

MAY 21, 2020

Overview of 2020-21 May Revision State Administration Proposals

PRESENTED TO: Assembly Budget Subcommittee No. 4
On State Administration
Hon. Jim Cooper, Chair



LEGISLATIVE ANALYST'S OFFICE

Unemployment Insurance (UI)

Update on Unemployment Claims

- California has experienced an unprecedented rise in unemployment claims since the beginning of March.
- As of May 9, California had roughly 3.6 million workers receiving unemployment benefits.
- In total, as of May 9, about \$12 billion in UI benefits have been distributed to Californians.
- The state UI Trust Fund became insolvent several weeks ago. As of May 18, the federal government has advanced \$1.1 billion to the state to cover regular state UI benefit payments over the next few months.
- As part of the May Revision, the administration requested increased expenditure authority in 2020-21 of \$38 billion, about \$34 billion of which is federally funded. The federal portion is comprised of funding for (1) a temporary \$600 weekly increase to normal benefits, (2) an additional 13 weeks of extended state benefits, and (3) benefits to the self-employed under the new Pandemic Unemployment Assistance program.



Employment Development Department (EDD)

Additional Resources Provided. The federal Family First Coronavirus Relief Act (FFCRA) provided state grants for administrative costs related to the increase in UI claims. The state has received the first of two installments—of \$59 million each—and expects to receive the second installment when the federal government makes these funds available. Funds have been used for (1) call centers, (2) vendor costs to set up new UI programs, (3) staff overtime, and (4) redirected staff salaries.

Additional Staff Redirected. The administration has said that it has redirected about 1,400 staff from other EDD branches and throughout state service to assist in UI claims processing.

Additional Staff Proposed. EDD's updated May Revision workload estimate proposes to hire an additional 780 positions for 2020-21. These positions would be federally funded under the existing program in which the federal government pays the basic administrative costs for the state UI programs.

Access Issues May Be a Concern. Despite the additional resources described above, there continues to be some concern regarding EDD's capacity to issue UI benefits promptly once a claim has been submitted. Under normal economic conditions, EDD is able to issue about 80 percent of first benefit payments within three weeks of claim submission. The subcommittee may wish to request that the department provide an update on access issues.



Paid Family Leave

Expanding Job Protection to Small Business Employees

- ***Existing Job Protection Requirements.*** Under existing state law, businesses with more than 50 employees must provide 12 weeks of job protected family and medical leave and businesses with more than 20 employees must provide 12 weeks of job protected child bonding leave.
- ***Governor's Budget Expanded Job Protected Leave Requirement to Smaller Businesses.*** The Governor's budget proposed to require all businesses, regardless of size, to provide 12 weeks of job protected leave for all situations covered by the state's Paid Family Leave program. The administration also included \$1 million General Fund for grants to small businesses to retrain existing workers when an employee takes protected leave as a result of this expansion.



Housing and Homelessness

Key Components of Governor's May Revision Housing and Homelessness Plan

(In Millions)

Issue	Fiscal Effect
New May Revision Proposals	
Project Roomkey ^a	\$750
Expenditure of National Mortgage Settlement	300
Proposal Maintained From January	
State Low-Income Housing Tax Credit Program Expansion ^b	500
Proposals Withdrawn From January	
California Access to Housing and Services Initiative	-750
Housing Production Technical Assistance	-10
Reversions of Previously Authorized Funding to General Fund	
Moderate-Income Housing Production	-250
Infill-Infrastructure Grant Program	-203
Housing Navigator Program	-5
Additional General Fund Solutions	
Special Fund Loans ^c	-141
Special Fund Transfers ^{d,e}	-115
^a Federal funding from Coronavirus Relief Fund.	
^b The administration's multiyear plan assume no reduction in revenues due to the tax credit expansion.	
^c Special funds under the purview of California Tax Credit Allocation Committee and the California Department of Housing and Community Development (HCD).	
^d Special funds under the purview of HCD.	
^e Transferred funds would not be repaid.	



Housing and Homelessness

(Continued)

LAO Questions for Consideration

- Are local governments able to maintain properties acquired through Project Roomkey and provide services to residents?
- Should local governments be required to use the properties acquired through Project Roomkey to serve people experiencing homelessness for a certain amount of time?
- How will the state provide oversight and assess progress of Project Roomkey?
- What are alternative uses of federal Coronavirus Relief Fund allocations to support people experiencing or at-risk of homelessness?
- Is the California Housing Financing Authority positioned to administer funds from the National Mortgage Settlement?
- What is the status of the market for state Low-Income Housing Tax Credits?
- How can the state preserve gains from recent investments in homelessness?



Employee Compensation

January Proposal

- The Governor's budget assumed that state costs to pay for state employee pay and non-retirement benefits would increase \$1.5 billion (\$660 million General Fund) to fully fund provisions included in ratified memoranda of understanding (MOUs) as well as the proposed Unit 18 (Psychiatric Technician) labor agreement. In addition, the budget set aside \$230 million General Fund in anticipation of new MOUs being ratified with seven other bargaining units with agreements scheduled to expire July 2020.

May Revision

- The May Revision includes \$609 million (\$266.8 million General Fund) to pay for anticipated increases in California Public Employees' Retirement System (CalPERS) health premiums and to provide some pay increases (for example, pay increases resulting from rising minimum wage). The May Revision suspends most pay increases in ratified agreements.
- The May Revision assumes employee compensation costs are reduced by \$2.8 billion (\$1.5 billion General Fund). This dollar amount is based on the expected savings associated with two-day-per-month furloughs. Budget bill language directs the administration to achieve these savings through the collective bargaining process, but authorizes the administration to impose cuts—up to 10 percent—if agreements are not reached by July 1, 2020. (Under the administration's proposal, these reductions would not be implemented if sufficient federal aid were received to restore these—and other—reductions.)



Employee Compensation

(Continued)

LAO Comments

- We agree that collective bargaining is preferred to imposing employee compensation reductions. The administration's approach helps to maintain employer-employee relations and reduces the risk that policies will be reversed through litigation.
- Although the savings in the May Revision are based on the estimated savings from two-day-per-month furloughs, we suggest the Legislature advise the administration and bargaining units to seek alternatives to furloughs to achieve at least some of the savings.



Pensions

January Proposal

- A number of supplemental pension payments—totaling more than \$5 billion—to CalPERS and California State Teachers’ Retirement System (CalSTRS) were authorized as part of the 2019-20 budget act to reduce state and school and community college unfunded liabilities. By reducing unfunded liabilities, these payments would reduce state and employer costs over the next few decades.
- Among the payments authorized in the 2019 budget, the state was scheduled to make payments totaling \$500 million over fiscal years 2020-21 through 2022-23 to reduce state employer pension liabilities. The Governor’s budget proposed accelerating these payments so that the full \$500 million would be paid in 2019-20.

May Revision

- The administration proposes to repurpose most of the CalPERS and CalSTRS supplemental payments to instead supplant contributions by the state and schools and community colleges. The May Revision also withdraws the \$500 million supplemental payment acceleration proposed in January and instead proposes to make—from Proposition 2 (2014)—a \$243 million supplemental payment to the California Highway Patrol pension plan, however, the administration indicates that the payment is subject to collective bargaining and may change.
- The administration also proposes to suspend CalSTRS’ ability to increase the state’s contribution rate through 2023-24. To offset the reductions, the state would make payments to CalSTRS from Proposition 2 debt payments.

LAO Comments

- The administration’s proposal achieves short-term savings for the state and schools and community colleges, but likely will result in higher costs in the future.
- Suspending CalSTRS’ ability to increase the state’s contribution rate sets a bad precedent and weakens the 2014 funding plan.



Government Reorganization and Restructuring

Department of Better Jobs and Higher Wages

- **New Department.** In January, the Governor proposed to consolidate employment, training, and data collection services provided by several entities within the Labor and Workforce Development Agency (LWDA) into a new Department of Better Jobs and Higher Wages.
- **Funding and Implementation.** The Governor's budget included budget legislation to form the new department and \$2.4 million (General Fund) in one-time resources to hire the department's executive team.
- **May Revision Withdraws Funding, but Moves Ahead With Implementation.** The May Revision proposes to withdraw funding for the new department's executive team. However, the administration included budget legislation to create the department in the May Revision. According to the administration, moving ahead with the new department is more critical now because coronavirus disease 2019 has severely impacted both jobs and wages.
- **LAO Comments.** Creating a new department is a multiyear project that requires consistent involvement by senior LWDA staff and departmental executive staff. Given the current workload at EDD related to unprecedented unemployment insurance claims—including the rapid implementation of new federal programs—it is unclear whether LWDA and departmental staff could dedicate the time and resources needed to create a new department at this time.

Cannabis Licensing Departments

- **Consolidation.** In January, the Governor expressed his intent to consolidate the cannabis-related licensing functions of the Bureau of Cannabis Control (BCC), the California Department of Food and Agriculture (CDFA), and the Department of Public Health (DPH) into a new Department of Cannabis Control starting in 2020-21.
- **Proposal Delayed.** The Governor now proposes to delay consolidation until next year.



Government Reorganization and Restructuring

(Continued)

- **LAO Comments.** We find the concept of consolidation to be promising and that delaying it is reasonable, as it will give the Legislature additional time to carefully evaluate the proposal.

Department of Business Oversight (DBO)

- **Reinvention.** In January, the Governor proposed numerous statutory changes related to DBO such as renaming it the Department of Financial Protection and Innovation and providing it with additional authority. This includes the ability to take enforcement actions against financial service providers for unfair, deceptive, or abusive acts or practices, and register providers of consumer financial services.
- **Funding and Implementation.** The Governor proposed \$10.2 million (special funds) for the new expanded department.
- **May Revision.** The Governor continues this proposal in the May Revision. However, this funding would be contingent on the Legislature adopting the statutory changes, which the administration does not anticipate occurring by the June budget deadline.
- **LAO Comments.** Given the complexity of the changes, we recommend the Legislature consider the proposal through the legislative policy process to ensure its ability to effectively scrutinize the changes. We also recommend determining the level of funding only after the policy decision has been made.

Seismic Safety Commission (SSC)

- **Transfer.** In January, the Governor proposed transferring the SSC to the Office of Emergency Services and estimated the associated cost would be \$949,000 General Fund.
- **May Revision.** The Governor continues to propose this transfer, but the estimated cost is \$446,000 lower.
- **LAO Comments.** We recommend considering delaying this decision to next year to allow for more opportunity to weigh its trade-offs. For example, while the proposal could achieve some efficiencies, it reduces SSC's independence, which has been a priority for the Legislature in the past.



Other Issues

State Office Buildings

- **Reevaluation of Office Space Needs.** The May Revision withdraws a January proposal for \$721.7 million in lease revenue bond funding for the design-build phase of the renovations of the Bateson, Jesse Unruh, and Natural Resources buildings to allow time to reevaluate office space needs. (These projects are part of a larger plan for sequencing the construction and renovation of a number of state office building projects in Sacramento.)
- **LAO Comments.** The proposed delay appears reasonable given the condition of the General Fund and the value of the proposed reevaluation, which will take into account possible changes in space needs as a result of greater telecommuting and other factors.

State Project Infrastructure Fund (SPIF)

- **Capitol Annex.** The May Revision proposes to transfer \$754.2 million from the SPIF—which was anticipated to fund the Capitol Annex project—to the General Fund and to fund the project with previously approved lease revenue bonds.
- **LAO Comments.** This change is reasonable given the General Fund condition.



Other Issues

(Continued)

Department of Consumer Affairs (DCA)

SPECIAL FUND LOANS

- The May Revision proposes to borrow \$166.7 million from nine DCA boards and bureau special funds, including those supporting (1) the Bureau of Automotive Repair (\$93.4 million), (2) the Board of Registered Nursing (\$30 million), and (3) the Board of Barbering and Cosmetology (\$25 million).
- In general, these special funds can likely support the loans in the near term. However, some leave only modest projected fund balances. In some cases, this could make it difficult for entities to support additional activities in the future. Also, there are other DCA special funds that could potentially provide loans, if the Legislature wanted to consider a different mix or level of special fund loans.

DCA FEE INCREASES

- The May Revision proposes to increase fees for five boards and bureaus (Medical, Acupuncture, Podiatric Medicine, Behavioral Science, and Private Post-Secondary Education).
- The fee increases appear necessary and are generally supported by the commissioned fee studies. However, such fee increases are typically considered through the policy process and the May Revision process provides little time for the Legislature to consider alternatives, such as whether any efficiencies could reduce the size of the increases.



Other Issues

(Continued)

Elections

- **Executive Order N-64-20.** The order requires that each county's election official send vote-by-mail ballots for the November 3, 2020 General Election to all registered voters. In-person voting opportunities would be available for certain groups of voters. The order indicated that the Governor will issue another order May 20, 2020 if counties need clarity on requirements for in-person voting opportunities.
- **May Revision.** The administration does not propose providing additional state funds to counties for elections.
- **LAO Comments.** Counties are very likely to need additional resources to conduct a predominantly vote-by-mail election in November. Specifically, among other costs, counties likely will experience increased costs related to printing and mailing ballots, equipment to process mail ballots, supplies and facilities to protect public health, and public outreach regarding voting changes. Given the revenue losses sustained by counties as a result of the pandemic-induced recession and the state's clear interest in well-administered elections, we recommend the Legislature consider providing county governments with additional funding for elections administration. These funds could be provided through low-interest loans or on a matching basis like in years past.

Veterans Homes

- **May Revision Proposal.** The administration proposes to close the Barstow Veterans Homes at a net cost of \$2.6 million General Fund in 2020-21, but annual savings of \$14 million once the closure is complete. (Under the administration's proposal, these reductions would not be implemented if sufficient federal aid were received to restore these—and other—reductions.)
- **LAO Comments.** While the proposal has merit in concept—given the facility has staffing challenges and is operating at half of capacity—the department has yet to fully engage stakeholders and develop



Other Issues

(Continued)

final facility closure and resident transfer plans. Given postponing this proposal would not forgo any savings, the Legislature could reject the proposal and instead pause admissions into Barstow and direct the department to develop a closure plan over the next year.

Other Cannabis-Related Issues

May Revision Proposals

- The May Revision provides \$148.1 million in mostly ongoing funds from the Cannabis Control Fund to BCC, CDFA, and DPH for cannabis activities. Similar to past years, the May Revision also includes budget bill language allowing for unlimited augmentations to their budgets for licensing, enforcement, and information technology subject to Joint Legislative Budget Committee notification.
- The May Revision also proposes statutory changes to shift sworn officers from DCA's Division of Investigation to BCC and delays a January proposal to change the point of collection for cannabis taxes.

LAO Comments

- Given uncertainty about the level of funding needed, we recommend providing funding for BCC, CDFA, and DPH on a one-year basis. We also recommend rejecting the proposed budget bill language, as it does not provide the Legislature with sufficient control over department budgets.
- We find it is reasonable to shift sworn officers to BCC. It is also reasonable to delay until next year changing the point of collection for cannabis taxes.



Revenue Proposals

Summary of Governor's Revenue Proposals and LAO Alternatives

(In Millions)

	2020-21		2021-22	
	DOF Estimate	LAO Estimate	DOF Estimate	LAO Estimate
Governor's Proposals				
Suspend net operating loss deductions	\$1,820	\$1,200 to \$1,500	\$1,300	\$850 to \$1,100
Limit business credits	2,000	1,300 to 1,600	1,540	1,000 to 1,300
Interaction between NOL suspensions and credit limits	611	400 to 500	454	300 to 400
Used car dealers remit sales tax with vehicle registration	12		24	
Estimated market value to calculate use tax on vehicles	30		61	
Expand first-year exemption from minimum franchise tax	-50		-100	
Extend sales tax exemption for diaper and menstrual products	—		-23	
LAO Alternatives				
Mortgage interest deduction conformity		200		400
Eliminate mortgage interest deduction for second homes		250		250
Local tax deduction conformity		350		350
Eliminate step-up on inherited assets		120		450
Eliminate first-year exemption from minimum franchise tax		60		60
Eliminate sales tax exemption for magazine subscriptions		9		11

DOF = Department of Finance and NOL = net operating loss.

