Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Richard Roth, Chair
Senator Norma Torres
Senator Tom Berryhill

Thursday, April 3, 2013
9:30 AM or Upon Adjournment of Session
Rose Ann Vuich Hearing Room 2040

Consultant: **Brady Van Engelen**

Item Number and Title

0840	State Controller
0845	Department of Insurance
0890	Secretary of State
7502	Department of Technology
8880	Financial Information System for California (FI$Cal)

(See Table of Contents on pages 1 and 2 for a More Specific Listing of Issues)

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AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Page 4)

AGENDA – DISCUSSION / VOTE ITEMS

Issues Proposed for Vote Only:

	Issue	2014-15 Amount	Fund Source	Staff Recommendation
	Secretary of State(0890)			
1	Legislative Workload Adjustments	$79,000	General Fund	APPROVE
	Department of Technology (7502)			
1	Capacity BCP's	$35.878 million	Technology Services Revolving Fund	APPROVE
2	Prior Year Adjustments	-$26.849 million (2013-14 reduction is -$25.791)	Technology Services Revolving Fund	APPROVE

Vote:

Issues Proposed for Vote Only – Issue Descriptions

Secretary of State

Issue 1 – Legislative Workload Adjustments

Governor's Budget Request: The Secretary of State requests $79,000 (General Fund) and one permanent Management Services Technician to implement the provisions of AB 849 (Garcia), Chapter 676, Statutes of 2013.

Background: AB 849 allows elderly/dependent adult victims of domestic violence, sexual assault, or stalking to apply to the Secretary of State's California Address Confidentiality Program (Safe at Home). AB 849 also requires that the Secretary of State identify, recruit, and train state, local, and non-profit agencies that specialize in the needs of the elderly/dependent adult population and designate them as enrolling agencies for the Safe at Home program.

Staff Comment: Staff has no concerns or issues with this request.

Staff Recommendation: Approve as budgeted.

Vote:

Department of Technology

Issue 1 – Capacity Budget Change Proposals

Governor's Budget Request: The Department of Technology is requesting a total of $35.878 million (Technology Services Revolving Fund) to address capacity increases in the customer service areas of the Vacaville and Gold Camp Data Centers. The requested amount for each service provided is listed below:

Request Number	Service Area	BCP Amount
1	Mainframe CPU Capacity	$7,629,000
2	Midrange Server Capacity	$14,284,000
3	Enterprise Data Storage	$8,810,000
4	Network Capacity	$5,155,000
	TOTAL	**$35,878,000**

1) **Mainframe CPU Processing Capacity ($7.629 million)** - The Governor's 2014-15 budget includes a proposal to increase expenditure authority by $7.629 million (Technology Services Revolving Fund) in FY 2014-15 to allow the Office of Technology Services (OTech) to purchase 1,930 millions of instructions per second (MIPS) of mainframe processing capacity to meet projected customer needs.

   The Office of Technology currently has over 500 customers of which, approximately 250 are mainframe processing customers, and many are still adding new applications, building new databases, and using WebSphere to add Web interfaces to their legacy applications. Mainframe computing demand is projected to increase by 11.3 percent in 2013-14.

2) **Midrange Server Capacity ($14.284 million)** - The Governor's 2014-15 budget requests increased expenditure authority of $14.284 million (Technology Services Revolving Fund). The request stems from the OTech need for additional hardware, operating system software, applications software, statewide E-mail, and database software to ensure adequate midrange service capacity to meet the needs of customer-driven workloads. This request also includes resources to meet the disaster recovery requirements of customers.

   There is an increased demand on services by customer departments at a variety of state entities. This increased demand, largely stemming from increased population and use of services, results in the growth of customer applications and the need for additional server capacity. OTech continues to experience a substantial increase in the midrange computing workload, database instances, Disaster Recovery, and web services.

3) **Enterprise Data Storage ($8.810 million)** - The Governor's 2014-15 budget includes a request to increase the spending authority of the Department of Technology by $8.810 million (Technology Services Revolving Fund) in FY 2014-15 for hardware, software, and connectivity components to ensure adequate data storage support to meet the needs from customer-driven workloads, approved information technology (IT) projects, and disaster recovery.

   While providing for the increasing needs of current customers, the OTech must provide resources for approved IT projects supported by the Department of Technology. In order to achieve both normal growth and approved IT projects, OTech must increase the number and density of virtual servers in preparation of departments growing or migrating over to the Office of Technology. Virtual servers require large amounts of data storage to support their efficient and effective use of IT resources and data processing. Increased IT density allows OTech to support the migration of IT workload from other agencies. In addition, OTech must provide for customers with disaster recovery data storage requirements that are currently located at OTech or relaying them to their data center.

4) **Network Capacity ($5.155 million)** - The Governor's 2014-15 budget includes a request to increase the spending authority of the Technology Agency by $5.155 million (Technology Services Revolving Fund) in FY 2014-15 to purchase switches, circuits, load balancers, firewalls, and maintenance services.

   OTech currently manages two data centers located in Vacaville and Rancho Cordova, and is responsible for the network infrastructure needs of the data centers that provide network services connecting their data center facilities to most of the executive branch departments and local agencies.

Staff Comment: Staff has no concerns or issues with this request.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 2 – Prior Year Adjustments

Governor's Budget Request: The Department of Technology is requesting a technical adjustment to align previously approved budget actions with ongoing costs related to prior year capacity budget requests. The adjustment amounts to a net reduction of $25.791 million in 2013-14 and a net reduction of $26.849 million in 2014-15.

Background: These technical adjustments are a result of one-time reductions, project cost reductions due to favorable contracts, and/or project completions. The initial budget request is determined in advance of the service or product being acquired and the actual cost may vary by the time the expense is incurred. The intent of the request is to better align the Department of Technology's budget with actual expenditures for prior year requests.

Staff Comment: Staff has no concerns or issues with this request.

Staff Recommendation: Approve as budgeted.

Vote:

Issues Proposed for Discussion / Vote

0840 STATE CONTROLLER

Department Overview: The State Controller (SCO) is the Chief Fiscal Officer of California. The Controller provides fiscal control for, and independent oversight of, more than $100 billion in receipts and disbursements of public funds. In addition, the Controller offers fiscal guidance to local governments, and performs audit functions to uncover fraud and abuse of taxpayer dollars. The SCO's primary objectives are to:

- Account for and control disbursement of state funds.
- Determine legality and accuracy of issue warrants in payment of the State's bills.
- Claims against the state.
- Administer the Uniform State Payroll System.
- Audit and process personnel and payroll transactions for state civil service, exempt employees, and state university and college system employees.
- Audit state and local government programs.
- Inform the public of the State's financial condition.
- Administer the unclaimed property law.
- Inform the public of financial transactions of city, county, and district governments.

The SCO is funded through the General Fund, as well as over 300 special funds and accounts and reimbursements. The Governor's budget requests $188.85 million ($48.99 million General Fund) and 1,392.1 personnel years to support the SCO.

2014-15 State Controller's Budget
(Dollars in millions)

FUND SOURCE	2012-13	2013-14	2014-15
General Fund	$45.69	$54.81	$48.99
Unclaimed Property Fund	$31.30	$33.56	$36.14
Central Service Cost Recovery Fund	$20.10	$24.16	$23.14
Other Special Funds and Accounts	$29.01	$15.73	$15.5
Reimbursements	$52.57	$64.56	$64.08
Total Expenditures	$178.67	$192.82	$188.85
Personnel Years	1,297.4	1,398.3	1,392.1

Issue 1 – 21st Century Project

Governor's Budget Request: The SCO requests 5.0 positions and $6.529 million ($3.59 million General Fund, $1.265 million Reimbursement Authority, and $1.674 million Special Fund) for FY 2014-15 to support ongoing legal costs. The SCO has requested that budget bill Llanguage and Control Section language be added to the 2014 Budget Act. This request also includes trailer bill language that would extend the sunset date of the 21st Century Project until June 30, 2017.

Background: The SCO is responsible for disbursement of pay to the state's 275,000 employees. In 2004, the Department of Finance (DOF) approved the justification documents submitted by the SCO requesting an updated payroll system that would provide a greater level of integration. The SCO procured Commercial Off-the-Shelf (COTS) software in 2005 and intended on utilizing that COTS software to update the state's payroll system.

The Department of General Services (DGS) awarded the second contract to a different vendor, SAP, on February 2, 2010. An updated Special Project Report (SPR 4), that was issued prior to the contract being awarded, identified the method that would eventually be utilized to implement the new MyCalPAYS system. The first, and smallest phase, would consist of converting payroll for the approximately 1,300 SCO staff to the new payroll system.

The initial pilot was deployed in June of 2012 and revealed a significant volume of errors. The SCO issued a cure letter in October of 2012 to SAP, requesting that the vendor deliver the resources necessary to correct the identified errors. SCO was not satisfied with the response and subsequently terminated the contract with SAP in February 2013. Due to the contract being terminated, the Technology Agency had little choice but to suspend the 21st Century Project.

In June 2013, the SCO and SAP participated in contractual mediation. The mediation process did not provide an acceptable outcome and, on November 21, 2013, the SCO filed a lawsuit against SAP for breach of contract. The 2013 Budget Act provided the SCO with $1.0 million for legal support, which is set to expire on June 30, 2014. According to SCO, the state has the potential to recoup 1.5 times the contract amount, or up to $150 million. Alternatively, SAP could be awarded $50 million.

Request Detail:
A more specific cost breakdown of the SCO's request for $6.529 million to support ongoing legal costs is provided below:

- $645,000 for 5.0 one-year limited-term positions these positions will be responsible for pertinent document retrieval, developing a project history and timeline, and maintenance of the MyCalPays system in support of the legal team.

- $996,000 for the project management advisory contract. The project advisors, Flagship Advisors is comprised of two people and provides assistance with business processes, integration, coordination, configuration, customization, testing, training, installation, data conversion, and work force transition.

- $2.5 million for legal counsel to defend the state against claims made by SAP. This request may only reflect a portion of total legal costs; the SCO has requested that provisional language be included to provide additional funding for legal costs, if necessary.

- $904,000 for costs associated with leasing a facility.

- $1.193 million for costs associated with IT services from the Department of Technology. These services include infrastructure support and data center storage support.

- $266,000 for data center services that will support the maintenance of the software purchases that are a component of the 21st Century Project.

As noted earlier, there are multiple components to this request, and it may be best to consider each component individually:

Proposed Trailer Bill Language - Government Code §12432 authorized the State Controller, beginning in FY 2006-07, to assess special funds within the state treasury for costs attributable to the replacement of the state payroll disbursement system. This replacement effort has been referred to as the 21st Century Project. This code section also notes that costs assessed to the 21st Century Project will be evenly split between the General Fund and special funds within the state treasury.

The provisions included in this section were set to expire on June 30, 2011. AB 119 (Blumenfield), Chapter 31, Statutes of 2011, extended the original sunset date by three calendar years, moving it to June 30, 2014. The requested amendment would once again extend the sunset date. The provisions included in Government Code Section §12432 would not expire until June 30, 2017.

Staff Comment: This requested trailer bill language would extend the current authority for assessments on special funds within the state treasury for costs related to the implementation of the 21st Century Project for an additional three years.

Requesting spending authority for a currently suspended IT project raises some concern for staff. The SCO has yet to publish an independent assessment on the lessons learned from the previous efforts related to the 21st Century Project. Yet, SCO is requesting funds and statutory authority for the continuation of the project, Beyond the legal case before SCO, staff is uncertain what the 21st Century project staff are proposing to accomplish given we do not know what remains salvageable from prior implementation efforts.

Requested positions and funding - Another component to this request is the SCO's request for 5.0 positions and $6.529 million ($3.59 million General Fund, $1.265 million Reimbursement Authority, and $1.674 million Special Fund) for FY 2014-15 to support ongoing legal costs. The requested positions would largely support the SCO's efforts in response to public records and discovery. The positions would also provide technical assistance to the legal team as needed. As noted earlier, costs attributed directly to SCO staff will total $645,000 for FY 2014-15, the remainder of the requested funds will be utilized for a variety of purposes including: legal support, data center services, capital facility costs, software maintenance costs, and payment to external consultants.

Staff Comment: Staff recognizes the need to support SCO's legal costs associated with this request. It is important to note that the requested positions and funding support sustainment of the current suspension of the 21st Century Project, not a progression towards a new automated payroll disbursement system. However, the request includes funding for Flagship Advisors which has provided the SCO with project management support for over four years, beginning in February 2010. After this amount of time, there should be an adequate level of knowledge transferred between the consultant and the project team. To further reduce costs associated with the 21st Century Project, while in its current suspended status, the Legislature may wish to consider eliminating funding for the external consultant contract. The requested five one-year limited-term positions contain a high-level of expertise that can adequately support the SCO's legal efforts. Also, it is unclear how many staff from the external consultant, Flagship Advisors, would be made available to support SCO's efforts.

<u>Provisional Budget Bill Language:</u> The SCO has requested that language be added to the budget act that authorizes additional expenditures for legal costs. The provisional items, under 0840-001-0001 and Control Section 25.25, would allow for further augmentation from all fund sources to fund litigation and related support efforts associated with the 21st Century Project.

Staff Comment: For historical purposes, staff concurs that costs associated with the 21st Century Project should be included under the SCO's annual budget bill item, and the control section associated with the SCO, 0840-001-0001 and control section 25.25. Staff does not have any issues with this portion of the proposal.

LAO Comment: The LAO recently published a review of the SCO's request. In their briefing the LAO noted several items:

***Legal costs are likely to exceed currently requested amount**.* The LAO noted that it is likely that this request has under-budgeted legal costs associated with the 21st Century Project. The SCO has estimated that legal costs from outside counsel will total between $4.5 million and $5 million for FY 2014-15. The SCO derived that estimate from monthly totals from September 2013, to date.

Lacking a project assessment. During consideration of the FY 2013-14 budget, the LAO proposed the SCO conduct an assessment on the 21st Century Project to determine a number of different items: the viability of the current software platform, whether or not the state's payroll process needed to be modified prior to the re-start of the project, lessons learned, and to present an analysis of alternatives.

LAO Recommendations: The LAO also made several recommendations associated with this request that the Legislature may wish to consider including:

1. Budgeting estimated costs for SCO's legal effort.
2. The Legislature should appropriate additional funds so the SCO, in consultation with the Department of Technology can provide an assessment.
3. Initiate a review of the performance of the Department of Technology concerning its oversight role, how its policies applied to the 21st Century Project, and impediments, either statutory or otherwise, that limit their ability to exercise oversight of IT projects.

Staff Recommendation: Hold open.

Vote:

Issue 2 – Software Cost Increases

Governor's Budget Request: The SCO requests $3.482 million ($797,000 General Fund, $1.692 million reimbursements and $993,000 Special Fund) in 2014-15 through 2017-18, to continue funding a contract with Integrated Data Management System (IDMS) technology services.

Background: The IDMS is comprised of a suite of software products that run on the mainframe housed at the Office of Technology Services. The systems are wholly integrated and allow for direct interface and/or provide for files to be passed between each unique system. The Controller's Office is highly dependent on IDMS applications, and uses the business functions for personnel, payroll, fiscal, and audits. There are a total of fifteen unique IDMS supported applications that the SCO utilizes.

In FY 2012-13, SCO paid $1.25 million for IDMS services. Costs have increased because the SCO is now one of only two state entities (California Highway Patrol is the other) that utilize IDMS applications and, therefore, are paying for a much higher share of the costs than before, when the costs could be distributed across multiple agencies. The Department of Technology recently negotiated a five-year contract with Computer Associates so SCO can utilize their services and their IDMS software until March 31, 2018.

Staff Comment: If the other user of IDMS, the California Highway Patrol, were to leave, costs would increase to $4.6 million annually. Given the high number of legacy systems utilized by the SCO, it is unlikely that a more cost-effective alternative can be acquired and integrated before the expiration of the contract. Additionally, some of the functions incorporated into the 21st Century Project would have replaced the need for IDMS. The suspension of the 21st Century Project, coupled with the additional year added to the project timeline for the Financial Information System for California (FI$Cal) project highlights SCO's need and reliance on IDMS.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 3 – MyCalPers

Governor's Budget Request: The SCO requests 15.0 five-year limited-term positions and $1.356 million ($759,000 General Fund and $597,000 Special Fund) from 2014-15 through 2018-19 to address the increased workload generated by the implementation of the California Public Employees Retirement System (CalPERS) Pension System Resumption (PSR) Project.

Background: The MyCalPERS system, which CalPERS migrated to in order to consolidate forty-nine various information systems within CalPERS' internal network, was intended to provide employers a streamlined, self-service environment for completing retirement and health business transactions. The SCO and CalPERS interface regularly on the SCO's Uniform State Payroll System and CalPERS' retirement system. The interfaces are complex and large, handling the information of over 274,673 active members.

In March 2009, CalPERS informed the SCO that employers would be responsible for the correcting and reporting of all discrepancies between SCO's Uniform State Payroll System and the new CalPERS system, a function that historically was performed by CalPERS staff. In 2011, CalPERS shared its test results of the MyCalPERS system with SCO staff, and SCO prepared to address the higher than originally expected level of errors by redirecting staff from its retirement unit. In 2012, the Legislature authorized seven limited-term positions to address the growing backlog of errors created due to the interface of the MyCalPERS system with the SCO's Uniform State Payroll System.

The SCO anticipates that the number of outstanding errors at the end of FY 2013-14 will be 316,636. SCO staff estimate that, under the current conditions, 17.8 PYs would be required to address the backlog of errors by FY 2018-19. However, the SCO contends that an automated fix to the errors occurring in the current Uniform State Payroll System will further reduce the error reporting rate. SCO staff will need to modify their current system in order to achieve a greater level of compatibility with the CalPERS system, and then will proceed with identifying a solution for files that have already been transmitted to the CalPERS system. If the SCO is successful in modifying their reporting process, and modifying their previously reported data, the total error rate will drop significantly. Recognizing this, the DOF has requested that provisional language be included that will provide the DOF with the authority to reduce the amounts authorized to the SCO if the transition is successful. The proposed provisional language is below:

> "*The Department of Finance may reduce the amounts authorized under Item 0840-001-0001 of this act, upon successful completion of a system change that significantly reduces the number of error records, and in turn, the SCO workload related to the CalPERS PSR System Resumption. This adjustment shall be in coordination with the SCO and CalPERS. No adjustments shall be made pursuant to this provision prior to a 30-day notification in writing to the Chairperson of the Joint Legislative Budget Committee and the chairpersons of the committee of each house of the Legislature that consider appropriations.*"

Staff Comment: The requested resources will help address the backlog of errors between the Uniform State Payroll System and the provisional language would allow for a reduction in funding if necessary.

Staff Recommendation: Approve as budgeted and adopt provisional budget bill language.

Vote:

Issue 4 – Sustained Accounting and Reporting Workload

Governor's Budget Request: The SCO requests the continuation of 2.1 two-year limited-term positions and $217,000 ($122,000 General Fund and $95,000 Central Service Cost Recovery Fund) in 2014-15 and 2015-16 to address the statewide cash management workload.

Background: The SCO is responsible for the fiscal control of over $100 billion in annual receipts and disbursements of public funds. Within the SCO, the Division of Accounting and Reporting (DAR) is responsible for statewide cash management activities, which include:

- Accounting and controlling the disbursement of all state funds.
- Determining the legality and accuracy of every claim against the state.
- Issuing warrants in payment of the state's bills including lottery prizes.
- Informing the public of the state's financial condition.

There are currently six full-time staff that provide state-wide cash management support at the SCO. The 2012 Budget Act provided SCO with two, two-year limited-term staff to support cash management activities for SCO staff. This request is a continuation of these positions. The requested positions are already filled, and the staff have been trained by the SCO to perform cash management-related activities.

Staff Comment: The SCO's calculations project workload hours to total approximately 14,540 for FY 2014-15. If the average PY were to work approximately 1,775 hours annually, DAR would need 8.19 staff to address the workload; this is in line with the requested position total. Given that the current cash-flow situation is not as dire as it was in FY 2011-12, when the positions were originally authorized by the Legislature, approving the positions on a limited-term basis, as proposed in this BCP, is reasonable.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 5 – Unclaimed Property: Fraudulent Claims Protection and Prevention

Governor's Budget Request: The SCO requests 16 two-year limited-term positions and $2.095 million (Unclaimed Property Fund) for FY 2014-15 and $2.082 million in FY 2015-16 to detect and prevent fraudulent unclaimed property claims.

Background: Under current law, the SCO is responsible for safeguarding unclaimed property until it is returned to the lawful owner. The Unclaimed Property Division (UPD) of the SCO reunites owners with their lost or abandoned property when the owner files a paper claim following a search for property on the SCO's website or after calling the Unclaimed Property Division call center to request a claim form. A claim may be filed by either the owner or the heir of the owner as reported by the holder.

Staff Comment: A similar request was submitted during consideration of the FY 2012-13 Budget. At that time the number of claims filed over the previous four years, ranged from two in 2007-08 to 1,017 in 2010-11. Given the wide variation in claims, staff recommended the 17.9 requested positions be provided on a limited-term basis.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 6 – Unclaimed Property: Insurance Workload

Governor's Budget Request: The SCO requests 11.0 permanent positions and $1.117 million from the Unclaimed Property Fund in FY 2014-15, and ongoing, to address life insurance companies' compliance with state unclaimed property regulations.

Background: Under current law, the SCO is responsible for safeguarding unclaimed property until it is returned to the lawful owner. In most cases, after three years, the property is transferred to the state. There are a variety of ways for property owners to be notified of property being held. Recently, legislative and administrative changes have increased workload in the areas of financial accountability and corporate actions, and the collection of securities. According to the SCO's, the goal of this program is to expedite the return of the property to owners by increasing the ability of the SCO to preserve the integrity of the ownership trail.

Recent audits conducted by the SCO have found that insurance companies often fail to pay death beneficiaries on their life insurance policy. Instead, companies draw-down the policies' cash reserves in order to continue collecting premium payments from the deceased policy holder. Once the cash reserves are depleted, the companies cancel the policy. Owners of such benefits, and the SCO, are often not notified. Since notice has not been given and the SCO does not have the property on file, the property is seldom conveyed to the lawful owner.

Staff Comment: The 2012 Budget Act authorized a similar request; providing the Unclaimed Property Division with 13.0 three-year limited-term positions and $1.303 million in Unclaimed Property authority for FY 2012-13 and $1.115 million in FY 2013-14. As of June 2013, the policyholders, heirs, or beneficiaries of property valued at $45.6 million have been located and paid.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 7 – Unclaimed Property: Holder Compliance

Governor's Budget Request: The SCO requests 23.0 permanent positions and $2.475 million from the Unclaimed Property Fund in 2014-15, and ongoing. The requested funds and positions will support the SCO's holder compliance program on a permanent basis.

Background: Banks and other institutions are required by law to remit unclaimed property to the state. The unclaimed property law states that after a property has remained inactive for three years, and holder efforts to reconnect the property with its owner have not proven successful, the property may be considered unclaimed. The most common types of property remitted to the state are bank accounts, safe deposit box contents, insurance policy proceeds, and stocks.

The SCO regularly conducts audits of banks, and other institutions that may hold property, to determine if unclaimed property is being safeguarded and used in accordance to the State's unclaimed property law. The SCO performs these audits through direct contact with businesses, hospitals, banks, retailers, utility companies, and major financial institutions; essentially any business entity that could be holding unclaimed property. The SCO also contracts with third-party vendors for review of out-of-state holders of unclaimed property.

When properties with cash value are remitted to the state they are deposited into the Unclaimed Property Fund. The state regularly sweeps the Unclaimed Property Fund, typically when the fund balance exceeds $50,000, into the General Fund. In FY 2012-13, these sweeps provided the General Fund with approximately $473 million in revenue.

LAO Recommendation: The LAO previously found that property holder outreach and compliance would result $5.5 million of property per year returned to its owners, and $4.1 million of property per year would be remitted to the SCO. However, the audits have resulted in about $2.3 million of property returned to owners and $4.1 million remitted to the SCO. The LAO has observed that the SCO's holder compliance initiative has remitted more property than originally projected to the SCO, but the results have varied from the earlier projections. The LAO would recommend that the positions be provided on a two-year limited-term basis and that the Legislature continue to monitor outcomes related to this effort.

Staff Recommendation: Approve budget change proposal on a two-year limited-term basis.

Vote:

Issue 8 – Unclaimed Property: Budget Bill Language

Governor's Budget Request: The Governor's May Revise includes a request to revise the existing provisional language for Item 0840-001-0970 to better define the expenditures paid from that account.

Background: Administration of the Unclaimed Property Program is a responsibility of the SCO, pursuant to the Code of Civil Procedure § 1300-1615. The Code of Civil Procedure provides the SCO with a continuous appropriation to carry out and enforce the Unclaimed Property Law. In addition to the continuous appropriation currently in statute, there is an item in the budget bill that provides the SCO with an appropriation for $36.1 million for the administration of the Unclaimed Property Program, as it relates to the administration of the program. The proposed budget bill language is below:

Provisional language for Item 0840-001-0970

> *The funding provided in Item 0840-001-0970 shall cover costs for personal services and related operating expenses and equipment (including legal costs that are not related to enforcing the recovery of property, and system related costs) for the Unclaimed Property Program. Continuous appropriations from the Unclaimed Fund are allowed for other program costs authorized under Section 1584(b) and Section 1325 of the Code of Civil Procedure. These continuous appropriations shall not be used to cover spending authorized under Item 0840-001-0970.*

Staff Comment: This request does not augment the overall amount of any funds, including the Unclaimed Property Fund, for use by the SCO.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 9 – Unclaimed Property: Assessments

Governor's Budget Request: The State Controller's Office requests three permanent positions to process assessments of fees when holders of unclaimed property do not remit escheated funds to the state in accordance with the unclaimed property law.

Background: The state's unclaimed property law, specifically Code Sections 1532 and 1577 of the Code of Civil Procedure (CCP), requires that holders report unclaimed cash exceeding $20,000 and those that fail to report will be assessed at a twelve percent interest to the date that the claim should have been reported. In 2008, the SCO's unclaimed property division successfully integrated a new system designed to track holder reporting and remitting activities associated with these assessments. However, no permanent staff was provided in conjunction with the implementation of the new system and the workload associated with supporting the SCO's efforts with these assessments was supported by student assistants.

Staff Comment: This workload was previously performed by hiring student assistants at a cost of $233,000. The workload that was previously performed by student assistants will now be performed by permanent staff.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 10 – Unclaimed Property: Securities Workload

Governor's Budget Request: The State Controller's Office requests 23.1 three-year limited-term positions and $1.999 million from the Unclaimed Property Fund to manage the securities portfolio in accordance with statute.

Background: The state's unclaimed property laws dictate that corporations, businesses, associations, financial institutions, and insurance companies annually report and deliver property to the SCO after there has been no activity on the account or no contact with the rightful owner for a period of time, which is generally three years. The SCO's unclaimed property division is responsible for the return of unclaimed property to its rightful owner. The unclaimed property division is statutorily required to provide a response to claimants within 180 days. The claims are usually either in the form of cash or securities. When a claim contains securities, the SCO is responsible for assessing the value of the claim. The requested positions will support the Unclaimed Property Division's sale of securities, claims on securities, and provide administrative support to the Unclaimed Property Division. The support total for each office is provided below:

19 positions for Security sales - Section 1563(b) of the Code of Civil Procedure directs the State Controller to sell unclaimed securities no sooner than 18 months, but not later than 20 months, after the final date that the securities were reported to the SCO. The requested positions will support the SCO's efforts to address corporate actions related to a security claim that must be taken prior to the security being sold and address a growing backlog of corporate actions that must be taken. The SCO estimates that, as of June 2013, 3,946 different security actions representing shares valuing approximately $40 million have been in SCO's portfolio longer than twenty months. There are currently five filled positions within this office.

2.5 positions for Security claims – As noted above, the SCO's Unclaimed Property Division receives more security claims than they have the capacity to process on an annual basis. The requested positions will support the SCO's efforts to reduce the growing inventory, and also provide a more timely response to claimants. The SCO anticipates that with the added positions the Unclaimed Property Division will be capable of providing a response to a security claim within a three month timeframe after approval. There are currently eleven full-time positions within this office.

1.6 Administrative Support Positions – The administrative support position will assist the Unclaimed Property Division in developing duty statements, records tracking, and records maintenance. There are currently eight full-time positions within the Unclaimed Property Division's administrative support unit.

Staff Comment: Sale proceeds of securities are swept to the General Fund until a claim is filed by the rightful owner, at which time, the SCO provides the securities claim in the form of cash proceeds. The SCO anticipates security sales proceeds to total $69.5 million for FY 2013-14.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 11 – Local Government Oversight

Governor's Budget Request: The State Controller's Office requests $1.159 million in reimbursement authority to support 9.0 three-year limited-term positions in order to provide oversight of local government entities.

Background: Generally, state oversight of local governments is limited to state and federal assistance provided to administer statewide programs. However, that oversight is often limited to urban counties and local governments that utilize a larger proportion of state and federal funding. While there are codified requirements that local governments must follow, there have been several instances of misuse including: unallowable taxes being imposed on property owned by residents and businesses, local defaults which can impact the state's overall credit rating, and misusing state and/or federal funds to offset local district General Fund expenditures. In addition, current statute provides for a more indirect oversight of local government funding using the following three elements:

1) **Annual Audits.** Each local government entity is required to have an annual audit performed by an independent auditor. If the local government has over $500,000 in federal expenditures, it must also have a single audit. Local governments are required to submit these audits to the SCO. The SCO can initiate a quality control review of the work papers of any auditor when there is suspicion that the work performed is inadequate.

2) **Financial Transaction Reports.** Statute requires the SCO to collect a report of annual financial transactions from each county, city, and special district and to publish them in reports available to the Governor, legislature, and general public. Statute further provides that, if the reports are not made in the time, form, and manner required, or if there is reason to believe a report is false, incomplete, or incorrect, the SCO shall appoint a qualified accountant to make an investigation and to obtain the information required. Statute specifies that the SCO's enforcement costs are to be reimbursed by the local government entity in question. Financial Transaction Reports represent the primary source of information on statewide data as it relates to local government expenditures.

3) **Accounting and Audit Guidelines.** Uniform accounting guidelines are intended to provide local governments with the information necessary to implement and operate a common 34 accounting and reporting system. Currently, such guidelines are only required for counties and special districts.

Staff Comment: This request represents a partial continuation of a request approved in the 2011 Budget Act, which provided the SCO with 16.4 three-year limited-term positions to conduct audit oversight of local entities. At this time, the SCO anticipates it only needs 9.0 positions to complete workload.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 12 – Statewide Training for Departmental Personnel and Payroll Staff

Governor's Budget Request: The SCO requests four two-year limited-term positions and $390,000 ($218,000 General Fund and $172,000 in special funds) in 2014-15 to meet statewide demand for payroll, personnel, and disability training programs for human resources staff.

Background: The statewide training unit (STU), within the SCO, that is responsible for providing personnel and payroll training to human resources staff in all civil service departments to ensure they are capable of utilizing the SCO's Uniform State Payroll System.

Demand for on-site training has far exceeded STU's capacity to deliver. For calendar year 2013, the SCO estimates that this division will only be able to provide approximately 40 percent of the requested training classes. Historically, the SCO has been able to provide an average of 47 percent of requested training. The requested positions would provide SCO with the capacity to provide their historical average of 47 percent of requested training.

Staff Comment: The SCO anticipates that they will have the capacity in 2016 to provide some training through e-learning, an online classroom environment, which it believes will increase its capacity to meet 57 percent of the requested demand.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 13 – Legislative Reform Workload

Governor's Budget Request: The SCO requests 3.2 two-year limited-term positions and $328,000 ($184,000 General Fund and $144,000 Special Fund) to support workload associated with the California Public Employees' Pension Reform Act (PEPRA) and the Federal Patient Protection and Affordable Care Act (ACA).

Background: Changes to both state and federal law have impacted the workload of the SCO's personnel and payroll services division. PEPRA modified retirement contribution rates for nearly 80,000 state employees. The SCO is responsible for ensuring that personnel and payroll activities are current, and will be required to reflect the changes made by this law. PEPRA modified a number of other changes to the Public Employees' Retirement Law that will require that the SCO modify their business practices going forward.

The ACA will require a greater level of detail in reporting requirements to ensure that the state is compliant with federal regulations. The complexity of the ACA will require additional workload to ensure that all reporting requirements of the state are met, and that the state is compliant with its obligations as an employer. CalHR has estimated that the penalties for non-compliance could potentially reach $350-$450 million annually for the state.

Staff Comment: Staff has no concerns or issues with this request.

Staff Recommendation: Approve as budgeted.

Vote:

0845 DEPARTMENT OF INSURANCE

Department and Budget Overview. The California Department of Insurance (CDI) regulates the California insurance market and enforces the California Insurance Code, including conducting examinations and investigations of insurance companies and producers and responding to consumer inquiries. CDI reviews and approves insurance rates to enforce the statutory requirement that rates are not excessive or unfair. The CDI also administers the conservation and liquidation of insolvent and delinquent insurance companies and fights insurance fraud, in conjunction with local and state law enforcement agencies. The January budget provides the CDI with 1,349.3 authorized positions and $245.07 million (Insurance Fund, federal funds, and reimbursements).

Issue 1 – Office of the Patient Advocate

Governor's Budget Request: The Department of Insurance requests an increase of special fund authority of $163,000 in Fiscal Year 2014-15 and $150,000 in 2015-16 and 1.5 positions to support implementation activities of AB 922 (Monning), Chapter 552, Statutes of 2011.

Background: AB 922 transferred the Office of the Patient Advocate (OPA) from the Department of Managed Health Care to the California Health and Human Services Agency (CHHSA) in 2012 in order to provide assistance to individuals, including those served by health care service plans regulated by the Department of Managed Health Care and the California Department of Insurance (CDI). AB 922 also requires the CDI to do the following:

- Provide assistance to OPA to develop informational guides for consumers
- Receive complaints referred by OPA
- Develop reports related to health consumer complaints
- Receive and handle referrals from OPA regarding studies and investigations
- Provide transfers of money from the Insurance Fund as needed for OPA

In FY 2012-13, CDI's Consumer Services Division was responsible for handling over 10,000 health-related complaints and responding to over 14,000 health-related telephone calls. CDI projects that the number of written complaints for FY 2014-15 will remain at approximately 10,000 and the number of phone calls will increase to over 16,000.

Staff Comment: Senate Budget Subcommittee No. 3 is addressing the role of OPA, and whether its current functionality best meets the intent of AB 922. Staff would recommend holding this item open until a resolution has been reached regarding the status of OPA.

Staff Recommendation: Hold this item open.

Vote:

Issue 2 – Principle-Based Reserving

Governor's Budget Request: The Department of Insurance requests $491,000 (Insurance Fund) for 2014-15 and $463,000 for 2015-16 and four positions to address increased workload associated with changes made to the insurance reserving methodology, and budget bill language stipulating that resources are only available upon the adoption of revisions by the Legislature.

Background: The CDI is responsible for ensuring that companies that offer life insurance policies maintain their solvency through adequate reserves. Claims for life insurance are readily verifiable and often paid very quickly, as opposed to casualty claims which are paid out over a longer duration or after litigation. Solvency is determined by an actuarial model that has been utilized by the industry for well over a century.

A newer modeling methodology, Principle-Based Reserving (PBR), which estimates insurer liability for future insurance claims will eventually become the industry standard. PBR will be operative, and the standard for life insurance reserves after legislative adoption by a super-majority of U.S. jurisdictions representing at least 75 percent of total U.S. premiums. CDI has requested four permanent positions to address the workload associated with conducting PBR.

In addition to the requested funding and positions, the CDI has requested budget bill language be added. The requested language would stipulate that resources related to PBR actuarial methodology only be made available upon the adoption of revisions made by the Legislature to the National Association of Insurance Commissioners valuation manual.

Staff Comment: Staff has no concerns or issues with this request.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 3 – Health Care Coverage Market Reform

Governor's Budget Request: The CDI requests $1.01 million (Insurance Fund) in expenditure authority in 2014-15 to fund a total of 9.0 positions, to address the workload associated with ABX1 2 (Pan) Chapter 1, Statutes of 2013, which amended and added several statutes to the California Insurance Code in order to conform with federal guidelines established by the ACA.

Background: Consumers of health insurance fall into one of three categories: individuals, small groups/businesses, and large groups or businesses with more than 50 employees. The majority of the regulation conducted by the CDI is of health insurance companies that cover individuals or small group/businesses. It is estimated that this represents approximately 12 percent of the state's regulated health insurance population. The Department of Managed Health Care is responsible for the remaining portion.

ABX1 2, which conformed state regulations with federal healthcare guidelines, has created a more complex health insurance market, added 2.7 million new insured lives to the health insurance market, and increased the number of inquiries and complaints received by CDI's Consumer Services Division. According to CDI, the consumer services division anticipates an increase in the number of complaints received via telephone and in writing.

LAO Recommendation: The LAO recommends that the Legislature approve the seven positions to address an expected increase in the volume of health-related consumer complaints on a two-year limited-term basis. At this time, it is unclear how ACA implementation will (a) affect consumer complaints relative to past experience and (b) change the share of Californians enrolled in CDI-regulated individual market health insurance products relative to health insurance products regulated by DMHC. Approving these positions on a limited-term basis would allow the Legislature to reexamine the CDI's need for these seven positions, or a smaller or greater number, on a permanent basis in several years once the permanent impacts to CDI of federal health care reform are better understood.

Staff Comment: The CDI contends that recruiting and hiring the requested positions on a limited-term basis might be problematic. This issue merits further discussion.

Staff Recommendation: Hold this item open.

Vote:

Issue 4 – Accelerated Death Benefits – Life Insurance

Governor's Budget Request: The CDI requests an increase of $370,000 (Insurance Fund) in expenditure authority for FY 2014-15, and $312,000 in FY 2015-16 and ongoing to fund 3.0 positions to support the implementation of SB 281 (Calderon), Chapter 345, Statutes of 2013.

Background: Under prior law, accelerated death benefit provisions of a life insurance policy would accelerate the actual benefit upon the insured becoming chronically ill. The policy would be held to the same legal standards as applied to stand-alone long-term care policies, regardless if the insured was receiving long-term care or not. SB 281 modified the legal standards for accelerated death benefit provisions of life insurance policies. These policies allow policy owners to access death benefits when they experience a catastrophic or chronic illness.

The CDI anticipates that the changes made as part of SB 281 will increase the workload of the Department's Consumer Services Division (CSD) by approximately 600 workload hours for call center support, 2,520 workload hours for written cases, and 1,750 workload hours related to legal examination and correspondence.

Staff Comment: Staff has no concerns or issues with this request.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 5 – Electronic Notice Transmission

Governor's Budget Request: The CDI is requesting an increase in expenditure authority from the Insurance Fund of $773,000 in Fiscal Year 2014-15, $603,000 in FY 2015-16 and FY 2016-17, and 5.0 three-year limited-term positions to support the implementation of SB 251 (Calderon) Chapter 369, Statutes of 2013.

Background: SB 251 authorizes, until January 1, 2019, an insurer, with the consent of the policyholder, to transmit electronically, in lieu of mail, certain notices pertaining to workers' compensation insurance: the offer of renewal required for personal auto, real and personal property, and liability insurance policies; the notice of conditional renewal for commercial insurance policies; and the offer of renewal and certain disclosures related to earthquake insurance so long as the insurer complies with the specified provisions of the Uniform Electronic Transactions Act (UETA) and additional procedures and standards.

Additionally, SB 251 requires that the Insurance Commissioner submit a report, on or before January 1, 2018, to the Governor and specified committees of the Senate and Assembly regarding the impact and implementation of the authorization of the electronic transmission of certain insurance renewal offers, notices, or disclosures.

Staff Comment: Staff has no concerns or issues with this request.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 6 – Stop-Loss Insurance Coverage

Governor's Budget Request: The CDI requests a one-time augmentation of $76,000 from the Insurance Fund to comply with provisions of SB 161 (Hernandez) Chapter 443, Statutes of 2013.

Background: SB 161 established regulatory requirements for stop-loss insurance for small employers, including on or after January 1, 2016, setting an individual attachment point of $40,000 or greater and an aggregate attachment point of the greater of $5,000 times the total number of group members, 120 percent of expected claims, or $40,000.

Staff Comment: Staff has no concerns or issues with this request.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 7 – Community Development Financial Institution Investments

Governor's Budget Request: The CDI requests an increase of $555,000 in expenditure authority from the Insurance Fund in Fiscal Year 2014-15, and an increase of $522,000 for FY 2015-16 and FY 2016-17, to fund five three-year limited-term positions to support the implementation of AB 32 (Perez), Chapter 608, Statutes of 2013.

Background: The California Organized Investment Network (COIN) program was created in 1996 as a public-private partnership by the CDI, the insurance industry, state government leaders, and community development organizations with the goal of helping to address the unmet capital needs for economic development and affordable housing in low-income urban and rural communities throughout California. The COIN program serves as a liaison between insurers that are seeking investment opportunities and the community organizations that are seeking investment capital for projects. Community Development Financial Institutions (CDFIs) work with COIN - an office within the California Department of Insurance - as financial intermediaries providing access to credit, loans, and investments to small businesses and non-profits that serve economically disadvantaged communities. CDFIs also offer administrative and technical assistance in these low-income communities. Generally, CDFIs lend to borrowers that do not satisfy the criteria for conventional lenders and focus on a particular community or certain groups of people.

In 1997, the COIN CDFI Tax Credit program was created to attract and leverage private capital to fund investments into CDFIs that yield economic and social benefits for California's underserved markets, as well as investments that yield environmental benefits. The program was set to expire at the end of 2011, but was extended until January 1, 2017 by AB 32. The goal of the CDFI tax credit program is to provide incentives to attract private capital investments that otherwise may not be available. The statewide amount of the credit for all recipients is capped at $2 million per year for the three taxes combined. Every $1 of the tax credit yields $5 of private investment, with the total tax credit allocation of $2 million generating up to $10 million of private investments in COIN-certified CDFIs. However, if less than $10 million is invested in qualified CDFIs in any calendar year, the remaining amount may be carried over to the next year and any succeeding year during which the credit remains in effect.

Staff Comment: Staff has no concerns or issues with this request.

Staff Recommendation: Approve as budgeted.

Vote:

0890 SECRETARY OF STATE

Department Overview: The Secretary of State (SOS), a statewide elected official, is the chief election officer of the state and is responsible for the administration and enforcement of election laws. The SOS is also responsible for the administration and enforcement of laws pertaining to the filing documents associated with corporations, limited partnerships, and the perfection of security agreements. In addition, the office is responsible for commissioning notaries public, enforcing the notary laws, and in conjunction with being the home of the State Archives, preserving documents and records having historical significance. The SOS is the filing officer for lobbying and campaign registration and disclosure documents filed under the Political Reform Act. The SOS also operates the Safe-At-Home program, maintains the Domestic Partners and Advanced Health Care Directives Registries, and is home to the California Museum for History, Women and the Arts.

The Governor's Budget proposes total spending of $103.83 million ($28.75 million General Fund) for the SOS in 2014-15. Proposed staffing totals 562 personnel years (PYs), an increase of three PYs compared with the current year.

2014-15 California Secretary of State Budget
(Dollars in millions)

Funding	**2013-13**	**2013-14**	**2014-15**
General Fund	$196	$27.57	$28.75
Secretary of State's Business Fees Fund	$32.63	$41.61	$53.01
Federal Trust Fund	$5.26	$30.95	$19.9
Reimbursements	$32.19	$12.08	--
Victims of Corporate Fraud Compensation Fund	$2.17	$1.53	$1.63
Total Expenditures	$72.39	$113.84	$103.88
Personnel Years	465.0	559.0	562.0

*dollars in millions

Issue 1 – Help America Vote Act (HAVA)/VoteCal

Governor's Budget Request: The Secretary of State's Office has submitted two requests associated with the implementation of the statewide mandates of the Help America Vote Act (HAVA) of 2002.

1) $14.8 million (Federal Trust Fund Authority) in Fiscal Year 2014-15 to continue the implementation of the statewide voter registration database, known as VoteCal.

2) $5.105 million (Federal Trust Fund Authority) in Fiscal Year 2014-15 to continue the implementation of HAVA mandates. These mandates include modernization of voting equipment, education and training programs for local officials, and development and dissemination of voting information to increase voter participation.

Help America Vote Act (HAVA) - On October 29, 2002, President Bush signed into law the Help America Vote Act of 2002. This legislation requires states and localities to meet uniform and nondiscriminatory election technology and administration requirements applicable to federal elections. To date, California has received $435.2 million in federal HAVA funds, including interest earned.

HAVA has, so far, allowed the state and counties to replace punch-card voting systems and improve voter outreach, poll worker training, county security measures, and voter access for persons with disabilities. Activities in FY 2014-15 include voting system testing and approval and voter education programs. Grants to counties account for $2.3 million of the funding.

VoteCal. Section 303 of the Help America Vote Act (HAVA) of 2002 (Public Law 107-22, 107th Congress) mandates that each state implement a uniform computer voter registration database that can be maintained at the state level. To address this mandate, the Secretary of State has begun the implementation of VoteCal, the state's voter registration database. This database must contain the name and registration information of every legally registered active or inactive voter in the state.

On January 10, 2013, Special Project Report Number 5 (SPR 5) was approved by the Department of Technology. According to SPR 5 full-deployment of VoteCal is planned for June 30, 2015. The SPR projects that the total cost of VoteCal through implementation will be $98.2 million. For FY 2014-15, the Secretary of State has requested $14.8 million in Federal Trust Fund. This request will support the customization of software, project management contract, oversight contract, staff salaries, and training at the local level.

Staff Comment: Staff has no concerns with this request.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 2 – Business Connect Project

Governor's Budget Request: The Secretary of State's Office requests an augmentation of $4.59 million ($4.092 million Business Fees Fund and $0.5 million Business Programs Modernization Fund) for the continuation of the Business Connect Project.

Background: The Secretary of State is responsible for the management of over 150 different types of filings of business entities in California. The Business Programs Division, which is responsible for the management of business filings, is comprised of three sections: the Business Entities Section; Notary Public/Special Filings Section; and, the Uniform Commercial Code/Statement of Information section.

The Secretary of State receives more than one million business filings annually, and its current systems rely on antiquated methods, such as index cards and other paper documentation, to process and maintain records. Many business filings and other requests for services must be conducted in-person or by mail. These outdated methods result in very slow processing times, preventing new businesses from opening their doors and creating jobs. Processing times for the office have been as long as 117 days, preventing new companies from beginning operations and creating delays and uncertainty for existing companies.

To address this, the Secretary of State proposed automating many of the filing functions within the Business Programs Division. In March 2011, the Secretary of State submitted a Feasibility Study Report (FSR) that outlined the goals for this project. At that time, it was estimated that total project costs would be approximately $21.36 million with annual ongoing maintenance and support costs totaling $1.8 million. Resources to support the project would be directed from the Business Fees Fund.

The project's overall cost has been revised in an updated Special Project Report (SPR), that was issued in December 2013 to reflect the selection of a vendor. Even though project costs associated with systems integration and the purchase of hardware and software are lower than originally anticipated, project costs will increase due to a greater need for offsite backup and disaster recovery. Total project costs are now estimated to be $22.2 million, reflecting an increase of approximately $800,000 from the originally approved FSR amount.

Staff Comment: The Secretary of State anticipates that the upward revision in funding will largely be offset by the elimination of 45 positions that are currently associated with the Business Connect Project, and the expiration of 54 limited-term positions that support the Business Programs Division, that will no longer be needed once the filing process is automated. The Secretary of State's Office estimates that total net benefit of reduced position authority amounts to approximately $7.1 million.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 3 – Transfer of State Records Management Program to Secretary of State

Governor's Budget Request: The Secretary of State (SOS) requests an augmentation of 1.0 personnel years and $432,000 (General Fund) to transfer the California Records and Information Management (CalRIM) program and its three Records Analyst positions from the Department of General Services to the Secretary of State's Office. This request also includes trailer bill language that would amend current statute to reflect the changes requested in this proposal.

Background: The State Archives, which is part of the SOS, collects, catalogs, preserves, and provides access to the historic records of state government and some records of local governments. The SOS also had responsibility for state records management until legislation created DGS in 1963.

The state records program within the Department of General Services (DGS) has two elements: California Information Records Management (CalRIM) and the State Records Center (SRC). CalRIM establishes guidelines for state agencies in records management and retention and provides training and other technical services to help state agencies maintain effective records programs. The SRC stores and retrieves vital records and semi-active and inactive records for state agencies.

CalRIM and the State Archives currently review and approve records retention schedules prepared by state agencies. State Archives staff determines if records identified on each retention schedule have archival value and should therefore be transferred to the archives at the end of the records' lifecycles.

Staff Comment: This request is part of a two-step process. A spring finance letter will request a multi-tiered adjustment with a reduction to DGS' budget totaling $432,000 ongoing, a cessation of the statewide surcharge for the CalRIM program, and a commensurate reduction to all state entities that currently pay into this portion of the statewide surcharge, which will total $432,000 ($267,840 GF) in aggregate.

Staff Recommendation: Approve as budgeted. Adopt proposed trailer bill.

Vote:

Issue 4 – Building Rental Agreement

Governor's Budget Request: The Secretary of State is requesting an augmentation of $2.419 million ($1.427 General Fund and $.992 Special Fund) for Fiscal Year 2014-15.

Background: Due to a calculation error, the Secretary of State's current rent authority is insufficient. When the Secretary of State's building bond was paid off and the Secretary of State moved under the Department of General Services Building Rental Agreement (BRA), the authority for rent was misaligned with actual invoices, the Secretary of State's authority for rent is insufficient in relation to the amount being invoiced. The Secretary of State has requested an augmentation of $2.419 million, of which $535,000 is one-time and $1.184 million is ongoing.

Spring Finance Letter: The Secretary of State submitted a Spring Finance Letter requesting that that total amount to support this request be reduced by $983,000 ($575,000 General Fund and $408,000 Special Fund). The net budget augmentation related to this request for FY 2014-15 will total $1.436 million. This adjustment will more accurately reflect the level of funding necessary to cover the BRA.

Staff Recommendation: Approve request as modified by Spring Finance Letter.

Vote:

7502 DEPARTMENT OF TECHNOLOGY

Department Overview: The Department of Technology was established to support state programs and departments in the delivery of state services and information to constituents and businesses through agile, cost-effective, innovative, reliable, and secure technology. The department retains statewide authority to centralize and unify information technology projects and data center services to enhance the ability to develop, launch, manage, and monitor large information technology projects.

In August 2010, the California State Legislature passed AB 2408 (Smyth), Chapter 404, Statutes of 2010, to reestablish the Office of the State Chief Information Officer (OCIO) as the California Technology Agency and to rename the State Chief Information Officer as the Secretary of the California Technology Agency. While Senate Bill 90 (Committee on Budget and Fiscal Review), Chapter 183, Statutes of 2007, had already made the OCIO a cabinet-level agency with statutory authority over strategic vision and planning, enterprise architecture, IT policy, and project approval and oversight for the state in 2007; AB 2408 codified into law significant functions, duties, and responsibilities of the office that had been assigned to the Office of the Chief Information Officer. In addition to consolidating statewide IT functions under one cabinet-level agency, the legislation passed in 2010 was also responsible for coordinating the activities of agency and department CIOs and promoting the efficient and effective use of IT in state operations.

On July 1, 2013, the Governor’s Reorganization Plan No. 2 (GRP2) created the Government Operations Agency and, as a part of that plan, moved the California Technology Agency (previous Organization Code 0502) under the newly-created Government Operations Agency, which now houses the Department of Technology.

The Office of Technology Services (OTech), within the Department of Technology, provides the information technology processing platforms for over 500 customers, including the Executive Branch and public entities. OTech is accountable to its customers for providing secure services that are responsive to their needs and represent best value to the state. OTech is a fee-for-service organization and operates as a 100 percent reimbursable department. OTech’s Service Level Agreements with its customers include a 99.9 percent service availability goal for IT services. OTech must continue to provide sufficient processing capacity to deliver their performance and service agreed to in the Service Level Agreements.

Budget Overview: The Governor’s 2014-15 Budget proposes $434.51 million dollars ($4.37 million General Fund) and 902.7 personnel years. The Governor’s 2014-15 budget request reflects an increase of $37.75 million dollars ($80,000 General Fund increase) and an increase of 5.0 Personnel Years.

2014-15 Department of Technology Budget Overview
(Dollars in millions)

Funding	2012-13	2013-14	2014-15
General Fund	$3.95	$4.29	$4.37
State Emergency Telephone Number Account	$94.04	$-	$-
Federal Trust Fund	$1.93	$-	$-
Reimbursements	$321	$2.80	$2.80
Technology Services Revolving Fund	$331.32	$322.85	$360.60
Central Service Cost Recovery Fund	$2.93	$3.23	$3.15
Total Expenditures	$434.51	$333.18	$370.93
Personnel Years	1,166.8	897.7	902.7

Issue 1 – Secure File Transfer

Governor's Budget Request: The Department of Technology requests a $103,000 reduction in budget authority for FY 2014-15 to replace contractor staff with two permanent civil service staff to support the Secured File Transfer Shared Service.

Background: The department's Secure File Transfer service provides a more secure way to share data as an alternative to more popular methods such as CD's, DVD's, USB drives and internet transfers. The Secure File Transfer service is extremely specialized and often entails tailoring systems to meet specific requirements of various customers. Currently, OTech has 7,450 Secure File Transfer accounts, with over 39 departments.

The Secure File Transfer service is currently supported by contractors. The service contract totals $323,000 a year. OTech estimates that workload associated with this service could be provided in-house by two permanent staff at $220,000 a year. Savings associated with this service would eventually be reflected in lower rates provided to the Department's customers.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 2 – Security Compliance

Governor's Budget Request: The Department of Technology requests a $684,000 (Technology Services Revolving Fund) budget augmentation and five limited-term positions to staff a two-year pilot project with the Office of Information Security (OIS).

Background: OIS, an office within the Department of Technology, is statutorily responsible for developing and maintaining state information security polices and standards and providing technology direction to agencies and departments to ensure the confidentiality, integrity, and availability of state systems and applications, and ensuring the protection of state information.

The technology security standards, which OIS establishes and monitors for compliance, are largely consolidated within Chapter 5300 of the State Administrative Manual (SAM). The SAM contains statewide policy on various issues, including IT. Chapter 5300 of SAM sets standards for a variety of IT security issues, including risk management, recovery planning, telecommunications, privacy, encryption, data retention, and remote access.

This pilot audit process would begin with the assessment of security measures and practices at eight departments that range in size. The selection criteria for an assessment would be dependent on several factors: departments believed to be most susceptible to risk, repeat offenders, and those deemed to play a critical role in the State Emergency Plan functions.

LAO Recommendation: The LAO has recommended approval with modifications of the Governor's proposal. The pilot will help the state to more accurately assess the extent of noncompliance, thereby informing the state's decisionmaking regarding establishing an effective enforcement approach to reduce its IT security risk. Given the limited resources budgeted for the pilot, it is appropriate that resources are prioritized as proposed---through the audit selection criteria---towards agencies and departments with the most critical information assets. However, to fully realize the benefits of the pilot, the LAO recommends the Legislature direct CalTech during budget hearings to address the following issues and make associated modifications to the pilot.

- The department should provide greater detail to the Legislature on the audit methodology and how the methodology will be developed. For example, will there be a standard methodology or will methodology be adapted based on the IT needs of the audited department? How will the department respond when noncompliance is found at an audited department? The Legislature would want to ensure that the audit methodology is consistent with its priorities.

- The department should add a robust evaluation component to the pilot to assess what was learned from the pilot and inform a decision whether or not to scale up the pilot by expanding OIS's auditing capacity. Specifically, the evaluation of the pilot should (1) compare the noncompliance identified in the pilot with noncompliance identified in prior self-certifications to determine the extent to which self-certification is underestimating the state's IT security risk, (2) assess the severity of the noncompliance, and (3) estimate the cost of achieving compliance in cases where noncompliance was identified.

- The Legislature should also direct CalTech to submit a report to the Legislature after the pilot concludes that highlights compliance challenges faced by the audited departments and includes recommendations as to how agencies and departments could more effectively be brought into compliance. The LAO also recommends the Legislature approve the proposed trailer bill language, as it will facilitate OIS's ability to recover costs associated with the audits, as audits are usually not currently requested by departments.

Staff Comment: Staff concurs with the LAO recommendation. To best determine if the auditing capacity of OIS should be expanded, additional reporting requirements should be added. As noted in the LAO recommendation, the evaluation should include a comparison of noncompliance prior to the implementation of the pilot versus noncompliance during the pilot process, an assessment of how severe a risk was posed by noncompliance, and the amount of resources required to ensure compliance when identified by OIS.

Staff Recommendation: Approve as budgeted, with additional reporting requirements included in theLAO recommendation. Adopt proposed trailer bill language.

Vote:

Issue 3 – Gold Camp Data Center

Governor's Budget Request: The Department of Technology requests $6.68 million (Technology Services Revolving Fund) to increase the heating and cooling capacity at the Gold Camp Data Center.

Background: The Gold Camp Data Center, located in Rancho Cordova, is one of two data centers owned and operated by the Department of Technology. The Gold Camp Data Center was designed and built approximately 13 years ago, and was designed to support the data conditions of that period. However, additional data requirements and new programs have added to the data center's workload. The requested funds would support the development of a new Uninterruptible Power Supply (UPS) system, associated power distribution equipment, and cooling components. The Department of Technology anticipates that the construction of the new UPS will be complete by November 2015.

Staff Comment: Upon completion of this project, the Department of Technology has projected that they will have the capacity for growth that will take them to FY 2022-23.

Staff Recommendation: Approve as budgeted.

Vote:

Issue 4 – Department of Technology Sunset

Governor's Budget Request: The Department of Technology requests the deletion of Government Code Section §11548.5, which includes a sunset of the Department of Technology on January 1, 2015.

Background: AB 2408 (Smyth) Chapter 404, Statutes of 2010, codified the changes made in the Governor's Reorganization Plan No.1 of 2009. One of the many changes included in AB 2408 was the extension of a repeal provision included in Government Code Section §11548.5 that would sunset the authority provided to the Department of Technology on January 1, 2015.

The Department of Technology contends that the services provided by the department are so sweeping that a sunset of their authority would be much less feasible than it was when the Legislature allowed the sunset of the Department of Information Technology (DOIT) in 2002.

Staff Comment: The requested language does not have an impact on the budget, and therefore should be considered in a policy committee.

Staff Recommendation: Hold open.

Vote:

8880 FINANCIAL INFORMATION SYSTEM FOR CALIFORNIA (FI$CAL)

Background: The Financial Information System for California (FI$Cal) Project is a partnership of four control agencies: the Department of Finance, the State Controller's Office, the State Treasurer's Office and the Department of General Services. FI$Cal is expected to provide the state with a single integrated financial management system that encompasses budgeting, accounting, procurement, cash management, and financial management and reporting. This "Next Generation" project, through the adoption of best business practices, is expected to reengineer business processes; improve efficiency; enhance decision making and resource management; and provide reliable, accessible, and timely statewide financial information allowing the state to be more transparent. After a lengthy multi-stage procurement process, a vendor was selected in 2012 to begin designing and implementing the project.

FI$Cal is the state's largest information technology project in terms of budget and scope, and has considerable project risks. In recent history, the Legislature has taken action to mitigate this risk and ensure the best chance for project success by prescribing a multi-stage procurement, requiring additional reporting, stipulating that the State Auditor's Office monitor the procurement process, and by having the active monitoring of project meetings by LAO staff.

The Administration is proposing a shift in implementation plans for the FI$Cal project that will lengthen the overall duration of the project, this change has been articulated in the Special Project Report #5 (SPR 5) and the department's BCP.

The current FI$Cal project plan anticipated that groups of state departments would join the new system over three 12-month waves of implementation between 2014 and 2016. The new project plan has lengthened the waves to 24-month periods and moved most of the departments into the last wave of implementation, this will extend implementation of the project by one year, until 2017. This change will increase total project costs from $616.8 million to $672.6 million, a 55.8 million or 9 percent, increase in total costs.

Issue 1 – Funding for Design, Development, and Implementation of FI$Cal

Governor's Budget Request: FI$Cal requests $4.3 million for Fiscal Year 2014-15 to replace the Department of General Services Activity Based Management System (ABMS) and convert DGS from partially deferred to a FI$Cal Wave 2 department. This request brings the total amount requested for FI$Cal for FY 2014-15 to $106.5 million ($94.4 million General Fund, $8.9 million various special funds, and $3.2 million Central Service Cost Recovery Fund). This request also includes trailer bill language to reflect these changes in statute.

Background: The process for IT procurement is generally the same, regardless of the cost and scope of the project. The review and approval process begins with the state entity seeking the IT project developing a feasibility study report (FSR). The FSR is essentially the business justification for undertaking a project. The FSR is translated into a budget proposal that is submitted to the Legislature for review and action. Modifications to the original FSR that alter scope, cost, and/or schedule are proposed in a Special Project Report (SPR). In January 2014 FI$Cal released the fifth iteration of an SPR (SPR 5). The Legislature approved SPR 4 in March 2012. The changes in SPR 5 are a result of the project team gaining a better understanding of the technical solution and what requirements will be necessary to fully implement each subsequent wave.

Approximately eighteen months have elapsed since the contract with FI$Cal's system integrator, Accenture, was executed (June 2012). Since then, the FI$Cal project team, including the systems integrator, have developed a better understanding of what requirements will be needed to fully implement all waves successfully. During pre-wave, the project team conducted a more in-depth analysis of each future wave to ensure that they were best positioned for a successful implementation. The project has been designed to increase functionality while also increasing the number of departments during each wave. The table below represents the number of departments included in each wave, added functionality of each wave, and the go-live date of each wave per SPR 5:

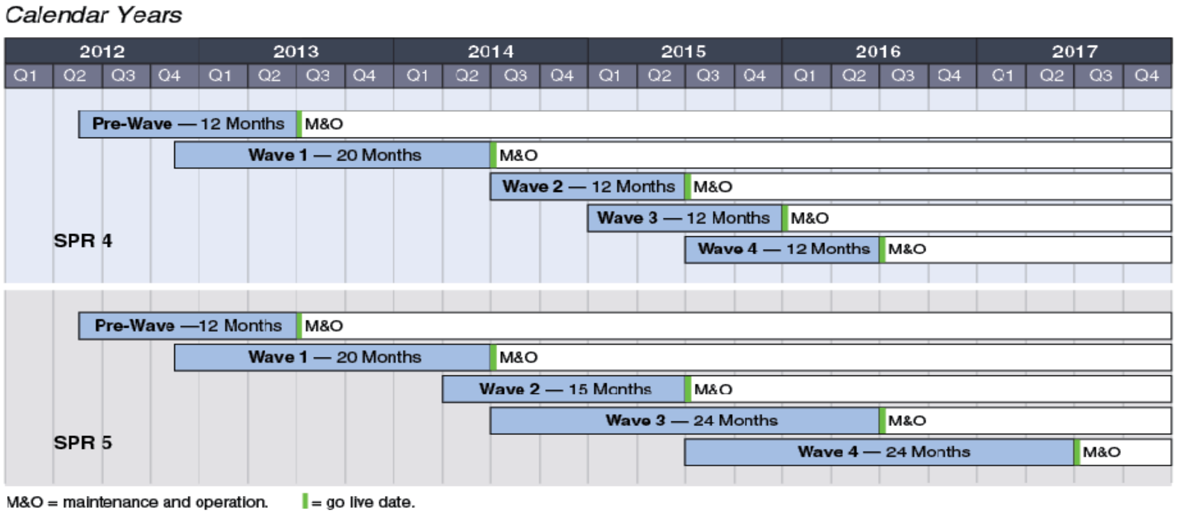
FI$Cal Schedule per SPR 5

Wave and go-live Date	Number of Additional Departments	Additional Functionality
Pre-Wave July 1, 2013	7	Chart of Accounts Master Vendor File Requisition to Purchase Order
Wave 1 July 1, 2014	23	DOF Control Agency Functions Department-level accounting, budgeting, cash management, and procurement
Wave 2 July 1, 2015	3	DGS Control Agency Functions
Wave 3 July 1, 2016	2	SCO Control Agency Functions STO Control Agency Functions
Wave 4 July 1, 2017	68	Public Transparency Website

SPR 5 will result in a twelve-month schedule extension of FI$Cal and increases the projects overall cost by $56 million. The request is a reflection of the FI$Cal project team incorporating the financial management functions within the Department of General Services (DGS) into the scope of the project. FI$Cal had originally intended to defer DGS' financial management activities until a later date. The FI$Cal project team has determined that the software that supports the financial management activities is outdated and will need to be replaced and the latest SPR reflects the change to incorporate DGS' financial management activities into the scope of FI$Cal. The most significant change as a result of the latest SPR is that there are now a larger number of departments included into Wave 4 – the final wave. A comparison of the implementation timeline under SPR 4 and SPR 5 is below:

Figure 3

Comparison of FI$Cal Implementation Timeline Under Special Project Report (SPR) 4 and 5



LAO Recommendation: *Monitor and Reassess Approach for Wave 4 Through Modified Annual Reporting.* Currently, the project is required to provide the Legislature an update in February of each year. As part of this update, the project is required to provide a discussion of lessons learned and best practices that will be incorporated into future changes in project management activities. The LAO thinks it is important for the Legislature to remain apprised of project developments through the annual report. However, the timing of the annual report to the Legislature should more closely align with the deployment of FI$Cal waves. As the February annual report is not available to the Legislature until seven months after the project's July deployments, too much time may have elapsed for the Legislature to address problems arising from the deployment of a wave. The LAO recommends that the Legislature revise the due date for the annual report from February 15 to October 15, in better time for the Administration and Legislature to make necessary budgetary changes. The LAO also recommends the Legislature direct the project after the completion of Waves 1, 2, and 3 to identify—as part of the annual report—foreseeable challenges with the implementation of future waves, particularly Wave 4.

Consider Retention Pay Program. Although it has not been conclusively proven that pay differentials improve staff recruitment and retention on IT projects, the LAO thinks the Legislature should consider directing the Administration to develop a retention benefit that rewards state workers for staying at the FI$Cal project through its completion. While the state may be limited in what types of retention benefits it could extend to FI$Cal staff due to civil service rules (for example, the state likely could not provide outgoing staff hiring preferences upon the completion of the project), the LAO thinks the Administration could explore various retention benefits. The LAO recommend that any retention benefit for FI$Cal staff include an assessment of the benefit program's impact on the project's ability to recruit and retain qualified staff. Measuring the outcomes of a retention benefit would help ensure that the benefit is set at an appropriate level and could be used to establish a best practice for future critical IT projects.

Approve 2014–15 Budget Proposal, While Understanding Inherent Project Risk. The Governor's budget proposal reflects a reasonable funding plan to implement the updated project plan (SPR 5). The LAO believes that the time and effort that project staff has spent in updating the project plan has reduced overall risk and strengthened FI$Cal's likelihood of success. Nevertheless, FI$Cal involves the development of the most ambitious and complex IT system in the history of the state and significant risk remains. In its review of the Governor's proposal and its ongoing oversight of the

FI$Cal Project, the Legislature should be aware of and monitor not only the general risk inherent in all IT projects but also the shifting of some risk to the latter end of the project due to the substantial increase in Wave 4 departments. The LAO recommends the Legislature ask the project to identify the steps it is taking to address the risks inherent in the substantial broadening of the scope of Wave 4. Ultimately, the LAO believes that the benefits of proceeding with FI$Cal development outweigh the risk and therefore recommend approval of the Governor's budget proposal. Should the project make significant changes going forward, a new budget proposal would be submitted for legislative review.

Bureau of State Audits: Pursuant to Government Code, Section 15849.22(e), the California State Auditor (State Auditor) is required to monitor the FI$Cal project throughout its development. The most recent report, issued February 26, 2014, noted that the project has made progress, but the State Auditor still does have some concerns. Some of the issues addressed in the annual report include the following:

- The increased size of SPR 5 may overwhelm the projects resources during the implementation of Wave 4 – the largest wave.
- The project is behind schedule in implementing some key budgeting functions.
- The project has taken full advantage of knowledge transfer opportunities, which could increase a dependence on a vendor for future maintenance of Fi$Cal.

Staff Comment: Staff largely concurs with the recommendations provided by the LAO. However, after discussing with the LAO and the FI$Cal project team, it appears that incorporating the information identified by the LAO into the quarterly reports that are currently provided by FI$Cal staff would be the most effective means to gather this information.

Staff also agrees with the concerns raised by the LAO regarding staff retention for FI$Cal. It is important to note that the staff retention and recruitment challenges faced by FI$Cal are not unique to this project. Many other large-scale IT projects suffer from the same challenges. Directing FI$Cal to identify a benefit plan that could address staffing challenges for this project may also benefit future projects. Staff would recommend that the FI$Cal project team work with the LAO to identify a recruitment and retention plan that will afford the FI$Cal, and future projects, a higher degree of staff continuity. As noted by the LAO, the plan should include identifiable metrics so best practices could be applied to future IT projects.

Assembly Budget Subcommittee No. 4 approved the requested funding on an ongoing basis. This subcommittee may wish taking the same action. Any changes that impact the cost of FI$Cal will require that a new SPR be developed, triggering a new request. This subcommittee may still hold informational oversight hearings regarding the process of FI$Cal.

Staff Recommendation: Approve as budgeted. Adopt proposed trailer bill. Direct FI$Cal project staffing to incorporate the information requested by the LAO, including information on the status of the implementation of the most recent wave release into the quarterly FI$Cal reports. Direct FI$Cal staff to coordinate with the LAO to identify a staff retention plan that addresses the staffing challenges associated with a large-scale IT project, such as FI$Cal.

Vote: