

STATE OVERSIGHT AGENCIES

fined, is subject to civil liability and criminal penalties. As amended March 26, 2001, this bill would require the State Auditor to prepare a written explanation of the Act, distribute it to each state agency, and post it on BSA's Web site. Each state agency would also be required to print and post the notice at its offices and send it by electronic mail to employees of the agency every six months.

SB 413 would also require the State Auditor to send a copy of any investigative report conducted under the Act which finds that an employee engaged in improper governmental activity to the employee's appointing power. The appointing power would then have to serve a notice of adverse action upon that employee or set forth in writing reasons for not taking adverse action. A copy of this notice of adverse action or reasons for not taking adverse action must also be provided to the State Personnel Board and the State Auditor by the appointing power.

In addition, SB 413 would repeal existing law which requires any state officer or employee filing a complaint of reprisal or retaliation to have also previously filed a complaint of improper governmental activity with the State Auditor or with the Inspector General.

A person cannot be retaliated against under the State Civil Service Act because he has opposed a practice that has been made an unlawful practice, or made a charge, testified, assisted, or participated in any manner in an investigation, proceeding, or hearing under the Act. This bill would establish that the burden of proof is on the supervisor, manager, employee, or appointing power to demonstrate by clear and convincing evidence that an alleged adverse employment action would have

occurred for legitimate, independent reasons, if a person demonstrates by a preponderance of evidence that opposing any practice made an unlawful employment practice under the act, or making a charge, testifying, assisting, or participating in any manner in an investigation, proceeding, or hearing under the act, was a contributing factor in any adverse employment action taken against him or her. Finally, SB 413 would provide that its provisions shall apply to the California State University and the University of California. [S. Appr]

ABX1 1 (Keeley), as amended January 31, 2001, is part of the state's response to the unprecedented energy crisis that began during the summer of 2000. The bill authorizes the Department of Water Resources (DWR)—until January 1, 2003—to enter into long-term contracts for the purchase of electric power and to sell that power to retail end-use customers and to local publicly owned electric utilities at not more than DWR's acquisition costs; the bill appropriates \$500 million from the general fund to DWR to purchase power. The bill also authorizes DWR to issue revenue bonds, with the authorization of the Department of Finance and the State Treasurer, to finance electricity purchases, and limits the amount that they may be issued to four times the amount of annual revenues generated from wholesale power. ABX1 1 also establishes in the State Treasury a new Department of Water Resources "Electric Power Fund," and requires all revenues payable to DWR under the bill to be deposited in the fund; and requires BSA to conduct a financial and performance audit of DWR's implementation of the bill. This bill was signed by the Governor on February 1, 2001 (Chapter 4, Statutes of 2001-02, First Extraordinary Session).

Legislative Analyst's Office

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The Legislative Analyst's Office (LAO) has been providing fiscal and policy advice to the California legislature for more than 55 years. It is known for its fiscal and programmatic expertise and nonpartisan analyses of the state's budget. Overseen by the 16-member bipartisan Joint Legislative Budget Committee (JLBC), LAO currently has a staff of 49 people. The analytical staff is divided into seven subject area groups of fiscal and policy experts.

The Office serves as the legislature's "eyes and ears" to ensure that the executive branch is implementing legislative policy in a cost-efficient and effective manner. The Office carries out this legislative oversight function by reviewing and analyzing the operations and finances of state government. Historically, one of the most important responsibilities of the LAO has been to analyze the annual Governor's Budget and publish a detailed review at the end of February. This

document, the *Analysis of the Budget Bill*, includes individual department reviews and recommendations for legis-

lative action. A companion document, *Perspectives and Issues*, provides an overview of the state's fiscal picture and identifies some of the major policy issues confronting the legislature. These documents help set the agenda for the work of the legislature's fiscal committees in developing a state budget. LAO staff works with these committees throughout the budget process and provides public testimony on the Office's recommendations.

LAO also reviews requests by the administration to make changes to the budget after it is enacted; prepares special reports on the state budget and topics of interest to the legislature; and prepares fiscal analyses of all proposed initiatives (prior to circulation) and measures that qualify for the statewide ballot.



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MAJOR PROJECTS

Health Insurance Portability and Accountability Act

In March 2001, the LAO released a report entitled *Health Insurance Portability and Accountability Act*, which analyzes federal legislation enacted in 1996 to protect health insurance coverage for workers and their families when they change or lose jobs. According to LAO, “[t]his new protection will impose additional administrative requirements on the health care industry. However, a section of the law requiring administrative simplification is designed to reduce these burdens” by accelerating the move from paper-based to electronic transactions through the establishment of national standards and requirements for the transmission, storage, and handling of certain electronic health care data. HIPAA affects not only health care providers, but also employers, insurers, and health plans, and is expected to be the most sweeping government action affecting the health care industry since the introduction of Medicare. HIPAA affects administrative policies and regulations, operational processes, education, and training and is expected to result in significant costs to implement.

HIPAA directs the U.S. Department of Health and Human Services (DHHS) to develop standards to achieve administrative simplification. These standards involve the development of national standards to allow the electronic exchange of specific health care transactions; codes to standardize certain types of health care information; unique identifier codes for health care plans, health care providers, and employers; security standards that carry out reasonable and appropriate administrative procedures and safeguards to ensure the integrity and confidentiality of patient information; and privacy standards to protect and enhance the rights of consumers, ensure the integrity of the health care system, and create a national framework for health privacy protection. DHHS plans to issue these standards in waves, starting with the first set of standards published in August 2000 which relates to transaction standards and code sets; the health care industry has until October 16, 2002 to comply with these regulations. DHHS has also released a second set of standards relating to privacy; compliance with these rules is required by February 26, 2003. According to LAO, at least seven more waves of HIPAA regulations will be issued, including national provider identifiers, national employer identifiers, security, national health plan identifiers, claims attachments, enforcement, and the national individual identifiers.

In its report, LAO summarized the requirements of HIPAA, analyzed its potential effects on state and county governments, evaluated the approach taken to date by state agencies to comply with the law, and recommended legislative actions to improve state compliance.

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LAO found that HIPAA will significantly affect the state Department of Health Services (DHS); as the agency overseeing the Medi-Cal and Healthy Families programs, DHS is the largest purchaser of health care services within the state. It will also affect many other state agencies, some of which have yet to plan for or request resources for HIPAA implementation in the 2001–02 budget. LAO noted that the 2001–02 Governor’s Budget requests a total of \$92 million for statewide planning and implementation of HIPAA. In analyzing the proposed budget, LAO found that the state has initiated significant efforts to comply with HIPAA, but that the administration’s approach has weaknesses. The report noted that the state has not designated a lead HIPAA agency and has not developed a statewide plan to address compliance efforts. According to

LAO, the proposed budget lacks the statutory framework for such a complex endeavor; further, LAO opined that the budget proposal under consideration—which proposes to fund specific HIPAA-related activities in four separate departmental budget items—would result in a fragmented funding process with a split in approval authority.

LAO recommended that the legislature approve the funding included in the 2001–02 budget to support state HIPAA compliance activities, but schedule all requested funds in one HIPAA fund budget item for such activities. LAO further recommended the enactment of legislation governing HIPAA compliance activities; designating the Health and Human Services Agency (HHS) as the lead agency; requiring HHS to develop a statewide implementation plan; requiring departments to complete HIPAA assessments to determine the impact of HIPAA compliance on department operations; limiting the terms of proposed HIPAA compliance positions; and establishing clear lines of authority over funding for this program.

Power Crisis is “Wild Card” in Budget Outlook

As part of its analysis of the 2001–02 budget bill, LAO issued a February 21, 2001 report detailing economic and demographic trends in 2001 and 2002 that are expected to have important effects on California’s budget outlook. LAO determined that the most pressing challenge currently facing the state relates to the electricity crisis which has resulted from the combination of sharply rising electricity demands, lagging investment in new generation capacity, and soaring wholesale market prices, which dramatically increased the costs of energy purchased by California’s utilities and ultimately by the State of California (see agency report on PUBLIC UTILITIES COMMISSION for a detailed discussion of this issue).

LAO noted that on February 1, 2001, the Governor signed ABX11 (Keeley), which authorizes the state Department of Water Resources to enter into long-term power contracts with electricity suppliers and resell the electricity to consumers in California. The state is also negotiating fixed-rate contracts

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with energy suppliers and an agreement aimed at helping California's investor-owned utilities regain financial stability. The Governor implemented emergency electricity orders aimed at conserving commercial electricity use. Given the recent progress by the administration and legislature in developing solutions to the crisis, LAO forecasts that the state will make it through the summer of 2001 without substantial electricity-related disruptions to the economy, but that consumers and businesses will face higher prices.

Medi-Cal Reimbursement Rates

On February 1, 2001, LAO issued *A More Rational Approach to Setting Medi-Cal Physician Rates*, a report concluding that reimbursement rates for physician services paid by the state Medi-Cal program have no rational basis.

The federal Medicaid program is administered by the California Department of Health Services (DHS) as the California Medical Assistance (Medi-Cal) program; the program provides health care services for qualifying low-income residents. LAO found that the rates paid to physicians for Medi-Cal services are low compared with the rates paid by the federal Medicare program and other health care purchasers. Unlike Medicare (which provides health care services to the elderly and to some disabled individuals), which uses a comprehensive, annually updated, ratesetting system, DHS has not conducted annual rate reviews or made periodic adjustments to Medi-Cal rates to ensure reasonable access to health care services. LAO found that rate adjustments have generally been adopted on an ad hoc basis, and not upon an assessment of the access of Medi-Cal beneficiaries to quality health care.

According to LAO, "a national study of physician rates in state Medicaid Programs by the Urban Institute found that these states, on average, paid physicians at rates equal to about 64% of Medicare rates. However, the study found that California's Medi-Cal rates were comparatively lower, amounting to an average of 47% of the Medicare rates in 1998." LAO also noted that, in 1999, the legislature enacted AB 461 (Hertzberg), which would have required DHS to conduct a rate review by April 1, 2000, including a comparison of Medi-Cal physician rates with those of Medicaid programs in five comparable states. However, Governor Davis vetoed this legislation, stating the DHS lacked the administrative resources to conduct such a rate review.

In its report, LAO recommended that the legislature establish a more rational process for periodically reviewing and adjusting Medi-Cal rates. In the short term, if the legislature wishes to continue to narrow the significant gap between Medi-Cal physician rates and the rates paid under other health programs, LAO suggested that Medicare rates be used as a benchmark. In the long term, the legislature should direct DHS to perform a comprehensive analysis of access to physician

services and the quality of care provided to Medi-Cal beneficiaries, and offer proposals commencing in 2002-03 for periodic future adjustments to physician rates based upon that analysis. LAO believes that this approach would benefit the state by potentially improving the quality of health care and ensuring that the Medi-Cal program complies with state and federal requirements to provide reasonable access to health care for Medi-Cal beneficiaries. LAO also found that these measures could lead to more efficient use of medical services, provide more fairness to medical providers by basing rates upon objective measures, and simplify the calculations of rates.

E-Government in California

In a January 24, 2001 report entitled "*E-Government in California: Providing Services to Citizens Through the Internet*," LAO evaluated California's experimentation with "e-government," a method of transacting business between government and the public by using automated systems and the Internet. LAO revealed that limited data are available to document

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the actual benefits of e-government, but identified potential benefits to its use—including lower government costs, reduced timeframes for service delivery, and streamlined government operations. Although potential benefits are apparent, LAO expressed concerns regarding (1) the lack of public input in determining the services provided; (2) the administration's failure to set statewide priorities for its various e-government projects; and (3) the failure of program staff at the department level to take "ownership" of the program that is being automated. LAO identified specific qualities the legislature should consider before approving e-government proposals. Good proposals should (1) reduce government costs or increase efficiency and/or effectiveness; (2) demonstrate public interest in and public ability to access the proposed service; (3) protect private confidential information; (4) implement reengineered processes; (5) be piloted first and operational in a short timeframe; and (6) have strong leadership and sponsorship from the state's program areas.

Although e-government is in early stages, LAO identified future issues that need to be addressed, including ensuring access, protecting information privacy, the imposition of user and credit card fees, authentication policies to ensure that government is providing services to an individual eligible to receive them, and the costs of modifying existing systems to accommodate e-government.

Implementing Proposition 36

Proposition 36, enacted by the voters in November 2000, requires that certain adult offenders convicted of nonviolent drug use or possession be sentenced to probation and drug treatment rather than prison, jail, or probation without treat-

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ment. The measure also provides \$120 million in state funds per year to counties to pay for the treatment programs.

In *Implementing Proposition 36: Issues, Challenges, and Opportunities* (December 14, 2000), LAO found that states and counties will face organizational, implementation, and funding issues in carrying out of Proposition 36. Issues identified by LAO include (1) developing methods for collaboration to ensure that key players work closely together to increase the likelihood of successful implementation; (2) assessing drug treatment capacity within counties, the needs of offenders who will be treated under Proposition 36, the gaps in the drug treatment "continuum of service," and ways to fill those gaps; (3) determining the criteria for supervising and monitoring offenders who will be in treatment, as well as deciding when to revoke their probation or parole and return them to incarceration; and (4) distributing funds provided under Proposition 36 to treat and supervise offenders in the community, and identifying other sources of funding.

According to LAO, collaboration among many different state and local agencies is the most important factor in the successful implementation of Proposition 36. LAO identified the Department of Alcohol and Drug Programs (DADP), the Board of Prison Terms, and the California Department of Corrections as the key state agencies involved in the implementation of Proposition 36. Key local agencies are the county alcohol and drug treatment agencies (frequently part of county mental or public health departments), trial courts, county probation departments, and educational, social, and health agencies. At a minimum, these key players should share information and discuss implementation plans. Although Proposition 36 did not designate an entity to oversee implementation at either the state or local level, it did envision specific roles for state and local agencies. LAO noted that the legislature may wish to consider legislation designating a lead state or county agency to take charge of implementation.

Under Proposition 36, most of the actual delivery of services will be undertaken by the counties. According to LAO, key issues that counties will face include determining the types and levels of treatment and supervision services that will be needed for the eligible population. Under Proposition 36, counties will provide drug treatment services to both eligible probationers and parole violators, probation supervision and court monitoring services to probationers, and other court-ordered services for probationers, including vocational training, family counseling, literacy training, and community service. Counties will be required to decide how to develop new or use existing assessment tools to identify the treatment needs of individual offenders, estimate the total treatment needs of the eligible population, ensure an adequate mix of treatment services to meet the needs of the population, develop a strategy to expand drug treatment capacity and fill gaps in the continuum, consider how the new treatment services will affect existing treatment programs, determine the types and levels of supervision and monitoring services for offenders, and develop qual-

ity control mechanisms to ensure that the programs they choose are delivering high-quality services to clients.

Another significant challenge relates to the general funding provisions of Proposition 36. DADP is directed to distribute \$60 million in the Substance Abuse Treatment Trust Fund (SATF) in 2000–01 fiscal year to the counties for maximum opportunity to build treatment capacity. LAO recommended that, during 2000–01, DADP use the simplest funding formulas that satisfies the basic requirements of the measure and develop more detailed distribution formulas for future years. DADP must consider two factors when developing the SATF distribution formulas: per capita arrests for controlled substances possession, and substance abuse treatment caseload within each county. LAO also recommended that DADP consider future funding formulas that provide specific incentives to counties. Additionally, counties and the state should identify other funding sources that may be available to supplement the state funds. Monetary supplements or cost-shares could be provided by offenders Medi-Cal, CalWORKs, and/or community college or adult education programs. Not only will these supplements increase the number of individuals affected, but they will preclude counties from determining that the SATF is insufficient to provide the treatment and supervision services necessary under the measure.

According to LAO, "Proposition 36 poses significant challenges to policymakers and state and local criminal justice and treatment practitioners. At the same time, it provides substantial opportunities to the state and counties to move to a different approach to handling criminal offenders with drug problems, consistent with the direction of voters. Research indicates that treatment of these offenders can, but certainly, does not always, succeed at reducing future criminality. Successful implementation will require a focused effort and close monitoring."

2000 LEGISLATION

AB 1727 (Reyes), as amended August 25, 2000, extends the Rural Crime Prevention Program until January 1, 2002 and extends the date for the Legislative Analyst to evaluate and submit a cost-benefit analysis of the Program from December 31, 2000 to December 31, 2001. The Governor signed this bill on September 2, 2000 (Chapter 310, Statutes of 2000).

AB 2831 (Alquist), as enrolled August 29, 2000, would have established the California Commission on Restructuring School Finance for Kindergarten and Grades 1 to 12 to propose simple, flexible, and workable funding programs that would enable schools to meet the special needs of individual pupils. The bill also would have required the Legislative Analyst to conduct a study of public school financing. Governor Davis vetoed AB 2831 on September 22, 2000.

SB 1710 (Hayden), as enrolled August 30, 2000, would have enacted the "2000 Public Subsidies, Public Benefits Act," and required LAO to complete reviews of the economic and employment impacts of selected state business tax expendi-

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tures and selected public subsidies. Governor Davis vetoed SB 1710 on September 23, 2000, saying that this bill would impose significant administrative costs for the Franchise Tax Board.

AB 1378 (Dutra), as amended August 18, 2000, would have authorized the creation of a pilot program for up to four school districts to demonstrate alternative means by which school facilities may be constructed to meet operational efficiency and educational improvement objectives. The bill would have required the Legislative Analyst to assess the pilot program and report to the legislature, Governor, and others by March 1, 2005. However, the Governor vetoed the bill on September 26, 2000, saying, "Other than requiring a re-

port from the Legislative Analyst's Office, this bill does nothing that could not be done under existing law."

AB 945 (Maldonado) would have required LAO to conduct a study to determine what entity is fiscally responsible for providing specialized health care services to pupils with exceptional needs. As amended June 26, 2000, however, the bill is no longer relevant to LAO.

2001 LEGISLATION

AB 1107 (Leach), as introduced February 23, 2001, would, among other things, delete requirements that the Department of Education and/or school districts submit certain reports to LAO. [A. *Appr*]

Little Hoover Commission

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The Little Hoover Commission (LHC), more formally known as the Milton Marks Commission on California State Government Organization and Economy, was created by the legislature in 1961 and became operational in the spring of 1962 (Government Code section 8501 *et seq.*). In 1993, LHC was renamed in honor of former Senator Milton Marks, who authored the legislation originally creating the Commission. Although considered to be within the executive branch of state government for budgetary purposes, state law provides that the Commission "shall not be subject to the control or direction of any officer or employee of the executive branch except in connection with the appropriation of funds approved by the Legislature" (Government Code section 8502).

The Commission's enabling act provides that no more than seven of its thirteen members may be from the same political party. The Governor appoints five citizen members, and the legislature appoints four citizen members. The balance of the membership is comprised of two Senators and two Assemblymembers. This unique formulation enables LHC to be California's only truly independent watchdog agency. However, in spite of its statutory independence, the Commission remains a purely advisory entity only empowered to make recommendations.

The Commission's purposes are to promote economy, efficiency, and improved service in the transaction of public business in the various departments, agencies, and instrumentalities of the executive branch of the state government; and to make the operation of state departments, agencies, and instrumentalities and all expenditures of public funds more directly responsive to the wishes of the people.

The Commission seeks to achieve these ends by conducting studies and making recommendations as to the adoption of methods and procedures to reduce government expenditures, the elimination of functional and service duplication, the abolition of unnecessary services and functions, the definition or redefinition of public officials' duties and responsibilities, and the reorganization or restructuring of state entities and programs. The Commission holds hearings about once a month on topics that come to its attention from citizens, legislators, and other sources.

MAJOR PROJECTS

Mental Health System Reforms

In *Being There: Making a Commitment to Mental Health* (November 2000), LHC examined the mental health system in California and questioned why so many people in need of mental health services do not have access to care. A generation ago, California shifted from a policy of institutionalizing persons with mental illness to allowing them to live in their communities. According to LHC, however, "[i]t is painfully clear that we have failed to follow through with all that was required

by this noble decision." Those who suffer from mental illness represent a disproportionate number of people who are homeless, jobless, or in jail. An estimated 1.5 million Californians who are in need of mental health care are not receiving it.

LHC identified four core areas of reform needed to improve California's response to mental illness: (1) raising public

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