



INTERNAL GOVERNMENT REVIEW AGENCIES

portion of the APA (not just the article setting forth rulemaking procedures) applies to the exercise of all quasi-legislative power conferred on a state agency by statute; delete a provision regarding Fair Political Practices Commission regulations to conform the statute to a judicial ruling; delete an obsolete reference to publishing notice of regulations in a newspaper; and make technical conforming changes. [S. GO]

SB 2104 (Leslie), as introduced February 25, would require the Department of Fish and Game (DFG) and the state Water Resources Control Board (WRCB), in addition to any other requirements contained in the APA, to hold at least one public hearing, in accordance with prescribed procedures, at which oral or written presentations may be made prior to adopting a new or increased fee for specified services. The bill would also prohibit DFG and WRCB from adopting a new or increased fee in an amount that exceeds the amount required to provide the service for which the fee is proposed to be adopted, and if, after an annual review, the new or increased fee is found to create revenue in excess of the actual cost required to provide the service for which the fee was adopted, DFG or WRCB would be required to adjust the fee to a level determined not to exceed the actual cost of providing the service. [A. CPGE&ED]

AB 3412 (Conroy), as amended May 16, would revise the APA to permit a small business, as defined, to elect to arbitrate a decision adopted by an agency after hearing, as specified, in lieu of the procedure for judicial review. [A. CPGE&ED]

The following is a status update on bills reported in detail in CRLR Vol. 14, No. 1 (Winter 1994) at page 15:

AB 1807 (Bronshvag), as amended March 23, authorizes regulatory agencies within the Department of Consumer Affairs to provide required written notices, including rulemaking notices, orders, or documents served under the APA, by regular mail. This bill was signed by the Governor on March 30 (Chapter 26, Statutes of 1994).

SCA 6 (Leonard), as amended February 16, 1993, would authorize the legislature to repeal state agency regulations, in whole or in part, by the adoption of a concurrent resolution. SCA 6, which would not be applicable to specified state agencies, would require the concurrent resolution to specify the regulation to be repealed or specific references to be made, as indicated, and would subject those resolutions to the same procedural rules as those required of bills. The measure would also require every regulation to include a citation to the

statute or constitutional provision being interpreted, carried out, or otherwise made more specific by the regulation. [S. RIs]

The following bills died in committee: **AB 64 (Mountjoy)**, which, as amended January 3, would have prohibited any regulation adopted, amended, or repealed by a state agency on or after January 1, 1995 and affecting emission and reporting requirements for air, water, and solid waste from taking effect unless and until the regulation is approved by statute; and **AB 633 (Conroy)**, which, as amended January 3, was no longer relevant to OAL.

BUREAU OF STATE AUDITS

State Auditor: Kurt Sjoberg
(916) 445-0255

Created by SB 37 (Maddy) (Chapter 12, Statutes of 1993), the Bureau of State Audits (BSA) is an auditing and investigative agency under the direction of the Commission on California State Government Organization and Economy (Little Hoover Commission). SB 37 delegated to BSA most of the duties previously performed by the Office of Auditor General, such as examining and reporting annually upon the financial statements prepared by the executive branch of the state, performing other related assignments (such as performance audits) that are mandated by statute, and administering the Reporting of Improper Governmental Activities Act, Government Code section 10540 *et seq.* BSA is also required to conduct audits of state and local government requested by the Joint Legislative Audit Committee (JLAC) to the extent that funding is available. BSA is headed by the State Auditor, appointed by the Governor to a four-year term from a list of three qualified individuals submitted by JLAC.

The Little Hoover Commission reviews reports completed by the Bureau and makes recommendations to the legislature, the Governor, and the public concerning the operations of the state, its departments, subdivisions, agencies, and other public entities; oversees the activities of BSA to ensure its compliance with specified statutes; and reviews the annual audit of the State Audit Fund created by SB 37.

MAJOR PROJECTS

BSA Reviews FTB and BOE Settlement Programs. In 1992, the legislature enacted statutes authorizing the Franchise Tax Board (FTB) and the Board of Equalization (BOE) to resolve tax disputes for fiscal year 1992-93 through separate tax

settlement programs. BOE's settlement program permits the Board to settle sales and use tax disputes which existed on July 1, 1992; the purpose of the BOE settlement program is to eliminate the time-consuming and costly litigation of tax issues in which neither the taxpayer nor the Board is entirely confident of winning in court. FTB's program empowers it to settle income tax disputes without having to resort to lengthy and expensive court battles; it is designed to encourage the speedy resolution of outstanding tax disputes through a voluntary program in which the taxpayer and the FTB would consider the expected value of taxes, the expense of the protest, appeals, and litigation processes, and the value each party places on paying money sooner than later.

On March 17, BSA released reports reviewing both settlement programs. In both cases, BSA determined that the settlement programs are more efficient and as effective as the boards' other alternatives for resolving such disputes. For example, for bank and corporation taxpayers, the FTB's 1992-93 settlement program resolved 99 cases in an average of three months, as compared to an average ranging from 36-46 months in each of the FTB's three other administrative tax dispute resolution processes; the program also reduced expenses incurred by the state and by taxpayers while at the same time sustaining taxes at rates comparable to the other processes.

According to BSA, BOE's program also shortens the normally lengthy tax dispute resolution process. Specifically, BOE's settlement program resolved 94 cases in fiscal year 1992-93 in an average of nine months, as compared with a range of 7-46 months on average during the same period in the Board's other administrative appeals processes. BSA also noted that the program creates a better working relationship between the Board and taxpayers when tax disputes arise, and also generally sustains taxes at rates comparable to the other processes BOE uses to resolve tax disputes.

BSA Reviews CYA and CDC Reports on Workers' Compensation Early Intervention Programs. On January 11, BSA released its review of reports submitted by the California Youth Authority (CYA) and the California Department of Corrections (CDC) on their early intervention pilot programs for workers' compensation injuries. CYA and CDC currently operate pilot programs which seek to ensure that parties involved in workers' compensation programs are fully informed of available options and that decisions on compensation for injured em-



ployees are reached and implemented quickly; the goal of the programs is to minimize the potential financial and personnel losses to the two departments by taking steps to return injured employees to work as soon as possible or identify those employees who will not be able to return to their regular jobs.

BSA's report focused on a review of the reports provided by the two departments; BSA examined the reports for accuracy of data, completeness, and compliance with statutory mandates. Among other things, BSA noted that events other than the 1989 implementation of the early intervention program, such as the passage of major workers' compensation legislation in 1989 and 1993, are currently blurring CDC and CYA attempts to measure the effectiveness of early intervention. BSA also found that CDC and CYA were unable to report on certain data requested by the legislature because no mechanism currently exists to effectively collect the data requested; some of the data presented by CYA and CDC do not completely conform to statutory requirements; BSA was unable to validate the accuracy of some of the source data used by both departments in compiling their reports; and some of the data reported by the two departments were not accurate.

In light of its findings, BSA recommended that the legislature defer further attempts to evaluate the accomplishments of the early intervention pilot programs until sufficient time has elapsed to accumulate meaningful data unaffected by competing workers' compensation legislation.

BSA Continues Review of Medi-Cal Drug Treatment Authorization Requests. On February 1, BSA released the sixth in a series of semiannual reports concerning how the Department of Health Services (DHS) processes reimbursement requests for certain prescribed drugs under the Medi-Cal program; these reports review DHS' process for counting and compiling data on drug treatment authorization requests (TARs) received and processed from June 1990 through November 1993. [14:1 CRLR 15; 12:4 CRLR 36; 12:2&3 CRLR 44; 11:4 CRLR 48; 11:2 CRLR 45]

BSA noted that DHS received approximately 141,200 drug TARs from June 1993 through November 1993, representing an increase of more than 30% since December 1992 through May 1993; according to BSA, the increase in the number of drug TARs received may have occurred partly because of a 35% increase since June 1990 in the number of Medi-Cal beneficiaries eligible to obtain drugs through Medi-Cal and changes in Medi-

Cal's list of contract drugs. BSA noted that from June 1993 through November 1993, DHS processed approximately 87% more drug TARs than it did during the first six months of its review. DHS reduced its total backlog of drug TARs from a high of 33,800 TARs for the six-month period of December 1992 through May 1993 to 7,194 TARs for the six-month period of June through November 1993, largely due to the addition of staff, including two full-time pharmacist consultants and nine outside contract pharmacist consultants. During June through November 1993, DHS' average time for processing mailed drug TARs met the five working days requirement mandated by state law, primarily because DHS redistributed the processing of mailed-in drug TARs to both the Los Angeles and Stockton offices and increased its staffing.

BSA also sampled drug TARs received by fax and DHS' audio response telephone system (Voice Drug TAR System or VDTs) to determine if DHS was processing these TARs within 24 hours of receipt, as required by federal law. Based on a sample of 38 drug TARs received by fax during June 1993 in the Stockton office, BSA found DHS in compliance with the 24-hour requirement. In Los Angeles, 98% of a sample of 131 drug TARs received by VDTs were processed within 24 hours; in addition, 99% of a sample of 124 drug TARs received by fax were processed within 24 hours.

BSA Determines That DOI Cannot Identify Its Costs for Implementing Proposition 103 and Performing Examinations. On April 6, BSA released its financial audit assessing whether certain fees levied by the Department of Insurance (DOI) under Insurance Code sections 12979 and 736 were based on DOI's actual costs of enforcing Proposition 103 and conducting examinations of insurance companies. The audit also reviewed whether the actual costs of Proposition 103 implementation and DOI's examination activities exceeded the revenues from the fees or whether the fees exceeded the costs. The audit focused on fiscal year 1992-93.

BSA reported that although DOI could separately identify revenues from fees collected to cover the costs of implementing Proposition 103, DOI could not separately identify the associated costs of enforcement. Further, DOI was unable to document the costs of its examinations of insurance companies. According to BSA, DOI did not design its accounting system to distinguish the expenditures for Proposition 103 from the costs of performing other regulatory activities; further, DOI

could not provide a reliable alternative methodology for identifying Proposition 103 costs.

BSA determined that because DOI could not identify the costs related to the enforcement of Proposition 103 and its examination of insurance companies, DOI may be overcharging or undercharging insurance companies for Proposition 103 examinations. BSA noted that, overall, DOI has collected more in revenues for operations than it has needed to cover operating costs. In fact, DOI had sufficient resources not only to pay for the costs of its regulatory activities, but also to lend over \$20 million to other funds during fiscal year 1992-93.

BSA Reviews Veterans Home of California Activities. On April 19, BSA released its report reviewing the policies and procedures of the state Department of Veterans Affairs (DVA) to maximize fees paid by residents of the Veterans Home of California and evaluating DVA's efforts to exhaust all sources of reimbursements from both the residents and the federal government. The Veterans Home in Yountville provides long-term residential care for aged and/or disabled war-time veterans. To offset costs, state law permits the home to collect revenue from the residents (based on a percentage of the residents' income) and to receive reimbursements from the federal government and other third parties. BSA noted four main deficiencies which may have resulted in lost revenues:

- By not implementing adequate procedures and adopting policies to recover all possible fees, the Veterans Home has not maximized revenue from residents.

- The Veterans Home does not have the authority to collect the state-funded cost of care provided to residents who leave the home to live somewhere else.

- By not implementing adequate policies and procedures to recover all possible reimbursements, the Veterans Home has not maximized reimbursements from the federal government.

- The Veterans Home could have received \$446,000 annually in aid and attendance allowances if the federal Department of Veterans Affairs determined that 95 residents had been eligible to receive the allowances and if the Veterans Home had obtained the statutory authority to receive the allowances for all veterans, including those with dependents.

BSA Reviews DOI's Conservation and Liquidation Division. In May, BSA released a report on its review and evaluation of the operations of the Department of Insurance's (DOI) Conservation and Liquidation Division. Specifically, BSA



INTERNAL GOVERNMENT REVIEW AGENCIES

reviewed the Division's operations concerning management of conserved insurance companies, personnel practices, contracting, allocation of costs to conserved companies, disposition of assets, and claims processing. This report follows a 1992 audit which evaluated DOI's regulatory practices aimed at early detection of problems that can lead to an insurer's insolvency. [12:4 CRLR 38, 147]

BSA explained that the Division is responsible for conserving and liquidating insurance companies that experience financial or other problems or that are not authorized to transact business in California. During conservation, an insurance company is placed under court-ordered control to conserve the insurer's assets until the insurer's status is determined. If the Insurance Commissioner determines that it would be futile to rehabilitate the insurer in conservation, he/she may apply to the court for an order to liquidate the assets of the conserved insurer. After the Division has liquidated a conserved insurer's assets, the Commissioner must apply for another court order to distribute the liquidated insurer's assets to its policyholders, creditors, and other groups in the order required by the Insurance Code; after final distribution of the assets takes place and the Division makes a declaration of that fact to the court, the closure of the insurer is complete.

BSA stated that its audit, which focused on the operation of the Division between 1991 and 1993, revealed a series of improper decisions by former Division managers which, in several instances, led to the expenditure of Division funds on questionable items. BSA's audit also disclosed lax procedures or no established procedures for important aspects of the Division's operation, including the identification of new employees to work in the Division, the administration of employees' salaries, the amount of overtime worked by Division employees, and proper disposal of assets of liquidated insurers. Specific findings of BSA include the following:

- Forty-two of the 76 estates with court-ordered liquidations are still not closed, even though three to fifteen years have elapsed since the court order.

- The Division's payroll grew rapidly between 1991 and 1993 (a 57% increase from 1991 to 1992 and another 57% increase from 1992 to 1993); according to BSA, the salary rates of Division employees outpaced the salary rates of comparable positions in the insurance industry and in the public sector.

- Between 1991 and 1993, the Division's payments for overtime increased by more

than 400%, which the Division attributed to an increase in the number of insurer conservations, estate closures, and insurer insolvencies, and efforts to improve controls over Division operations.

- In June 1993, two former Division managers paid approximately \$72,000 in net severance payments to 26 employees, even though these employees never severed their employment with the Division. In November 1993, the Division informed all of these employees that the payment they received was improper and requested that the employees return the payment; according to BSA, only \$9,000 of the \$72,000 has been repaid thus far.

- According to BSA's interviews with Division employees, vacant positions within the Division were advertised primarily by word of mouth, and most of the employees who were hired formerly worked for failed insurance companies.

- The Division did not always attempt to obtain competitive bids before awarding contracts, nor did it always write all of the essential provisions into its contracts.

- In 1992 and 1993, the Division allowed its employees and consultants, as well as their friends and families, to purchase the assets of liquidated insurers, posing a conflict of interest.

BSA noted that DOI has taken steps to address most of the problems identified in the audit; for example, DOI terminated the employment of the Division's general manager and demoted the Division chief to a position elsewhere in the Department. Also, the Division has adopted new procedures covering its essential activities, including compensation of Division employees; selecting, managing, and paying outside consultants and law firms; disposing of the assets of liquidated insurers; and creating an operating budget for the Division each year. However, BSA opined that DOI needs to do more to remedy the shortcomings of the Division; for example, an area of primary importance is for the Division to create a strategic plan that will enable it to better prioritize its workload into the foreseeable future.

Other BSA Reports. BSA has released several other reports since January 1, including the following: *Department of Health Services' Licensing and Certification Program Performance Audit* (January 1994); *Employees of the University of California, San Diego, Misappropriated Public Funds For Personal Profit And Falsified Documents To Make Other Improper Payments* (January 1994); *A Review of the State's Bond Sales for 1991 and 1992* (January 1994); *Investigative Activity Report and Public Reports of Investigations Completed by the Bureau*

of State Audits from May 7 Through December 31, 1993 (February 1994); *A Review of the State's Allocations and Expenditures of the Additional Transportation Funds Made Available by the 1989 Transportation Blueprint Legislation* (March 1994); *A Review of Caltrans' Management of the Contract With Morrison Knudsen Corporation for the Design and Construction of Railcars* (March 1994); *State of California Statement of Securities Accountability of the State Treasurer's Office June 30, 1993* (March 1994); *Review of the Implementation, Administration, and Plans for Termination of the California Residential Earthquake Recovery Program* (April 1994); *The State's Contributions to the Public Employees' Retirement System and the State Teachers' Retirement System* (April 1994); and *An Analysis of the State's Compliance With Requirements for Consultant Contracts* (April 1994).

LEGISLATION

SB 1989 (Marks). Existing law requires the State Auditor, among other things, to examine and report annually upon the financial statements prepared by the executive branch of the state and to perform other related assignments, including performance audits, that are mandated by statute. As amended May 16, this bill would require the State Auditor, by March 1, 1995, to prepare a specified report that recommends to the legislature the scope and approach to conduct a statewide performance review. [S. Appr]

AB 2711 (V. Brown). Existing law requires the Department of Finance (DOF) to develop a performance budgeting pilot project, in accordance with specified principles, involving at least four state departments, to be implemented during the 1994-95 fiscal year, for the purposes of improving the delivery of governmental services through the use of strategic planning and performance measurement. As amended May 17, this bill would enact the State Government Performance Review Act that would require the Controller, DOF, and BSA, in consultation with the Legislative Analyst, to develop a plan for conducting performance reviews of all state agencies, as specified, and to conduct these reviews of at least three state agencies; require the Controller, DOF, and BSA to report, within a specified time, to the Joint Legislative Audit Committee regarding the steps taken to formalize the working relationship between these reviewing agencies in order to achieve the above objectives; require the Controller, DOF, and BSA to file a joint report with the legislature containing specified infor-



mation by January 31, 1995, and each January 31 thereafter, until the performance reviews of all state agencies have been completed; and require reviewed state agencies to file supplementary reports with the legislature containing prescribed information. [A. Floor]

COMMISSION ON CALIFORNIA STATE GOVERNMENT ORGANIZATION AND ECONOMY (LITTLE HOOVER COMMISSION)

Executive Director:
Jeannine L. English
Chair: Richard Terzian
(916) 445-2125

The Little Hoover Commission (LHC) was created by the legislature in 1961 and became operational in the spring of 1962. (Government Code sections 8501 *et seq.*) Although considered to be within the executive branch of state government for budgetary purposes, the law states 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.)

Statute provides that no more than seven of the thirteen members of the Commission 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 the Commission 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 purpose and duties of the Commission are set forth in Government Code section 8521. The Code states: "It is the purpose of the Legislature in creating the Commission, to secure assistance for the Governor and itself in promoting economy, efficiency and improved service in the transaction of the public business in the various departments, agencies, and instrumentalities of the executive branch of the state government, and in making the operation of all state departments, agencies, and instrumentalities and all expenditures of public funds, more directly re-

sponsive to the wishes of the people as expressed by their elected representatives...."

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, programs and functions, the definition or redefinition of public officials' duties and responsibilities, and the reorganization and 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.

In early March, Nathan Shapell announced that he was stepping down as Chair of the Little Hoover Commission; Shapell, who will serve out his current term on the Commission, has been a member of the Commission for 25 years, 18 of which he has served as Chair. Richard Terzian, who served as Vice-Chair under Shapell, replaced Shapell as the Commission Chair.

MAJOR PROJECTS

Putting Violence Behind Bars: Redefining the Role of California's Prisons (January 1994) is but one of several studies of various aspects of crime recently released by California research and oversight agencies, and reflects the importance of crime as an issue in the 1994 election year. (See reports on SENATE OFFICE OF RESEARCH and OFFICE OF THE LEGISLATIVE ANALYST for summaries of related studies.)

The Little Hoover Commission's study focuses on "the tail-end of the anti-crime machine"—the state prison system. In its study, LHC focused on three elements: (1) the sentencing structure, which determines who will be placed in prison and for how long; (2) prisons programs, "the single best chance the system has to affect the 90% of prisoners who are released back to the streets"; and (3) operational problems in the Department of Corrections, the agency that runs the second-largest prison system in the world. The Commission made seven major findings:

- The sentencing system is complex and inequitable, frustrating the public's desire for consistency and certainty.
- The degree to which the present criminal justice system distinguishes between violent and non-violent offenders is not sufficient to protect the public and maintain the credibility of the system.
- The present parole system is not structured as an effective deterrent to criminal behavior.

- The effectiveness of prison work programs is hampered by the absence of statutory direction and lack of a unified management structure.

- The Department of Corrections' education program is neglected, unfocused, and poorly structured.

- The Department's longstanding practice of allowing each prison to operate independently has hindered accountability for performance and hampered standardization of policies, leaving the state open to charges of mistreating prisoners.

- The Department is prevented in some instances from operating effectively, efficiently, and safely.

LHC also advanced over thirty recommendations to address these findings, including the following:

- The Governor and legislature should create a sentencing commission and charge it with developing a new sentencing structure which meets the philosophical goals of the criminal justice system: protecting the public safety, tailoring the punishment to the crime, addressing the needs of victims, fostering responsibility in inmates, and balancing costs with benefits. The new system should be insulated from politically motivated, piecemeal tampering, and should be monitored regularly by the commission.

- The Governor and legislature should shift the demarcation between indeterminate and determinate sentencing so that all or most violent crimes fall under a sentencing structure that ensures inmates are regularly evaluated, with the severity of their crime, their behavior in prison, and their future prospects linked to their release date.

- The Governor and legislature should enact parole reform that will provide a greater deterrent to continued criminal activity by parolees, including (a) structuring the work-credit system so that the time earned off a sentence is suspended rather than eliminated, and then is re-imposed if parole is violated; and (b) lengthening the maximum parole violation sentence to longer than one year for violent crimes.

- The Governor and legislature should reinstate rehabilitation as a goal of the corrections system, and specifically target populations most likely to benefit; and enact legislation that establishes a single, unified structure within the Department of Corrections for all work programs, including the Prison Industry Authority.

- The Department of Corrections should restructure its education program, either by creating a correctional school district or by creating a superintendent of correctional education and placing that person in a top policymaking role.