



**The *Reporter* summarizes below the activities of those entities within state government which regularly review, monitor, investigate, intervene, or oversee the regulatory boards, commissions, and departments of California.**

## OFFICE OF ADMINISTRATIVE LAW

Director: John D. Smith  
(916) 323-6221

The Office of Administrative Law (OAL) was established on July 1, 1980, during major and unprecedented amendments to the Administrative Procedure Act (APA) made by AB 1111 (McCarthy) (Chapter 567, Statutes of 1979). OAL is charged with the orderly and systematic review of all existing and proposed regulations against six statutory standards—necessity, authority, consistency, clarity, reference, and nonduplication. The goal of OAL's review is to "reduce the number of administrative regulations and to improve the quality of those regulations which are adopted...." OAL has the authority to disapprove or repeal any regulation that, in its determination, does not meet all six standards. OAL is also authorized to review all emergency regulations and disapprove those which are not necessary for the immediate preservation of the public peace, health and safety or general welfare. The regulations of most California agencies are published in the California Code of Regulations (CCR), which OAL is responsible for preparing and distributing.

Under Government Code section 11347.5, OAL is authorized to issue determinations as to whether state agency "underground" rules which have not been adopted in accordance with the APA are regulatory in nature and legally enforceable only if adopted pursuant to APA requirements. These non-binding OAL opinions are commonly known as "AB 1013 determinations," in reference to the legislation authorizing their issuance.

### MAJOR PROJECTS

**OAL Rulemaking Update.** On June 22, OAL approved new section 4, Title 1 of the CCR, to implement SB 726 (Hill) (Chapter 870, Statutes of 1993). [14:2&3 CRLR 11; 14:1 CRLR 14; 13:4 CRLR 16]

Section 4 requires state agencies proposing rulemaking actions that affect small business to adopt a plain English policy statement overview of the regulation. Among other things, section 4 requires an agency adopting such a regulation to prepare and submit to OAL with the notice of proposed action either the express terms of the proposed action written in plain English or, if that is not feasible due to the technical nature of the regulation, a noncontrolling plain English summary of the regulation; requires the agency to include in the rulemaking file either a statement that the agency has drafted the regulation in plain English, or a statement confirming that the agency has determined that it is not feasible to draft the regulation in plain English and a noncontrolling plain English summary of the regulation; and requires agencies which have determined that a proposed regulatory action does not affect small business to include "a brief explanation of the reason(s) for the agency's determination."

### LEGISLATION

The following is a status update on bills reported in detail in CRLR Vol. 14, Nos. 2 & 3 (Spring/Summer 1994) at pages 11-12:

**AB 2531 (Gotch)**, as amended June 28, revises and reorganizes specified provisions of the APA. Among other things, AB 2531 changes the name of the rulemaking portion of the APA from "Office of Administrative Law" to "Administrative Regulations and Rulemaking"; reorganizes, consolidates, and renumbers articles and sections of the APA; reorganizes the procedural requirements of the APA; consolidates all provisions on assessing the impact of proposed regulations on business and the economy; clarifies existing law to provide that the rulemaking 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; deletes a provision regarding Fair Political Practices Commission regulations

to conform the statute to a judicial ruling [12:2&3 CRLR 44; 11:2 CRLR 44]; deletes an obsolete reference to publishing notice of regulations in a newspaper; and makes technical conforming changes. This bill was signed by the Governor on September 29 (Chapter 1039, Statutes of 1994).

The following bills died in committee: **AB 3674 (Johnson)**, which would have—among other things—required all state agencies proposing to adopt or amend any administrative regulation to estimate the cumulative impact of all regulations on specific private sector entities that may be affected by the proposed adoption or amendment of the regulation, and to include this estimate in the notice of proposed action; **SB 2104 (Leslie)**, which would have required 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, and prohibited 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; **AB 3412 (Conroy)**, which would have revised 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; and **SCA 6 (Leonard)**, which would have authorized the legislature to repeal state agency regulations, in whole or in part, by the adoption of a concurrent resolution.

## 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

**The Department of Motor Vehicles and the Office of Information Technology Did Not Minimize the State's Financial Risk in the Database Redevelopment Project** (August 1994) is BSA's review of DMV's implementation of its Database Redevelopment Project. DMV initiated the Project in 1987 to redesign its systems and databases to meet all existing requirements and functions, structure the system to be more responsive to future changes, and improve the efficiency of electronic data processing (EDP) services. However, BSA's audit indicates that as early as 1989, DMV became aware that it needed to resolve significant technical problems related to the system's response time and its transitional architecture before it could be assured of the Project's success; and DMV continued its efforts to fully implement the Project despite the significant unresolved problems and deficiencies, which led to the ultimate failure of the Project in 1994. BSA's audit also revealed that the Office of Information Technology (OIT), the state's information technology oversight body, continued to recommend additional funding for the Project despite the fact that DMV had not followed approved policies to minimize financial risk to the state. Also, BSA found that DMV's actual and obligated costs were \$5.1 million higher for the Project than were originally reported to the legislature and the Department of Finance, and that the DMV violated numerous contracting laws and regulations, including falsifying a purchase order for approximately \$46,000. Other BSA findings include the following:

- DMV progressed beyond the developmental stages of the Project even though it had failed to accomplish the

objectives of each stage and had not resolved significant technical problems encountered during the developmental process; in its unsuccessful attempt to implement the Project, DMV spent an additional \$34.6 million.

- DMV did not use a formal cost reporting system to monitor expenditures related to the Project.

- DMV did not always adequately justify its use of sole-source consulting contracts for the Project.

- From November 1987 to November 1991, DMV allowed contractors to begin work before the Department of General Services (DGS) approved the contracts or contract amendments; additionally, DMV significantly modified one contract without obtaining DGS' approval.

As a result of its findings, BSA recommended that DMV complete the milestones it establishes for the development of new EDP systems; conduct sufficient testing and analysis to determine that proposed systems will achieve their projected benefits, both monetary and programmatic; and ensure that technical problems identified during quality assurance reviews of such systems are resolved before continuing to devote resources to those projects. BSA also recommended that DMV implement a standard cost reporting system for all EDP projects; obtain approval from the Department of Finance if it expects to deviate by more than 10% from its approved level of funding for EDP projects; follow all contracting laws and regulations when awarding contracts; and consider taking disciplinary action against the employees involved in falsifying the purchase order. Finally, BSA recommended that OIT exercise its authority to approve proposed expenditures for EDP projects only if established policies and procedures have been met and followed; and ensure that departments accomplish the objectives and requirements included in approved feasibility study reports and special project reports before allowing projects to move forward.

**A Review of the Department of Education's Cost and Development of the California Learning Assessment System (CLAS)** (August 1994) analyzes the Department of Education's (DOE) implementation of a statewide system to assess students' progress and abilities. SB 662 (Hart) (Chapter 760, Statutes of 1991) directed the Board of Education and DOE to develop and implement an assessment system which would have, as its primary purpose, the improvement of instruction in California's public schools. In response to this directive, DOE began to develop a comprehensive, statewide assessment

system with various components, including the CLAS exam which tests the specific content areas of reading, written expression, mathematics, science, history, and social sciences. SB 662 appropriated approximately \$9.3 million to DOE during fiscal year 1991-92 for the development and implementation of the CLAS exam; for fiscal years 1992-93 and 1993-94, the legislature appropriated additional funding of approximately \$14.8 million and \$25.9 million, respectively. However, BSA notes that in the 1994-95 budget bill, Governor Wilson eliminated additional funding for CLAS with the intention that the funds be set aside until legislation is enacted to reform the testing process; the 1994-95 budget bill also renamed CLAS as the California Comprehensive Testing Program.

BSA conducted its audit to review DOE's process for developing items for the CLAS exam; determine whether DOE complied with state laws and regulations when it awarded contracts for developing and implementing the CLAS exam; and report on the nature and amount of funds expended for the CLAS exam from January 1992 through May 1994 and determine the appropriateness of those expenditures. Among other things, BSA's audit reported the following findings:

- DOE used various groups to develop the CLAS exam, including advisory committees, development teams, and review panels; this development framework was similar to the process followed by DOE in earlier exams.

- DOE used its contract with Far West Laboratory for Educational Research and Development to circumvent the state's civil service system. According to BSA, DOE obtained the services of 28 employees who were not civil service employees but who worked at DOE and were in some cases supervised by state employees.

- DOE has not exercised adequate control over its contract expenses for the CLAS exam. For example, BSA contends that DOE paid travel costs to Far West and the county offices of education for Sacramento and Los Angeles that exceeded the maximum reimbursement rates allowable by state rules, resulting in approximately \$14,000 in excess expenditures. Also, BSA stated that DOE did not require contractors to submit written progress reports to support monthly invoices, incorrectly calculated retention amounts, and issued a duplicate payment for one invoice.

- DOE appropriately used a competitive bidding process to award the CLAS contracts to three private companies and three county offices of education; however, for three contracts and three inter-



agency agreements reviewed by BSA, the contractor performed work or provided services before approval of the contract. By doing so, according to BSA, DOE exposed the state to potential monetary liability for work performed if the contract has not been approved.

BSA stated that if the program's funding is restored, DOE should develop and follow standard written procedures to ensure that the methods used to recruit and select new members of the advisory committees, development teams, and review panels are fair and consistent and that the committees and teams represent the diversity of California's population. To ensure that it does not circumvent the state's civil service system, BSA suggested that DOE discontinue its use of a fiscal agent to obtain contract employees; submit a budget change proposal to the Department of Finance requesting that civil service positions be funded with existing resources; and recruit and hire civil service employees for clerical, consultant, research associate, and production specialist positions. To ensure that its expenditures for contracts are appropriate and reasonable, BSA recommended that DOE review invoices that it has already paid and recover all travel costs that exceed the state's reimbursement costs; review all future invoices before payment to ensure that payments for travel costs do not exceed the state's reimbursement rates; require its contractors to submit written progress reports along with invoices for payment; and strengthen its controls to ensure that it withholds the correct amounts from progress payments and that duplicate payments are not made. Finally, BSA recommended that DOE ensure that its contractors do not perform work or produce services before DOE obtains approval for its contracts.

**BSA Continues Review of Medi-Cal Drug Treatment Authorization Requests.** On August 1, BSA released the seventh in a series of semiannual reports concerning the Department of Health Services' (DHS) processing of reimbursement requests for certain prescribed drugs under the Medi-Cal program; collectively, these reports review DHS' process for counting and compiling data on drug treatment authorization requests (TARs) received and processed from June 1990 through May 1994. [14:2&3 CRLR 13; 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 156,600 drug TARs from December 1993 through May 1994, representing an increase of more than 99% since the period of June–November 1990. Accord-

ing to BSA, the increase in the number of drug TARs received may have occurred partly due to a reduction in the number of drugs on DHS' Medi-Cal list of contract drugs; removal of drugs from DHS' list of contract drugs causes the number of drug TARs to increase, since any drug not on the list requires a TAR. BSA also noted that from December 1993 through May 1994, DHS processed 152,114 drug TARs, 97% more than during June–November 1990. According to BSA, during the six-month period from December 1993 through May 1994, DHS generally did not meet the state requirement to process mailed-in drug TARs within five days.

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. BSA found that the Stockton drug unit processed 80% of the TARs received by fax within 24 hours of receipt, and processed the remaining 20% of the TARs in no more than two hours beyond the 24-hour requirement. BSA also found that the Los Angeles drug unit processed 74% of the TARs received by VDTS within 24 hours of receipt.

**Restrictive Implementation Schedules Effectively Limited Competition for the California State Lottery's New On-Line Gaming System** (July 1994) reviews the California State Lottery's compliance with California law in implementing a new on-line system.

As background information, BSA noted that until June 1992, one of the Lottery's primary objectives was to independently manage and own its on-line gaming system; however, at some point between June and October 1992, Lottery management decided to move away from owning its on-line gaming system. On January 27, 1993, the Lottery issued a request for proposals (RFP) reflecting its desire to have one vendor provide its system, including a central data system, software, and Lottery terminals. The RFP required the winning vendor to replace the Lottery's old on-line gaming system using either a preferred or an alternative implementation schedule. Under the preferred implementation schedule, the Lottery required a vendor to replace the old Lottery-owned on-line gaming system by October 14, 1993—within six months from the date the Lottery Commission would approve the contract; the RFP also stated that the Lottery could assess liquidated damages of up to \$250,000 per day for each day the vendor did not have the new vendor-owned on-line gaming system operational after October 13, 1993.

Under the alternative implementation schedule, the final RFP required a vendor to replace the Lottery-owned central data system by October 14, 1993, and replace the 12,000 Lottery-owned terminals by January 30, 1994; the RFP also stated that the Lottery could assess liquidated damages of up to \$250,000 per day for each day the vendor did not have the central data system and software operational after October 13, 1993, and for each day the vendor did not have all the Lottery terminals replaced after January 30, 1994. Further, if the winning vendor opted to use the alternative implementation schedule, for each Lottery-owned terminal that the vendor had not exchanged with a vendor-owned terminal by October 14, 1993, the Lottery would pay the vendor only half of the negotiated percentage of sales generated from those terminals. The RFP required vendors to submit their proposals by February 17, 1993; of the three vendors that the Lottery identified as likely bidders, only the Lottery's incumbent vendor, GTECH Corporation, submitted a proposal.

After reviewing the Lottery's entire procurement process for awarding the contract for the new on-line gaming system, BSA concluded that the restrictive implementation schedules included in the Lottery's RFP had improperly limited competition for the contract to a single vendor; BSA noted that this is inconsistent with Lottery policy that prohibits the drafting of an RFP so as to limit bidding to a single vendor. According to BSA, the Lottery's preferred implementation schedule was restrictive to two of the three vendors interested in the procurement because it was too short; and the alternative implementation schedule was restrictive to the two nonincumbent vendors because it was not viable. BSA noted that during the RFP preparation and solicitation process, the Lottery failed to question the advice of its consultant, made a "questionable decision" to not pursue negotiations to extend the contract for the old on-line gaming system with GTECH, and Lottery staff did not fully recognize that two of the three vendors had raised serious concerns about the RFP and had indicated they might not submit proposals. Because the restrictive implementation schedules limited competition to a single vendor, BSA noted that the Lottery could not be assured that it had received the best on-line gaming system at the best price.

In response to its findings, BSA recommended that the Lottery improve the oversight of its procurement process by critically reviewing the advice it receives from consultants hired to assist it during the



# INTERNAL GOVERNMENT REVIEW AGENCIES

procurement process, especially when Lottery staff raise concerns; foster an environment of open communication with vendors; and develop contingency plans when vendors raise concerns about elements of the procurement process, and implement those plans when necessary.

**Continued Improvement Needed in the State's Controls Over its Operations** (June 1994) contains BSA's findings regarding the state's control of its financial activities and its compliance with federal grant requirements and state regulations. Among other things, BSA found that the state continues to have many weaknesses in its accounting, auditing, and administrative control structure; these weaknesses, which BSA found in numerous departments, result in inaccurate financial statements, noncompliance with state and federal regulations, and waste, loss, and misuse of state resources. Among others, BSA made the following findings:

- The Department of Health Services did not have adequate procedures for monitoring and collecting almost \$240 million in accounts receivable.

- The Department of Transportation lost approximately \$972,000 in interest earnings because of \$6 million in late billings reviewed by BSA.

- The Department of General Services has not audited within the required three years 80 of the 151 departments to which it delegated purchase authority totalling more than \$214 million as of August 1993.

- Because the Department of Finance allowed certain departments to use funds that would have been available for future general fund expenditures, the state has approximately \$16.5 million less for future general fund expenditures than originally anticipated.

- The state did not fully comply with federal regulations in 28 of the 46 major grants BSA reviewed.

- The Stephen P. Teale Data Center has not attempted to collect approximately \$14 million in undercharges to the Department of Motor Vehicles from prior years and approximately \$94,000 in undercharges to the Governor's Office from prior years.

- The Stephen P. Teale Data Center could not provide records, including those identifying amounts owed by individual clients, to support \$18.6 million in amounts due from other funds, and could provide no supporting documentation for \$2.4 million in contracts payable.

- The state does not recognize the liability for earned vacation credit in its budgetary basis financial statements and, as of June 30, 1994, that liability was \$1 billion.

- The Office of Criminal Justice Planning purchased more than \$840,000 in computer equipment with federal grant money when the purchase was not authorized in the grant agreement, and the Office could not provide evidence of other authorization for the purchase.

Despite these ongoing problems, BSA noted that the state has made significant improvements in certain areas as a result of its response to weaknesses previously identified by BSA and the Office of the Auditor General (OAG). [11:4 CRLR 37-38; 11:3 CRLR 47] For example, for fiscal year 1990-91, OAG reported that the Office of Local Assistance did not have an adequate system in place to ensure that local educational agencies reported interest earned on advances from the state for construction projects [11:2 CRLR 45]; by fiscal year 1992-93, the Office had corrected that deficiency.

**Other BSA Reports.** BSA released several other reports since May 19, including the following: *Investigative Activity Report and Public Reports of Investigations Completed by the Bureau of State Audits From January 1 Through July 31, 1994* (September 1994); *The Adelanto Redevelopment Agency Needs to Improve its Procedures to Comply with the Community Redevelopment Law* (July 1994); and *State of California Financial Report, Year Ended June 30, 1993* (June 1994).

## LEGISLATION

The following is a status update on bills reported in detail in CRLR Vol. 14, Nos. 2 & 3 (Spring/Summer 1994) at pages 14-15:

**AB 2711 (V. Brown)**, as amended August 26, enacts the State Government Strategic Planning and Performance Review Act which requires the Controller, the Department of Finance (DOF), and BSA, in consultation with the Legislative Analyst, to develop a plan for conducting performance reviews of all state agencies. This bill requires DOF to survey state agencies to obtain specified information concerning strategic plans and to identify state agencies for which DOF recommends the development or updating of a strategic plan. Those identified agencies would be required to develop a strategic plan and report to the Governor and the Joint Legislative Budget Committee regarding the steps being taken to develop and adopt the plan. This bill was signed by the Governor on September 24 (Chapter 779, Statutes of 1994).

**SB 1989 (Marks)**, as amended May 16, would have required the State Auditor, by March 1, 1995, to prepare a specified report that recommends to the legislature the scope and approach to conduct a state-

wide performance review. This bill died in committee.

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

The Commission seeks to achieve these ends by conducting studies and mak-