases and 3,400 pending first-level tax ruling appeal cases, for a total of 8,200 pending cases. During the fiscal year, the CUIAB received 2,500 new tax appeal cases and 1,200 new tax ruling appeals, for a total of 3,700 incoming cases.

According to the Administration, the total staffing needed to address the incoming workload and also reduce the pending caseload is 21.9 PEs, including one Presiding ALJ PE, 9.2 ALJ PEs, and 11.7 PEs in support staff. However, the CUIAB only receives enough funding to support 9.4 PEs, including 5.0 ALJ PEs. The UI funding is allocated by the EDD from the federal UI grant funds, based on an agreement with US Department of Labor, to fund CUIAB Tax Appeal Program activities.

SFYs 2017-18 & 2018-19	Projected Workload	First Level Avg Workload per ALJ	Second Level Avg Workload per ALJ	Presiding ALJ PEs	ALJ PEs	Support Staff PEs	Total PEs Needed	Current Staff Funded	Additional Staff Needed
Tax Appeals	3,770	474	379	1.0	8.1	10.7	19.8	8.4	11.4
Tax Ruling Appeals	1,830	1,622	1,298	-	1.1	1.0	2.1	1.0	1.1
Total	5,600			1.0	9.2	11.7	21.9	9.4	12.5

SFY 2019-20 & On Going	Projected Workload	First Level Avg Workload per ALJ	Second Level Avg Workload per ALJ	Presiding ALJ PEs	ALJ PEs	Support Staff PEs	Total PEs Needed	Current Staff Funded	Additional Staff Needed
Tax Appeals	2,620	474	379	1.0	5.6	8.2	14.8	8.4	6.4
Tax Ruling Appeals	1,220	1,622	1,298	-	0.7	1.0	1.7	1.0	0.7
Total	3,840			1.0	6.3	9.2	16.5	9.4	7.1

Staff Recommendation: Approve as budgeted.

Issue 14: Benefit Systems Modernization

Summary. The Governor proposes one-time \$4 million in special funds, and 15 positions, and a redirection of \$3.16 million in special funds and 15 positions in 2017-18 to complete stage two of the project approval lifecycle for its Benefit Systems Modernization Project. Included in the funding above is \$1.8 million as part of the one-time budget augmentation toward the requirements vendor contract, and \$1.1 million in provisional language. The resources will be for state staff, requirements vendor, project oversight from California Department of Technology, and for Independent Verification and Validation vendor services to continue activities towards building an integrated, secure and sustainable Benefits System to service California claimants seeking unemployment, disability or paid family leave benefits.

Background.

The EDD administers several benefit programs, including the Unemployment Insurance (UI), Disability Insurance (DI), and Paid Family Leave (PFL) programs that provide financial stability to workers and communities.

In 2012, a partial system modernization was completed for both the DI program, which implemented DI Online, and for the UI program, which implemented UI Online in 2015. The PFL system has not been modernized since being implemented in 2004. While the partial system modernization projects provided some relief in terms of new customer self-service capabilities, the resulting systems are now overly complex and not sustainable from both technology and staffing standpoints. The EDD possesses three independent, non-integrated benefit systems that all rely to varying degrees on an aging mainframe, Common Business Oriented Language (COBOL)-based system, as well as legacy external sub-systems and components. Maintaining viable system interfaces and data integrity between disparate benefit system databases that reside on different technological platforms is very complex, expensive, and difficult to maintain. In addition to the many technology challenges, recruitment and retention of staff with the COBOL skillset is increasing difficult as there is a diminishing base of staff with COBOL system knowledge.

EDD notes the following challenges with its current systems:

1. External Customers

- Limited Capabilities: Full service functionality and real time information is not available via the Internet and using smart phones.
- System Changes are Slow & Costly: EDD can't respond timely to customer, stakeholder, and legislative needs and expectations.

2. EDD Program Staff

- Complex: The legacy system and new system combination requires more staff time to use and maintain. There are many manual processes.
- Duplication: Multiple systems retain the same data and overlapping functions to ensure coordination between disparate systems. This results in duplicate work efforts and constant data synchronization problems.

- Work Arounds: Staff-built work-arounds (for example the use of 500 macros) in the legacy system result in mission critical undocumented and unsupported processes.

3. EDD Technical Staff

- High cost associated with maintaining both legacy and new systems.
 - a. SFY 2015-16 vendor only maintenance and operations support cost for current benefit systems was \$17.8 million.
 - b. Program funding has not kept pace with the increasing cost of maintaining the legacy and new systems.

As a result, the existing benefit systems are not fiscally sustainable. The EDD's customers experience a lack of consistency when utilizing the various benefit systems, certain customer groups cannot utilize online services and must submit information manually or through contacting an EDD representative.

Project Approval Lifecycle. The Department of Technology adopted the Project Approval Lifecycle (PAL) to improve the quality, value and likelihood of success for information technology (IT) projects undertaken by the State of California. The PAL is divided into four stages (Stage 1 Business Analysis, Stage 2 Alternatives Analysis, Stage 3 Solution Development and Stage 4 Project Readiness and Approval) each separated by gates of approval. Each stage consists of a set of prescribed, cross-functional, and parallel activities to develop deliverables used as the inputs for the next stage. The gates provide a series of “go/no go” decision points that request only the necessary and known information needed to make decisions for that particular point in time. Based on Stage 1 findings for the project, the Department of Technology identifies an estimated 10 percent savings in UI, DI, PFL and IT staff costs in addition to reductions in existing vendor contract costs following full implementation. The 10 percent figure is an estimate that will be further refined as this effort advances through the remaining PAL Stages.

Stage 2 provides a basis for project management, program and business management, executive management, and state-level control agencies to understand and agree on how the proposal's business objectives will be achieved. Market research is also conducted in Stage 2 based on the stated objectives as the means to research viable IT solutions (alternatives) available in the open market. Market research provides a process for gathering data on product characteristics, suppliers' capabilities and the business practices that surround them—plus the analysis of that data to define viable solution alternatives and make informed procurement decisions.

Governor's Budget.

The Governor proposes one-time \$4 million in special funds, and 15 positions, and a redirection of \$3.16 million in special funds and 15 positions in 2017-18 to complete stage two of the project approval lifecycle for its Benefit Systems Modernization Project.

Additionally, as part of the one-time budget augmentation, \$1.8 million is for the vendor contract. Budget Act provisional language would allow EDD's budget to be augmented by up to \$1.0 million, provided there is sufficient justification for an increase, in order to fully fund the

requirements vendor contract.

The Administration anticipates substantial ongoing savings after full systems replacement. These savings would derive from automating many Unemployment Insurance (UI), Disability Insurance (DI) and Paid Family Leave (PFL) claim filing processes that are currently done manually as well as eliminating the need for Information Technology (IT) staff to support existing legacy mainframe applications. The Business Analysis (Stage 1) of CDT's PAL process identifies an estimated 10 percent savings in UI, DI, PFL and IT staff costs in addition to reductions in existing vendor contract costs following full implementation. The 10 percent figure is an estimate that will be further refined as this effort advances through the remaining PAL Stages. This includes reaching out to states that have already enacted full modernizations to identify what the impact to their ongoing programmatic and support costs has been post implementation. Stage 2 of the PAL process will help the Department determine what ongoing savings may be realized by full systems replacement with the ultimate goal of reducing or eliminating the ongoing need for the UI program to rely on state General Fund support. This information will be used to plan and schedule future General Fund reductions as appropriate. This effort is EDD's primary strategy to reduce the UI program's dependence on the General Fund for supplemental funding.

The EDD has determined that the addition of ITB project managers and staff, and a redirection of program staff, is critical for the successful completion of the project planning phase. Program staff will be redirected full time to focus on the PAL activities and a backfill will be done to ensure the daily program duties are performed.

1. **One Benefits System:** EDD will replace three stand-alone systems with one benefits system that provides all functionality. This will mitigate the legacy system issues currently experienced including the ongoing support costs and sustainability. Other benefits include: mitigating data synchronization issues by having one logical database, eliminating duplicate logic/services thereby simplifying the system support required, and reducing the risk of erroneous data entry and duplication. Having one technology development platform reduces complexity and allows for more timely changes to the system. Faster issue resolution and the ability to develop, test, and release more system enhancements increases productivity.
2. **Technology Support:** Having one technology platform will reduce IT staff support costs as staff would only have one technology platform to support. Current benefit systems require different skill sets to maintain the systems (COBOL, .Net, Structured Query Language, and Database 2). With one platform, technical support staff, including developers and testers, will need to know one system, framework, etc.
3. **Better Service to Customers:** Having one benefits system will provide claimants and employers a single portal to EDD services. Customers using one benefits system will experience the same look and feel across all of the benefit programs across EDD. This will result in fewer identity and account management issues by having a standardized process for establishing a customer's identity. System availability will be improved by having fewer systems and sub-systems reliant on one another for business processing.

The EDD has determined that the addition of ITB project managers and staff, and a redirection of program staff, is critical for the successful completion of the project planning phase. Program staff will be redirected full time to focus on the PAL activities and a backfill will be done to ensure the daily program duties are performed.

Staff Recommendation. Approve as budgeted.

7350 DEPARTMENT OF INDUSTRIAL RELATIONS**Issue 15: Strategic Enforcement of Labor Standards**

Summary. The Administration proposes a three year phase-in and an increase of 31 positions and \$4.6 million in 2017-18, 58.5 positions and \$8.6 million in 2018-19, 82.5 positions and \$11.6 million in 2019-20, and \$11.4 million ongoing from the Labor Enforcement and Compliance Fund. These resources seek to combat wage theft and labor law violations. Additionally, the Administration is proposing accompanying trailer bill to address enforcement issues.

Background.

Division of Labor Standards Enforcement (DLSE) Responsible for Enforcing Labor Standards. State law places responsibility for enforcing labor standards on DLSE within the Department of Industrial Relations (DIR). The division is headed by the Labor Commissioner and carries out its enforcement responsibilities through several units:

- Bureau of Field Enforcement (BOFE). The BOFE carries out investigations of employers to enforce labor standards. Most BOFE investigations are the result of a complaint submitted to DLSE, but BOFE also initiates some investigations proactively. When an investigation identifies noncompliance, BOFE issues citations with penalties plus the amount of unpaid wages due to workers, if any. The BOFE also defends citations when they are appealed.
- Wage Claims Adjudication (WCA). This unit provides an administrative process for individual workers to pursue unpaid wages and other damages from an employer who has violated wage and hour requirements.
- Judgment Enforcement Unit (JEU). The JEU collects unpaid wages and penalties that are assessed against employers. Several strategies are used for collection, including the use of liens (which prevent the employer's property from being sold until unpaid wages and penalties are paid) and levies (which allow DLSE to seize unpaid wages and penalties from an employer's bank accounts and other property).
- Retaliation Complaints Investigations (RCI). The RCI unit investigates complaints from workers who allege that they faced unlawful retaliation - such as dismissal - because they engaged in certain protected activities, such as reporting a labor

standards violation to DLSE or threatening to report a violation. Following an investigation, the RCI unit issues a determination that may include requiring the employer to take actions to address the retaliation, such as reinstating the worker. If an employer does not comply with a determination, DLSE may pursue enforcement of its determination in trial court.

DLSE Funding. DLSE is funded almost entirely from various special funds. The LECF receives

revenues from an assessment on all employers that equals a percentage of the workers' compensation insurance premiums paid by employers. The amount of this assessment is set annually by DIR to cover the amount of spending from the LECF approved in the state budget.

Strategic Enforcement. In recent years, BOFE has targeted more of its investigations using what the administration describes as a strategic enforcement approach. This approach focuses on wage and hour violations, which are relatively complex and time-consuming to investigate, over violations of more easily verified violations like not carrying workers' compensation coverage. This approach also involves collaboration with worker and industry organizations (such as community-based groups, unions, and employer or industry associations) to identify targets for investigation and otherwise facilitate the investigation process. Specifically, the intent of the strategic enforcement approach is to take advantage of worker and industry organizations' ability to (1) provide information about which employers may have particularly serious or extensive labor standards violations and (2) facilitate the cooperation of workers, who play a significant role in investigations of wage and overtime violations but may be hesitant in some cases to cooperate with DLSE investigations because of distrust toward the agency or fear of retaliation from the employer. The new funding and positions requested in the Governor's proposal are intended to allow DLSE to increase the number of investigations conducted under the strategic enforcement approach.

Budget Change Proposal (BCP) Request. The BCP includes a significant increase to BOFE staff phased in over three years, with a 63 percent increase in BOFE staff in 2019-20, compared to 2016-17. Additionally, the BCP includes funding and positions to allow DLSE to increase the number of investigations conducted under the strategic enforcement approach. This approach focuses on wage and hour violations, which are relatively complex and time-consuming to investigate over violations of more easily verified violations, like not carrying workers' compensation coverage. The Administration's strategic enforcement approach also involves collaboration with worker and industry organizations (such as community-based groups, unions, and employer or industry associations) to identify targets for investigation and otherwise facilitate the investigation process.

Finally, the proposal identifies several industries as priorities for additional investigations. The priority industries include janitorial services, garment manufacturing, construction, residential care homes for the elderly and person with disabilities, car washes, agriculture, food processing, and restaurants. These industries overlap with industries previously identified by the Legislature as warranting an elevated level of oversight.

Trailer Bill Language. According to the DOF and the department, the proposed trailer bill language addresses many investigative and administrative process inefficiencies that encumber the Division staff in their investigations, enforcement actions, and payment of final wage judgements to workers. The main changes of the trailer bill are summarized below:

Changes to General Labor Standards Enforcement Processes

- Specify that the statute of limitations on workers recovering unpaid wages and other penalties (generally two to four years) looks back from the date that an employer is

notified of a BOFE investigation instead of the date citations are issued, to preserve the ability to recover unpaid wages and penalties that would have moved beyond the statute of limitations by the time a citation is issued.

- Allow BOFE citations to be served through certified mail. Currently, citations generally must be served in person.
- With some exceptions, prohibit employers from introducing documents as evidence to appeal a BOFE citation if those documents were previously requested as part of the BOFE investigation but were not provided.
- Allow certain workers in the car wash, farm labor, and garment manufacturing industries to recover unpaid wages and other damages from existing state special funds, and allow DLSE to subsequently recover the unpaid wages and damages from employers to reimburse those special funds. Currently, workers in these industries may only be compensated from the special funds for amounts they are unable to recover from the employer.
- Require the Department of Alcoholic Beverage Control, the Board of Barbering and Cosmetology, and the Bureau of Automotive Repairs to suspend or revoke licenses for employers if they have not satisfied judgments for unpaid wages and other damages. This is similar to an existing process at the Contractors State License Board.

Changes to Retaliation Investigation Processes

- Pause the statute of limitations for workers to pursue legal action against an employer for retaliation while a retaliation complaint is investigated by DLSE.
- Allow DLSE to decline to investigate a retaliation claim if the worker has initiated a parallel claim in another venue, such as challenging the alleged retaliation with the State Personnel Board, through a collective bargaining agreement grievance procedure, or through the courts.
- Allow DLSE to request a court order to temporarily reinstate a worker while a retaliation complaint investigation is ongoing.
- Extend the time the RCI unit has to investigate a retaliation complaint from 60 days to 1 year.
- Extend the time for employers to comply with DLSE's determination on a retaliation complaint investigation from 10 days to 30 days.
- Give the labor commissioner the discretion to delegate the approval of reports that are generated from retaliation complaint investigations. Currently, only the labor commissioner or a chief deputy may approve the reports.

- Eliminate the ability for parties to a retaliation complaint investigation to appeal DLSE's determinations to the director of DIR, except in certain cases where an administrative appeal is required by federal law.
- Specify that, if DLSE pursues court action to enforce its determination from a retaliation complaint investigation, it must do so within three years.
- Require an employer to pay for DLSE's legal costs when DLSE prevails in an action to enforce its determination on a retaliation complaint investigation.
- Place penalties on employers that willfully refuse to comply with a court order to enforce DLSE's determination from a retaliation complaint investigation.
- Clarify that workers may not be retaliated against for reporting a work-rated fatality, injury, or illness, or other activities protected by the federal Occupational Safety and Health Act.

Legislative Analyst's Office Comments.

Targeting of BOFE Inspections Appears to Have Significantly Improved in Recent Years.

The LAO notes legislatively-required reports for 2009-10 through 2013-14 indicates that the targeting of BOFE inspections significantly improved over this period. While the number of inspections and citations declined; the average number of citations per inspection increased—suggesting an increasing emphasis on employers with multiple violations over employers with fewer or no violations. The LAO notes that this measure does not necessarily indicate whether the violations uncovered through these inspections were the most serious. Additionally, the average amount of unpaid wages found due per filled staff position in BOFE also increased significantly over the same period, suggesting that resources dedicated to investigations of wage and hour violations became increasingly effective.

DLSE's Data Collection and Analysis Capabilities Are Still Developing. The DLSE implemented CalAtlas, an information technology system used to track complaints and investigations statewide, roughly six months ago. Prior to CalAtlas, information about complaints and investigations was not tracked consistently across field offices, limiting DLSE's ability to assess trends in complaints and analyze the effectiveness of past investigations and use this analysis to refine investigation targeting. The CalAtlas system represents a step forward in DLSE's ability to track information about complaints and investigations and use this information to improve their effectiveness. However, the Governor's proposal does not describe how the information that will be collected in CalAtlas will be used to inform strategic targeting of investigation resources going forward. Given how recently the new system was brought online, the LAO is concerned that DLSE's data collection and analysis capabilities may not have sufficiently developed to ensure the most effective use of the proposed increased staff.

Statutorily Required Report Is Past Due. As mentioned previously, state law requires that DLSE report to the Legislature each March on BOFE operations. Among other things, these reports are required to contain information about the labor commissioner's enforcement plan, the number of investigations conducted and the types of violations found, the amount of wages

found to be unlawfully withheld from workers and the amount of such wages collected. The most recent annual report to the Legislature was submitted in 2015, for the 2013-14 fiscal year. A report for 2014-15 should have been submitted in March 2016 but, as of the writing of this post, has not yet been submitted. A report for 2015-16 would be expected in March 2017. The Governor's proposal suggests that in future years the annual BOFE report would be the primary way that DLSE would update the Legislature about the outcomes and effectiveness of the requested new positions and funding. The delay in issuing the statutorily required report makes it difficult for the Legislature to evaluate the more recent effectiveness of BOFE inspections (that is, after 2013-14) and raises concerns about whether the annual BOFE report would be an adequate means for DLSE to report to the Legislature on the outcomes of this proposal.

Vacancies Are a Concern. In 2015-16, roughly 18 of the BOFE's 94 approved positions (about 20 percent) were vacant. The DLSE has identified several issues that have led to this level of vacancies, including problems with administrative challenges that prevented hiring for certain key investigative classifications for a period of time, infrequent examinations and small hiring lists, and increased retirements. The DLSE has taken some steps to reduce the number of vacancies and believes it has sufficient funding to fill previously approved but vacant positions. The 20 percent vacancy rate in 2015-16 represents an improvement over prior years, but the LAO remains concerned that a significant portion of the positions requested in the Governor's proposal might not be filled on a timely basis if they are approved.

The LAO recommends that the Legislature not approve further increases requested for 2018-19 and later years, instead requiring DLSE to return with a follow-up proposal as part of the Governor's 2018-19 budget. This approach would allow the Legislature to receive additional information on the implementation of any funding and positions approved for 2017-18, prior to approving any additional funding or positions.

Some Proposed Law Changes More Directly Related to Budget Proposal Than Others. The Governor's proposed trailer bill touches on many aspects of DLSE enforcement. Some of the proposed changes, such as allowing BOFE to serve citations through the mail, are directly related to creating efficiencies in enforcement processes and merit the Legislature's serious consideration. Other proposed changes are less related to the budget proposal, such as imposing new penalties on employers that fail to comply with a court's order to enforce DLSE's determination from a retaliation complaint investigation. These proposed changes may have merit, but may be deliberated to understand their implications. In order to fully understand the effects of the Governor's proposed trailer bill, the LAO recommends that the Legislature invite stakeholders, including workers, worker representatives, and employers, to comment on the various proposals' implications.

Staff Recommendation. Hold Open.

Issue 16: Public Works Enforcement

Summary. The Administration is proposing six positions and \$805,000 in 2017-18, and \$759,000 in 2018-19 from the Labor and Workforce Development Fund to education awarding bodies of their requirements to comply with registration requirements, and one attorney position with \$212,000 in 2017-18 and \$204,000 ongoing from the State Public Works Enforcement Fund. Additionally, the Administration is proposing to trailer bill language to increase enforcement and compliance with registration compliance.

Background

Existing law places certain requirements on most construction projects that receive public funding, referred to as “public works projects.” One of these requirements is that contractors on public works projects pay their workers “prevailing wages”—defined as the wages paid to a majority of workers in a particular type of work within the locality where the work is performed. The Labor Code also establishes other requirements for public works projects, including a requirement that contractors on certain public works projects employ apprentices. State law places responsibility for enforcing public works requirements on the Division of Labor Standards Enforcement (DLSE), within DIR. Specific DLSE responsibilities include determining prevailing wage rates, reviewing contractors’ payroll records, and conducting onsite investigations of public works projects.

Currently, the prevailing wage determination function and enforcement of the public works requirements are funded from the State Public Works Enforcement Fund (SPWEF), a special fund that receives revenues from an annual registration fee of \$300 paid by all contractors that wish to bid on public works contracts. The SPWEF is solely used to support public works enforcement. The contractor registration fee was established as part of the 2014-15 budget package. Prior to 2014-15, public works enforcement was supported by a combination of the Labor Enforcement and Compliance Fund (LECF), which receives the proceeds of a general assessment on all employers; a fee on bond proceeds for bond-funded public works projects; and the General Fund. Over the years, challenges with the previous system of collecting fees on bond proceeds made it difficult for DLSE to generate sufficient revenue to maintain public works enforcement, requiring the SPWEF to receive loans from other special funds and the General Fund. Currently, the SPWEF has a \$1.3 million loan from the General Fund, a \$2.2 million loan from the Uninsured Employer Benefit Trust Fund, and a \$5 million loan from the Occupational Safety and Health Fund that have not been repaid.

The Administration notes that the annual revenues from the recently created contractor registration fee are less than estimated when the fee was established and do not cover current spending levels for public works enforcement. Specifically, the administration estimates that expenditures from the SPWEF in 2016-17 will be \$13 million, while revenues coming into the SPWEF from the contractor registration fee will be only \$10 million. The shortfall of revenues will result in a \$3 million decline in the SPWEF’s reserve. If fee revenues continue at this level and no adjustments are made to spending levels, SPWEF’s reserves would be virtually exhausted in 2017-18.

The Administration believes that one reason revenues have not met expectations is that some

contractors may not be complying with the registration requirement. During 2015-16, less than 30,000 contractors registered and paid the fee, compared to an initial rough estimate of 40,000 or more registrations. Through its enforcement efforts, DLSE found about 600 instances where contractors were working on a public works project during 2015-16 without registration. Contractors that are found to be bidding or working on a public works contract without registration are subject to a penalty of up to \$2,000 and may face temporary disqualification from bidding or working on public works projects for repeat violations.

The Administration also notes that some institutions that award public works contracts, known as “awarding bodies,” may not be adequately verifying that contractors bidding on projects have complied with the registration requirement before awarding the contract, thus potentially contributing to contractor noncompliance and reduced fee revenues. There currently is no specific penalty for an awarding body that fails to verify that contractors bidding or working on public works contracts are registered.

Governor’s Proposal

The Governor proposes a few actions to address the funding shortfall in the SPWEF in 2017-18 and later years. First, the Governor proposes to provide funding to DLSE on a two-year limited-term basis for six positions to conduct outreach with awarding bodies to improve their awareness of their responsibility to ensure that contractors have complied with this requirement, with the intent of increasing compliance and fee revenue over time. Funding for these positions—\$805,000 in 2017-18 and \$759,000 in 2018-19—would be provided from the Labor and Workforce Development Fund (LWDF), a special fund designated for enforcing Labor Code provisions and educating employers and workers about labor law. As part of this outreach, DLSE would encourage awarding bodies to require contractors to “prequalify,” or demonstrate compliance with various labor law requirements, including the contractor registration requirement, before bidding on public works contracts. Under current law, awarding bodies are authorized, but most are not mandated, to require contractors to prequalify. DLSE believes that increased use of prequalification could increase compliance with the contractor registration requirement and with labor law requirements generally.

The Governor’s proposal would reduce expenditures from the SPWEF by moving the support of the prevailing wage determination function from the SPWEF to the LECF beginning in 2017-18. This action would free up \$2.2 million in the SPWEF on an ongoing basis and would largely address the funding imbalance going forward, even if contractor registration fee revenues remain flat in future years.

For 2017-18 only, the Governor proposes to shift the portion of statewide administrative costs allocated to the SPWEF (such as the fund’s portion of reimbursements to the state Department of Finance and Department of Human Resources) to other special funds administered by DIR. This one-time action frees up an additional \$1.1 million in the SPWEF in 2017-18.

Current law gives DLSE the authority to “debar,” or prohibit a contractor from bidding or working on public works contracts, for up to three years if the contractor violates public works requirements under certain conditions. The Governor’s proposal would provide \$212,000 from the SPWEF for one additional Attorney III position to allow DLSE to conduct additional debarment proceedings.

In addition to the budget change proposal, the Administration is also proposing trailer bill language. Below is a summary of some of the key provisions included in the TBL:

- **Effective Date.** Applies requirement to register as a public works contractor to work performed on or after January 1, 2018, regardless of a contract date.
- **Small Projects Exemption.** Provides administrative relief for contractors and awarding agencies on small projects. Among the provisions, the TBL creates a new minimum threshold triggering registration requirement for projects over \$25,000 for new construction; over \$15,000 for maintenance.
- **Unregistered Contractor Sanctions.** Among its provisions, the TBL requires all contractors and subcontractors engaged in the performance of a public work must be registered. If the Labor Commissioner determines that a contractor or subcontractor has violated the registration requirement, unregistered contractors shall forfeit as a civil penalty to the state \$100 per day up to \$8,000. A registered public works contractor or subcontractor who enters into a contract with an unregistered lower-tier subcontract to perform any public work shall be subject to one or both of loss of registration from the current year, and a civil penalty of \$100 per day, up to \$10,000.
- **Public Works Fund.** Specifies that DOF and LWDA may approve a short-term loan each fiscal year from the LECF to the SPWF. Amends previous language specifying the loan source was the Labor and Workforce Development Fund.
- **Awarding Agency Sanctions.** Specifies that an Awarding Agency (AA) authority that fails to provide the notice to DIR, or enters into contract with or permits unregistered contractor or subcontractor to engage in work, is subject to fine of \$100 per day up to \$10,000. Additionally, if Labor Commissioner determines that AA willfully violated requirements of this section or chapter on 2 more projects within a 12 month period, the AA shall be ineligible to receive state funding or financial assistance for any construction project undertaken by the AA for one year. Penalties received shall be deposited into the State Public Works Enforcement Fund.
- **Liquidated Damages Waiver.** This bill deletes authority to waive liquidated damages for unpaid wages.

Legislative Analyst's Office Comments.

The LAO notes that the Administration's proposal to begin paying for the costs of prevailing wage determinations from the LECF instead of the SPWEF is a reasonable and straightforward way to relieve pressure on the SPWEF in the near term while the administration pursues efforts to increase SPWEF revenues through greater compliance with the contractor registration requirement. However, the LAO believes that the SPWEF is the preferable long-term funding source. Shifting the prevailing wage determination function to the LECF would mean that the costs of determining prevailing wages are funded from a general assessment on all employers, most of whom are not affected by prevailing wage requirements. Ideally, the prevailing wage

determination function would eventually shift back to the SPWEF as compliance with the contractor registration requirement improves and fee revenues increase. If the Legislature shifts prevailing wage determination to the LECF, the LAO recommends that the Legislature require that DLSE report at a later date on the feasibility of returning the prevailing wage determination function to the SPWEF.

The LAO notes that there may be other factors that affect compliance with the registration requirement that are at least as important as awarding bodies' awareness of their responsibilities, including the extent to which awarding bodies are (or are not) held accountable for verifying the registration of contractors. The proposal to provide temporary positions for outreach to awarding bodies should be considered in the context of other possible changes to increase awarding bodies' incentives to verify contractor registration. The administration's recently trailer bill proposal appears to include provisions intended to address some of these compliance issues.

The LAO recommends that the Legislature require DLSE to report by March 2019 on (1) changes in the amount of contractor registration fees collected; (2) the estimated effect of any efforts to increase compliance with the contractor registration fee, including outreach to awarding bodies and other steps to increase awarding body accountability for ensuring contractor registration; (3) what adjustments are necessary to the level of the contractor registration fee in order to support ongoing public works enforcement costs and repay the SPWEF's outstanding loans to other funds; and (4) the feasibility of shifting support for the prevailing wage determination function back to the SPWEF.

The LAO notes that given uncertainty in the level of ongoing contractor registration fee revenues in the SPWEF, it is premature to approve the administration's requested staff to pursue additional contractor debarments, even after taking steps to reduce SPWEF expenditures (such as shifting public works determination to the LECF). Accordingly, the LAO recommends the Legislature reject the proposed position.

Staff Comments. The subcommittee may wish to discuss with the Department what strategies are available to ensure oversight and the long term success of the program. The changes proposed in the trailer bill assume that shifting the responsibility and penalties to the awarding bodies will increase compliance. The funding for the program has had a history of challenges and it is uncertain how these changes will provide stability. Staff notes that it may be premature to permanently shift funding back to the LECF. Instead, shifting funding to the LECF in the short-term may be a more efficient approach, and have DIR report back based on the recommendations that the LAO. This may help the Legislature develop a better understanding of the impacts the BCP and trailer bill language has had on program and its fund condition. The LAO makes a reasonable argument that increasing staff for debarment may be premature, especially since the future funding for the program is uncertain. DIR has indicated that they are amenable to some type of reporting requirement.

Staff Recommendation. Hold Open.

Issue 17: Process Safety Management Unit - Non-Refinery Inspections

Summary. This proposal requests 13.0 positions, 10.0 of which will be safety engineers, and an augmentation of \$2.5 million in 2017-18 and \$2.4 million ongoing, to the Occupational Safety and Health Fund for the Division of Occupational Safety and Health (DOSH) to expand the existing Process Safety Management (PSM) non-refinery inspection program from 45 annual Program Quality Verification inspections to a total of 113 inspections annually.

Background. The 2014-15 budget increased the PSM function by 15.0 positions (11.0 new positions and 4.0 redirected from within DOSH) and \$2.4 million, which focused exclusively on the refinery inspection needs for the 15 refineries located in the state. The resources also allowed DOSH to acquire the necessary data, and develop the requisite methodology for evaluating and categorizing risk in the various non-refinery facilities.

California has approximately 1,940 non-refinery industrial facilities that handle or process anywhere from 50 to 120 million pounds of hazardous chemicals. These facilities include, but are not limited to, ammonia refrigeration, water treatment and wastewater treatment, chemical plants, and explosives manufacturers. All of these facilities fall under the jurisdiction of the PSM Unit.

In response to Senate inquiries and Supplemental Report Language regarding the number of staff and inspections required to provide adequate oversight of non-refinery facilities, DIR submitted a status report to the Legislature during 2016-17 budget hearings. The status report outlined the amount of resources needed to achieve various inspections levels, but did not make any specific recommendations regarding enforcement levels requested by DOSH at that time. This proposal identifies the augmentation needed to increase the capacity to inspect non-refinery facilities.

The PSM non-refinery program currently has six Safety Engineers (SE's) that are trained to conduct program quality verification (PQV) inspections. Three are located in the Santa Ana District Office and three are located in the Concord District Office. A PQV is a planned, proactive inspection and is a thorough assessment of a facility's safety preparations and emergency response procedures. A PQV inspection is more expansive than complaint and/or accident inspections, which are reactive in nature and generally focused on the specifics which gave rise to the accident or complaint. The other inspections may include, but are not limited to: referrals from other government agencies, and records and permit inspections.

To target non-refinery inspections on facilities that pose the greatest health and safety risk to workers and the public, DIR collaborates with the US Environmental Protection Agency (US EPA) to obtain risk information. As a result, the state has now ranked the 1,940 facilities on the basis of their risk to workers and the public. Each inspector is able to conduct about 7.5 inspections per year, at a rate of 200 to 300 hours per inspection, for an annual total of 45 PQV inspections statewide, exceeding the goal of 40 inspections which had been established for 2014-15. Under this proposal, the unit will increase its annual PQV inspections from 45 annually, to about 113 annually.

Staff Recommendation. Approve as Budgeted.

7900 CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM**Issue 18: Healthcare Fund Administrative Expenses Trailer and Budget Bill Language**

The Administration has proposed trailer and budget bill language that would do the following:

- **Require All Administrative Costs Be Paid from Contingency Reserve Fund (CRF).** Under the proposed language, all administrative expenses currently being paid from the Health Care Fund (HCF) would be paid from the Contingency Reserve Fund (CRF). Any future administrative expenses - regardless of health plan - would be paid only from the CRF. The proposed language does not eliminate the HCF. Instead, the HCF would continue to be used to pay for specified non-administrative costs.
- **Changes Language Related to Local Government Contributions to CRF.** The proposed language makes a number of changes to Section 22901 of the Government Code related to local government's contributions to the CRF. The language would require local governments to pay (1) the same surcharge to the CRF that the state pays and (2) additional surcharges for any administrative services provided to the local government that is not provided to the state.
- **Budget Bill Reduces CRF Reserve.** In past budgets, Control Section 4.20 has specified that CalPERS would maintain a three-month reserve in the CRF. The proposed budget bill language for Control Section 4.20 directs CalPERS to maintain a one-month reserve in the CRF.

Background. CalPERS administers the health plans offered to active and retired employees of the state and about 1,200 local governments in California. CalPERS incurs costs to administer the health plans provided to its members. These costs include personnel costs (CalPERS employees are state employees), costs to contract with consultants and professional services, and other operating expenses.

Current law allows these administrative expenses to be paid through two funds - the Public Employees' Contingency Reserve Fund (CRF) and the Public Employees' Health Care Fund (HCF) - so long as the costs are approved in the annual budget act.

The CRF was established in 1962 as a means to pay for administrative costs across the CalPERS healthcare program. Employers pay for administrative costs through a surcharge on health premiums. The HCF was established in 1988 to fund CalPERS "self-funded" plans, such as Preferred Provider Organization (PPOs). Contributions to the HCF are built into these plans' premiums.

Control Section 4.20. Control Section 4.20 of the annual budget act establishes the surcharge levied on the state to fund the CRF pursuant to Section 22885 of the Government Code. In 2016-17, this surcharge was established as 0.31 percent of gross health premiums paid by the employer. Section 22901 of the Government Code requires local governments that contract with CalPERS for health benefits to pay the same surcharge as the state to fund the CRF.

In addition, the Legislative Analyst's Office notes that Section 22901 gives the CalPERS board the authority to require contracting local governments to pay an additional amount so that the local government pays an amount sufficient to bear all of the administrative costs incurred by the

board in providing health benefits to the local government's active and retired employees. In most years, and currently, CalPERS indicates that it provides the state and contracting local governments the same administrative services. CalPERS typically charges state and local government employers the same surcharge to fund the CRF. In at least one instance, CalPERS has charged local governments an additional surcharge to pay for services not provided to the state.

In 2006-07, CalPERS charged contracting local governments an additional surcharge of 0.17 percent of premiums to pay for services related to a new accounting reporting requirement (GASB 45). CalPERS did not provide this service for the state because the State Controller's Office was given this responsibility. Whereas CalPERS charged the state a surcharge of 0.27 percent of premiums in 2006-07, it charged contracting local agencies 0.44 percent of premiums.

The Administration disagrees with the LAO's interpretation and states that there is ambiguity in current law to allow for local governments to be charged an additional surcharge, however there is precedence from CalPERS to charge an additional surcharge. It is unclear how the Administration's proposal would impact local governments.

Administrative Costs Have Grown. Administrative costs paid from the HCF and the CRF nearly doubled between 2006-07 and 2016-17. The 2017-18 budget assumes these costs will be about \$70 million, less than 1 percent of the total cost of CalPERS' health benefits program. DOF states that the CalPERS health benefits program's administrative costs have grown over the past decade primarily due to an increase in the number of health benefit plans containing a self-funded component. The growing number of health plans with a self-funded component - and membership in those plans - resulted in administrative costs paid from the HCF to increase much faster than costs paid from the CRF.

2016-17 Budget Act Action. Although the CRF always has been included in the budget, increased costs from the HCF historically were not considered in the state budget. In light of the rapid growth in costs paid from the HCF in recent years, the Legislature approved statutory changes as part of the 2016-17 budget package to require administrative expenses from the HCF be approved by the Legislature in the annual budget. Additionally, the 2016-17 Budget Act included provisional language directing DOF to complete a zero-based budget exercise in developing the 2017-18 budget. DOF's zero-based review was specifically directed to include (but not be limited to) the evaluation of program objectives, workload metrics, cost allocation methodologies, reserve levels, personnel services, and operating expenses and equipment.

Zero Based Budget Results. DOF provided staff with a one-page summary that included four bullets identifying DOF's conclusions from its zero-based budget exercise. DOF found that the CalPERS health benefits program is resourced adequately to carry out its statutory workload and requirements. Additionally, in meetings with staff, DOF has indicated that there has not been a gross misuse of funds. The Administration did not identify functions within the health benefits program that is not funded at an appropriate level. Out of five bullets listed in the administration's recommendations, two would require legislative actions, which are to reduce the reserve for administrative expenses from 3 months to one month, and to consolidate administrative revenues and expenditures into a single fund. The other bullets indicate that DOF will continue working with CalPERS on workload metrics, information technology project processes, and administrative efficiencies.

Staff Comments

Last year, the Legislature included additional transparency to the HCF by bringing the fund under the budget, thereby providing for Legislative review. This change only has been in place for seven months and was part of the budget package agreed to last year by the DOF and Legislature. It is unclear why a statutory change beyond the action taken last year is necessary. Additionally, it is unclear why the Administration is proposing to reduce the reserve from 3 months to 1 month, and how this would impact CalPERS operations.

Staff Recommendation. Hold open.