Statewide Issues and Various Departments

This Chapter describes items in the Budget that are statewide issues or related to various departments.

Employee Compensation and Collective Bargaining

The Budget includes $1.2 billion ($602 million General Fund) for employee compensation, health care costs for active state employees, and retiree health care prefunding for active employees. Included in these costs are salaries and benefit increases as a result of contract negotiations and pay increases related to minimum wage changes in Chapter 4, Statutes of 2016 (SB 3). Funding is also included for 2018 calendar year increases in health care premiums and enrollment.

Through the collective bargaining process, the Administration remains focused on addressing the state’s $74 billion unfunded liability for retiree health benefits. The strategy for addressing the liability includes equal cost-sharing between the employee and employer to prefund retiree health benefits, and for new employees, extending the period to qualify for retiree health benefits, and reducing the employer subsidy for retiree health benefits. Agreements reached in the past year have all included these retiree health provisions.

Since the 2016 Budget Act, the Administration has negotiated successor contract agreements with the bargaining units represented by the Service Employees International Union (SEIU), Attorneys and Administrative Law Judges, Public Safety Officers, Craft and
Maintenance Workers, Stationary Engineers, Health and Social Service Professionals, Psychiatric Technicians, and Firefighters. The Administration will continue bargaining with the unit representing Physicians and Dentists, the only bargaining unit that remains without an agreement.

Additionally, as part of Chapter 2, Statutes of 2016 (AB 133), the 2015 Budget Act included a one-time allocation of $240 million to pay down the state’s unfunded liability for retiree health care. This amount was to be apportioned to the trust fund accounts of bargaining units that had reached a memorandum of understanding with the Administration by November 1, 2016, and where such agreement includes employer and employee contributions for prefunding retiree health care. Pursuant to the requirements of AB 133, the $240 million appropriation has been apportioned to the Attorneys and Administrative Law, California Highway Patrol, Correctional Officers, Public Safety Officers, Professional Engineers, and Professional Scientists units.

Currently, the state has approximately $400 million set aside in the prefunding trust fund to pay for future retiree health benefits. By the end of 2017-18, the trust fund balance will more than double and approach $1 billion in assets.

**State Retirement Contributions**

The Administration remains committed to the long-term sustainability of the state retirement systems and to ensuring the benefits promised its employees are paid out during their retirement years.

Presently, like many other public pension funds, the California Public Employees’ Retirement System (CalPERS) and the California State Teachers’ Retirement System (CalSTRS) are struggling to keep funding on track to pay for future benefits. Weak investment returns in a low-interest rate environment have exposed the volatility of portfolios heavily reliant on stock returns. This dynamic is compounded by a maturing membership, with active employees—who pay into the system—nearly equaling the number of retirees drawing benefits. An increase in retiree life expectancy is also increasing costs. When the financial markets fall, the pension systems must spread the losses over a relatively small number of employees—driving substantial increases in contribution rates as a percentage of payroll. CalPERS and CalSTRS are facing negative cash flows, meaning the systems have to sell assets to pay for benefits. Additionally, because both systems are less than 100 percent funded, contributions above the normal
cost—the cost associated with employee benefits earned in a given year—are necessary to continue to pay down unfunded liabilities.

To address these issues, both CalPERS and CalSTRS have been evaluating the long-term investment assumptions—or discount rate—that the pension systems use to estimate contributions from employers, including the state. Lowering expectations for long-term investment earnings will trigger contribution increases for employers and most employees.

The Budget includes $5.3 billion ($2.8 billion General Fund) for state contributions to CalPERS for state pension costs. In addition, the Budget includes $672 million General Fund for California State University retirement costs. These estimates include the effect of the recent CalPERS board decision to reduce the current 7.5 percent discount rate to 7 percent over the next three budget years. The reduction of the discount rate results in additional state contributions of approximately $172 million ($105 million General Fund) in 2017-18, increasing to $2 billion ($1.1 billion General Fund) when the discount rate changes are fully implemented. Total state pension contributions are expected to reach $9.7 billion ($5.6 billion General Fund) by 2023-24 due to changes in the discount rate, scheduled contribution increases under existing funding policies, and payroll growth.

The Budget also includes $2.8 billion General Fund for state contributions to CalSTRS. The Budget assumes CalSTRS will adopt new mortality assumptions, implement a discount rate reduction, and exercise its authority to increase state contributions by 0.5 percent, resulting in an additional $153 million in General Fund contributions. The proposed funding is consistent with the funding strategy signed into law in 2014, and positions CalSTRS on a sustainable path forward, eliminating the unfunded liability in about 30 years.

Figure SWE-01 provides a historical overview of contributions to CalPERS, CalSTRS, the Judges’ Retirement System (JRS), the Judges’ Retirement System II (JRS II), and the Legislators’ Retirement System (LRS) for pension and health care benefits.

**Secure Choice Retirement Savings Program**

Chapter 804, Statutes of 2016 (SB 1234), authorized the Secure Choice Retirement Savings Investment Board to implement the California Secure Choice Retirement Savings Program—a state-administered retirement savings program for private sector employees.
in California with no access to workplace retirement savings plans. According to the feasibility study sponsored by the Board, there are approximately 6.8 million workers who do not have access to a workplace retirement plan. The program offers all eligible workers an opportunity for retirement savings at a low cost to provide financial security during their retirement years. The Budget provides an initial $15 million General Fund loan to fund the necessary start-up and administrative costs to implement the program. Additional General Fund loans will be provided in future years, as the program ramps up activities. Each loan will be repaid from the administrative fee charged to participants.
Civil Service Improvement

The Administration continues to pursue strategies to improve the state’s civil service system that enable state departments to quickly recruit, hire, train, and develop employees through a merit-based process. Since the 2016 Budget Act, the Administration has furthered these efforts by implementing a web-based job analysis library for personnel officers, expanding the leadership competency training program for supervisors and managers, and consolidating approximately 2,000 human resource policy memoranda into a single and searchable online resource. To further these efforts, the Budget includes $2.8 million in reimbursement authority for the Department of Human Resources to expand the capacity of the statewide training center, providing additional streamlined and tailored instruction for civil service employees. The Budget also establishes a statutory framework to further ongoing class consolidation efforts, which will increase promotional opportunities for employees while ensuring sufficient probation periods remain in place. The proposed statutory language will also provide departments—and job candidates—with hiring flexibility, by refreshing eligibility lists more frequently to respond to a dynamic workforce.

Information Technology Security

The Administration remains committed to keeping data about government operations safe and secure. In 2015, the Governor issued an Executive Order to establish the California Cybersecurity Information Center through the Office of Emergency Services as a coordinating entity for state agencies involved in protecting the state’s computer networks and technology infrastructure. Several units at the Department of Technology are dedicated to preventing and responding to attacks on the state’s Data Center, which houses the majority of the state’s server capacity and network infrastructure. The Department of Technology’s Office of Information Security audits departments for compliance with state security policies and the Military Department’s Cyber Network Defense Team performs security assessments to identify vulnerabilities in departments’ information technology infrastructure. Additionally, the Administration funds individual departments for information technology security operations as part of departments’ state operations appropriations.

The Budget includes $9.9 million ($5.3 million General Fund) to strengthen the state’s information technology security operations across various departments.
Cannabis Regulation

The Medical Marijuana Regulation and Safety Act enacted in 2015 created a regulatory framework for the licensing and enforcement of the cultivation, manufacture, transportation, storage, and distribution of medical cannabis in California. Proposition 64, the Adult Use of Marijuana Act, made the recreational use of cannabis legal to people over the age of 21. In addition, Proposition 64 makes it legal to sell and distribute cannabis as a regulated business beginning on January 1, 2018.

Proposition 64 levies new excise taxes on the cultivation and retail sale of both recreational and medical cannabis as of January 1, 2018. The cultivation tax is $9.25 per ounce of flower and $2.75 per ounce of leaves, to be paid on all recreational and medicinal cultivation of cannabis, and will be adjusted for inflation beginning in 2020. In addition, there will be a 15-percent tax on the retail price of cannabis. Recreational cannabis will also be subject to state and local sales taxes. Medical cannabis, on the other hand, is exempt from existing state and local sales taxes.

The amount and timing of revenues generated from the new excise taxes are highly uncertain and will depend on various factors including state and local regulations, how cannabis prices and consumption change in a legal environment, and future federal policies and actions toward the cannabis industry. Under Proposition 64, revenues generated from the new excise taxes will be allocated for various purposes, as specified by Proposition 64, including regulatory costs, youth substance use programs, environmental clean-up resulting from illegal cannabis growing, programs to reduce driving under the influence of cannabis and other drugs, and to reduce negative impacts on public health or safety resulting from the legalization of recreational cannabis.

As the state moves forward with the regulation of both medical cannabis and recreational cannabis, one regulatory structure of cannabis activities across California is needed. Implementing the current medical and recreational cannabis statutes separately will result in duplicative costs of an additional $25 million for a second track and trace system. Additionally, a separate regulatory framework for each would lead to confusion among licensees and regulatory agencies, undermining consumer protection and public safety.

The Budget includes $52.2 million for the regulation of cannabis in 2017-18 to fund regulatory activities, processing of licenses, and enforcement. Since cannabis license fees will not be collected until January 1, 2018, the General Fund provided loans to the Marijuana Control Fund to cover the initial implementation and regulatory costs for cannabis-related activities. It is anticipated that these loans will be repaid in 2018-19.
Specific proposals include:

- **Department of Consumer Affairs**—$22.5 million to enhance the Bureau of Medical Cannabis Regulation within the Department of Consumer Affairs. The Bureau will regulate the transportation, storage, distribution, and sale of cannabis within the state and will also be responsible for licensing, investigation, enforcement, and coordination with local governments.

- **Department of Public Health**—$1 million for the licensing and regulation of medical cannabis product manufacturers.

- **Department of Food and Agriculture**—$23.4 million to provide Cannabis Cultivation Program administrative oversight, promulgate regulations, issue cannabis cultivation licenses, and perform an Environmental Impact Report. In addition, the Department of Food and Agriculture is responsible, with assistance from the California Department of Technology and the Board of Equalization, for establishing a track and trace program to report the movement of medical cannabis products throughout the distribution chain using unique identifiers.

- **Board of Equalization**—$5.3 million in 2017-18 to notify businesses of the new tax requirements and update its information technology systems to register businesses and process tax returns from retail sales. Proposition 64 requires the Board of Equalization to administer an excise tax on cannabis sales and a cultivation tax on all harvested cannabis that enters the commercial market.

- **Department of Health Care Services**—$5 million in 2016-17 for the public information program specified in Proposition 64. The program, to be established and implemented no later than September 1, 2017, will cover a number of health-related topics pertaining to cannabis and cannabis products.

### State Fleet Zero-Emission Vehicles

Building upon the Governor’s Executive Order B-16-12, which mandated specified increases to the number of zero-emission vehicles purchased for use in the state fleet, the Administration released an updated Action Plan in October 2016. It commits the state to further increasing the percentage of zero-emission vehicles purchased annually, starting at 15 percent in 2017-18 and reaching 50 percent by 2019-20. To more effectively implement the new directive, the Budget includes $6.6 million ($3.3 million General Fund) for engineering assessments associated with electric vehicle charging infrastructure.
at state facilities. The Department of General Services will be required to certify it has maximized all available funding from non-state sources in advance of supporting these activities with state funds.

**Public Utilities Commission**

The California Public Utilities Commission regulates privately owned telecommunications, electric, natural gas, and water companies, in addition to overseeing railroad/rail transit, moving and transportation companies. The Commission is the only agency in the state charged with protecting private utility consumers and overseeing that customers have safe, reliable utility service at reasonable rates. The Budget includes $1.8 billion for the Commission.

During the last legislative session, the Governor signed a package of legislation enacting various reforms to improve safety, governance, accountability and transparency of the Commission. In an accompanying signing message, the Governor also called on the Commission to take additional actions to further improve transparency and accountability, including appointing an Ethics Ombudsman; establishing a web portal for the Public Advisor to receive public complaints and comments; creating a more streamlined process for releasing information to the public; improving coordination with other state agencies and departments; increasing the Commission’s presence outside of San Francisco; and working with the California Research Bureau to study the governance of telecommunications service.

The Governor also directed the Administration to work with the Commission to develop a reorganization plan to transfer Commission duties and responsibilities over transportation-related entities to departments within the California Transportation Agency; codify the appointment of all senior executive staff who will serve at the pleasure of the Commission, including the Executive Director, General Counsel, Chief Internal Auditor, and Chief Administrative Law Judge; and codify the appointment of a Deputy Executive Director for Safety.

The Administration and the Commission will continue to work on implementing these measures throughout the current and upcoming fiscal years. Additional reform measures that may require legislative approval include subjecting the Commission to the judicial review provisions of the California Public Records Act and revising the Commission’s public records response and confidentiality statute.
The Budget includes several proposals to implement the reforms:

- **Enhanced Transparency**—An increase of $953,000 from various funds to implement multiple transparency initiatives identified in the reform package. Specifically, this proposal will support a new proceeding to update and implement the new *ex parte* rules and reporting requirements pursuant to Chapter 807, Statutes of 2016 (SB 215), fulfill the Commission’s statutory mandate to transcribe complete records of all proceedings and testimony before the Commission or any commissioner on any formal hearing within specified timelines, provide timely response to public records requests and subpoenas, and publish contract and contract process audit information as required by Chapter 815, Statutes of 2016 (AB 1651).

- **Improved Governance**—An increase of $549,000 from various funds to improve cross-agency collaboration. The Commission will participate in federal administrative agency processes that can impact the Commission and California’s progress towards climate change goals. These resources also support implementing reforms enacted in Chapter 808, Statutes of 2016 (SB 512), to improve Commission operations and governance, including applying the Code of Ethics from the Administrative Procedures Act to administrative law judges, holding monthly meetings in areas outside of San Francisco, publishing information on the Internet informing public participation, and allowing certain local governments to be paid intervenor compensation when they intervene or participate in Commission proceedings for the purpose of protecting health and safety.

**INFRASTRUCTURE**

**Debt Service**

General Obligation (GO) and lease revenue bonds are used to fund major infrastructure improvements such as new road construction, flood control levees, and other critical public infrastructure. California voters have approved more than $112.3 billion of new GO bonds since 2000, including the Kindergarten through Community College Public Education Facilities Bond Act of 2016 (Proposition 51) approved in November 2016. As the state issues the remaining voter-authorized bonds, debt service costs will continue to increase.

Estimated General Fund debt service expenditures in 2017-18, after various other funding offsets, will increase by $151 million over current-year expenditures, to a total of $5.5 billion. This increase is comprised of $104 million for GO debt service
($4.9 billion total) and $48 million for lease revenue bonds ($598 million total) and is attributed to recent bond sales and the planned issuance of additional bonds over the next year.

The Administration continues to take actions to better manage this area of the Budget, such as requiring GO bond programs to demonstrate an immediate need for additional bond proceeds prior to issuing new bonds. These efforts have helped reduce the amount of unspent GO bond proceeds in the state treasury from approximately $13.9 billion as of December 2010, to just less than $1.4 billion by the end of October 2016, excluding the recent fall 2016 bond sales. In addition, only the most critical new lease revenue bond funded projects have been approved, thus minimizing new debt service while continuing to make needed investments.

**California Five-Year Infrastructure Plan**

In conjunction with the release of the Governor’s Budget, the Administration is releasing the 2017 Five-Year Infrastructure Plan. The Plan outlines the Administration’s infrastructure priorities for the next five years, including investments in transportation and high-speed rail, state institutions, natural resource programs, and education. Given the state’s General Fund constraints, the Plan proposes limited investments to the most critical infrastructure projects.