# INTERNAL GOVERNMENT REVIEW OF AGENCIES

**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

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The Office of Administrative Law (OAL) was established on July 1, 1980, during major and unprecedented amendments to the Administrative Procedure Act (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 also has the authority 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.

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 Administrative Procedure Act (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:

*AB 1013 Determinations.* The following determinations were issued and published in the *California Regulatory Notice Register* in recent months:

-December 22, 1989, OAL Determination No. 16, Docket No. 89-004. OAL determined that a policy implemented by the California Energy Commission (CEC) interprets legislation and is a regulation subject to OAL review. The policy at issue adds a "specific intent" requirement to rules promulgated by CEC concerning eligibility for passive solar energy tax credits.

Although solar tax credit statutes were repealed in 1987, some taxpayers have filed amended returns claiming credits for prior years in which homes complying with the CEC eligibility regulations were built. In response, CEC requested a formal ruling from the Franchise Tax Board (FTB) on whether structural elements which were not designed or intended at the time of installation to apply solar energy could nevertheless constitute a "solar energy system" and thus qualify for the tax credit. FTB's Chief Counsel issued a letter stating the CEC regulations implementing the tax credit statute are "restrictive, not permissive" and that unless the components were designed or intended to use solar energy at the time of installation, they do not qualify for the credit. Thus, CEC began reviewing individual claims for solar tax credits and denying them if the claimant could not demonstrate specific intent to qualify for the tax credit at the time of installation.

In ruling in favor of the taxpayer, OAL rejected CEC's argument that it had made no interpretation of law, and that any such interpretation was made by FTB; OAL found that CEC's incorporation and application of FTB's ruling was unlawful underground rulemaking. OAL also noted that the subsequent legislative enactment of the specific intent requirement (Chapter 1352, Statutes of 1989) is not relevant to its determination or to ongoing litigation over this issue.

-December 29, 1989, OAL Determination No. 17, Docket No. 89-005. The Division of Labor Standards Enforcement (DLSE), the enforcement arm of the California Department of Industrial Relations, is responsible for enforcing various provisions of the Labor Code, including those involving wages, hours, and working conditions. The California Labor Commissioner, who heads DLSE, issued a Policy and Procedure Memorandum in 1982 (Memo 82-5) governing the treatment of mandatory service charges which are included in the full price of putting on a banquet.

Section 350 of the Labor Code provides that a gratuity is the sole property of the employee for whom it is left, but mandatory service charges are not included in the definition of "gratuity". Memo 82-5 directed a distribution of at least 75% of the charge to the employees who actually provide the services but allowed the remainder to be retained by the establishment for its administrative functions.

Although the Labor Commissioner rescinded Memo 82-5 on June 9, 1989 in light of the pending determination, OAL found that Memo 82-5 is a regulation requiring compliance with the APA. With the rescission and rejection of the memo, DLSE reinstated Memo 76-1, which interprets the Labor Code to require employers to include the service charge as part of the employer's gross receipts. Thus, it is subject to sales tax, may be used to satisfy minimum wage obligations, and must be included as part of the regular rate of pay for overtime purposes.

-December 29, 1989, OAL Determination No. 18, Docket No. 89-006. In another determination regarding action by DLSE, OAL found that Interpretive Bulletin No. 86-3 (IB 86-3) is a regulation requiring adoption in compliance with the APA. DLSE issued IB 86-3 on September 30, 1986, interpreting its role in enforcing vacation pay claims which would be paid out of an employer's general assets.

These unfunded vacation plans are subject to DLSE jurisdiction pursuant to *Suastez v. Plastic Dress-up Company*, 31 Cal. 3d 774 (1982). In subsequent litigation brought by trade associations against the Labor Commissioner, the U.S. Ninth Circuit Court of Appeals held that DLSE regulation of unfunded vacation plans is not preempted by the federal Employee Retirement Income Security Act of 1982 (29 U.S.C. sections 1001-1461), and lifted an injunction imposed by the lower court which prohibited DLSE from enforcing any vacation claims. *California Hosp. Ass'n v. Henning*, 783 F.2d 946 (9th Cir. 1986).

OAL determined that IB 86-3 interprets law (rather than merely restating existing law) to the extent that the Bulletin specifies that its enforcement is retroactive, limits the types of claims which may be brought, establishes a grace period for employers who did not

pay claims while the *Henning* injunction was effective, places a ceiling on accrued vacation pay, provides for treatment of "paid days off," and establishes a procedure for recoupment of advance on vacation time. The remainder of the Bulletin, which reasserts jurisdiction over enforcement of unfunded vacation pay disputes, is not regulatory and is thus not subject to the APA.

-January 22, 1990, OAL Determination No. 1, Docket No. 89-007. OAL reviewed a standard used by the state Water Resources Control Board (State Board) and the Regional Water Quality Control Board, North Coast Region (Regional Board), in administering the Toxic Pits Cleanup Act (TPCA or Act) found at Health and Safety Code section 25208-25208.17. The State Board and nine designated geographical Regional Boards are responsible for water quality control throughout the state (Water Code section 13001).

The Act governs discharges of liquid hazardous waste and hazardous waste containing free liquids which threaten drinking water. TPCA also established a program to ensure that existing surface impoundments of hazardous waste, which were installed prior to the enactment of more stringent federal and state laws requiring precautions such as double liners and leak detection, are either made safe or closed.

The challenged standards pertain to the meaning of the terms "discharge" and "free liquids" appearing in an interoffice communication between members of the Regional Board staff. The memorandum, circulated in 1987, states that the term "discharge" encompasses the continuing effects of past disposal practices where the wastes remained in impoundment after the enactment of TPCA. Furthermore, the term "free liquids" includes any liquid—such as rainfall—which comes into contact with hazardous waste, whether or not the rainwater is hazardous, if the water may become hazardous due to evaporation. The memorandum stated: "Thus, as a general rule, the State Board has concluded that a surface impoundment containing solid hazardous waste is covered by TPCA 'as soon as it receives water from precipitation.'"

OAL found that these standards do not fall within the meaning of a regulation and do not require adoption pursuant to the APA because they restate rather than interpret the Health and Safety Code. Relying on a previous determination, OAL concluded "that the memorandum's analysis of the terms 'discharge' and 'free liquids' are the only tenable interpretations possible and thus do not constitute a 'regulation.'" (See CRLR Vol. 9, No. 1 (Winter 1989) p. 28 for background information.)

-February 8, 1990, OAL Determination No. 2, Docket No. 89-008. OAL has determined that a management plan adopted by the Department of Parks and Recreation (Department) for commercial recreational boating on the North Fork and Middle Fork of the American River is a regulation required to be adopted in accordance with the APA. Under Public Resources Code section 5003, the Department has authority to protect and develop the state park system for the public's use and enjoyment.

In 1984, the Department commissioned a study of whitewater recreation on the River, including proposals for its management, from a private environmental consulting firm. An Advisory Task Force composed of commercial operators, environmentalists, and private recreational users met throughout 1986 and made recommendations on the plan before the Department issued a draft proposal in 1987 for the management of recreational whitewater boating on the River. This draft was part of the development of an eventual management plan for the River's commercial recreational use.

The Request for Determination was filed by a private recreational user sitting on the Task Force who challenged the final Whitewater Management Plan (WWMP), which has never been completely disclosed to OAL or to the public. The Request challenges the WWMP's adoption of specific elements which regulate commercial use by requiring permits as well as imposing restrictions on such things as the number of boats and trips per day, the timing of boat trips, safety requirements, and liability waivers.

The portion of the WWMP which regulates the time, place, and manner of commercial operation of recreational boating was found by OAL to be regulatory in nature and required to be adopted in accordance with the APA; other segments of the plan (*e.g.*, those describing in detail the North Fork and Middle Fork of the River and discussing the history of the regulation of its use and the applicable law) are restatements of fact and existing law and are therefore not regulations.

-February 8, 1990, OAL Determination No. 3, Docket No. 89-009. In this determination, OAL was asked to examine a policy of the Board of Registration for Professional Engineers and Land Surveyors which prohibits fire protection engineers (FPEs) from performing design services or designing fire protection systems.

According to OAL, the regulation of engineers "unofficially" falls into two categories under the Business and Professions Code, beginning with section 6700, and Title 16 of the California Code of Regulations (CCR), commencing with section 404. "Practice engineers," comprised of mechanical, electrical, and civil engineers, are licensed to practice or offer to practice design services and perform creative work. In contrast, most "title engineers," who are registered with the Board under engineering branch titles, are restricted from performing such services. This category includes control system, corrosion, fire protection (FPE), manufacturing, metallurgical, quality, traffic, and safety engineers. However, five engineering titles—agricultural, chemical, industrial, nuclear, and petroleum engineers—include design services in their definitions in Rule 404.

Within this murky framework, the Board has sought to enforce two policies: (1) generally, FPEs may not perform design services; and (2) specifically, FPEs may not perform design services as they relate to fire protection systems, because such design services are considered to fall within the scope of practice of civil, electrical, or mechanical engineers (practice engineers). While OAL agreed with the Board's contention that FPEs may not perform services confined to practice engineers, the Office found no statute or regulation which states that the design of fire protection systems may be rendered by practice engineers. Thus, OAL found that both policies interpret existing law and are invalid underground regulations.

-February 14, 1990, OAL Determination No. 4, Docket No. 89-010. OAL reviewed the Board of Registration for Professional Engineers and Land Surveyors' policy of requiring one year of "Party Chief" experience before qualifying to take the land surveyor examination.

To become a professional land surveyor, the Business and Professions Code (beginning with section 8700) requires applicants to pass two examinations. The first division of the exam tests the applicant's knowledge of fundamental surveying, mathematics, and basic science. The second division tests the applicant's ability to apply knowledge and experience from field training. Before an applicant may take the second division, section 8742 of the Code requires the applicant to possess specific educational qualifications, satisfied through one of three ways.

This determination concerns the Board's interpretation of one of the ways in which applicants may meet the second division requirements. After completing six years of actual experience in land surveying, including one year of responsible field training and one year of responsible office training, the applicant submits verification to the Board. Section 424, Title 16 of the CCR, specifies the nature of the experience which satisfies the examination requirements, but the Board has applied an additional condition on applicants. According to a letter from the Board to the applicant who requested this determination, an applicant's field training must have been as "Party Chief" (defined in Rule 424 as "responsible for direction and supervision of survey crews"). This more stringent requirement does not appear in any regulation or statute and, according to OAL, is therefore an interpretation of law requiring adoption pursuant to the APA.

-March 6, 1990, OAL Determination No. 5, Docket No. 89-011. In this determination, Legal Services of Northern California challenged procedures and criteria contained in an addendum to a letter from the Department of Social Services to all district attorneys and all Title IV-D Administrators. Title IV, Part D of the federal Social Security Act, known as the Child Support Enforcement Act, sets forth guidelines for state child support enforcement services as a condition to the state's receipt of Aid to Families with Dependent Children (AFDC) grants. The Department complies with Title IV-D by entering into cooperative agreements with county district attorneys to provide child support enforcement programs as set forth in Welfare and Institutions Code section 11475.2.

An addendum issued by the Department in January 1989 as Family Support Division Letter 89-3 contained procedures and criteria to be used by district attorney's offices in opening, prioritizing, and closing child support cases and accounts. The addendum requires program administrators to assign a low priority to cases where collection from an absent partner is unlikely for specified reasons. Additionally, the addendum contains six pages of criteria for closing a case where the parent is insolvent, habitually criminal, mentally incompetent, disabled, etc., or if the case has been assigned a low priority status for the preceding three years. OAL found these procedures to be regulations requiring adoption according to the APA.

In this determination, OAL recognized that "there is some authority for the proposition that contractual provisions previously agreed to by a party may not later be challenged by that party as an underground regulation"—that is, a contractual exemption from the APA. However, even assuming this argument to be valid, the requester was not a party to the cooperative agreement or the addendum.

-March 20, 1990, OAL Determination No. 6, Docket No. 89-012. In this determination, OAL concluded that Policy Memorandum No. 88-11, issued by the Child Development Division (CDD) of the State Department of Education, is a regulation required to be adopted pursuant to the APA.

Under section 8200 of the Education Code, CDD administers a variety of subsidized child care and development programs, sometimes by entering into agreements with contractors in a competitive award process which requires submission of an application and a budget for the proposed program. Under the statute, the administrative costs for all state-funded child care and development programs shall not exceed 15%. In October 1988, CDD issued Policy Memorandum No. 88-11 setting forth specific guidelines for CDD to follow in reviewing the "administrative costs" portion of an applicant's proposed program budget, and stated that adherence to the guidelines would be required during the fiscal year 1989-90 application renewal process. OAL found that the application of these budget guidelines was invalid underground rulemaking; the guidelines may not be used until properly promulgated pursuant to the APA.

-March 23, 1990, OAL Determination No. 7, Docket No. 89-013. In this determination, OAL found that section 1004.40 of the State Board of Equalization's Audit Manual, which provides that withdrawals of assets by a member or members of a joint venture prior to 80% completion of the venture are sales of the property transferred and hence subject to sales and use tax (the "80% completion rule"), is a regulation within the meaning of the APA.

The Board is charged with administering numerous tax programs, including the sales and use tax, for the support of state and local governments. The requester's clients formed joint ventures to build large construction projects—contributing construction equipment in return for equity in the joint venture at the commencement of the project, and distributing that equipment to the various joint venture members when it was no longer needed for the project as it progressed. In performing sales and use tax audits of the joint ventures, Board staff applied the "80% completion rule" from the Audit Manual: if the distribution of equipment occurred prior to 80% completion of the joint venture project, the distribution was treated as a sale or transaction subject to tax.

In concluding that the "80% completion rule" is an underground regulation which may not be applied or enforced until promulgated pursuant to the APA, OAL rejected the Board's arguments that the challenged rule is not a regulation because it has not been formally adopted by the Board. OAL found clear evidence that the Board's staff and its own hearing officer had applied the rule; and the prohibition against underground rulemaking in Government Code section 11347.5 is broad and not limited to formal actions of the board members of an agency. OAL also rejected the Board's argument that because the "80% completion rule" is not binding on its staff, it is therefore not a regulation. OAL found that the rule was a "criterion", the use of which is prohibited without APA rulemaking.

-April 12, 1990, OAL Determination No. XX, Docket No. 89- 014. In this determination, OAL reviewed a rule written and issued by the superintendent of the Avenal State Prison of the Department of Corrections, which permits inmates en route to or from the prison law library and processed through work exchange to carry only his own legal materials. After an exhaustive review of federal and state caselaw on the rights of prisoners to assist fellow inmates in preparing legal documents, OAL determined that this particular rule is not a regulation because it is not statewide in its application; it is a "local rule" applicable to one prison only, and is tailored to the structural set-up of that particular prison.

-May 23, 1990, OAL Determination No. 9, Docket No. 89-015. Here, OAL determined that the State Board of Equalization's interpretation of section 214 of the Revenue and Taxation Code, which exempts from taxation property used exclusively for religious, hospital, scientific, or charitable purposes (the "welfare tax exemption"), is a regulation. As amended in 1988, the welfare tax exemption also includes "property used exclusively for housing and related facilities for employees of religious...organizations...to the extent the residential use of the property is institutionally necessary for the operation of the organization."

The California Catholic Conference, an association of Roman Catholic bish-

ops in California, asked OAL to review the Board's Assessors' Handbook AH 267, which interprets the welfare tax exemption and caselaw discussing it, as applied to religious housing. OAL found that the Handbook's guidelines for application of the exemption were narrower than those in either the statute or the applicable caselaw, and concluded they were regulations warranting adoption pursuant to the APA.

*Privatization of Publication of CCR.* In March, OAL announced that it has completed its six-year revision project to organize the former California Administrative Code (now the California Code of Regulations) into a uniform format called the Revised Official California Code of Regulations. At approximately the same time, however, the State Printer informed OAL that it would no longer publish the CCR, compelling OAL to find a private publisher. OAL contracted with Barclays Law Publishers, which will now publish the CCR to the tune of $4,000 per set, plus $2,000 per year for a subscription to the update service.

The Public Records Distribution Act (Government Code section 14900 *et seq.*) requires OAL to distribute at least 100 copies to state government depository libraries for free, to ensure public access to state regulations. Until April 1990, the State Printer printed and distributed the CCR to all 153 California depository libraries (not merely government depository libraries) free of charge. However, much to the chagrin of numerous depository libraries across the state, OAL did not include this provision in its contract with Barclays, thus requiring many libraries to purchase the set from Barclays.

The California State Library Government Publications Section appealed to the Governor's Office to direct OAL to continue providing the CCR to all depository libraries, but without success. Instead, the Governor directed the State Library to continue negotiations directly with OAL. In the meantime, southern California depository librarians conducted a letter writing campaign to legislators. In response, the Senate and Assembly have discussed alternatives, but a legislative solution is unlikely this session.

According to OAL General Counsel John Smith, OAL and the State Library have negotiated for OAL to provide a combination of microfiche and hard copies of the CCR to all of the depository libraries which have requested them. Additionally, OAL will provide a set to each county clerk for distribution. OAL believes that this settlement satisfies its obligation to ensure public access to the CCR as required by the Public Records Distribution Act and by Government Code section 11344 *et seq.*, which generally charges OAL with responsibility for printing, publication, and distribution of the CCR.

LITIGATION:

In *Fair Political Practices Commission v. Office of Administrative Law, et al.*, No. 512795 (Sacramento County Superior Court), FPPC challenges OAL's authority to review FPPC regulations under the APA as it has been amended since 1974. The FPPC contends that its regulations are subject to review under the APA as it existed at the time of the electorate's approval of the Political Reform Act in 1974 (PRA), which—*inter alia*—created the FPPC.

Since that time, the APA has been amended several times to establish procedures for adopting emergency regulations by unanimous vote, and to create OAL and its regulatory review authority for the standards of necessity, authority, clarity, consistency, reference, and nonduplication. The FPPC claims that, insofar as these APA amendments impose any requirements on the FPPC other than those existing at the time of its creation in 1974, the APA amendments are a *de facto* and impermissible amendment of the PRA.

The FPPC has been concerned about OAL's review of its rulemaking since OAL was created in 1980, and seeks to preclude OAL from reviewing its regulations and issuing AB 1013 determinations regarding FPPC policies, guidelines, opinions, and advice letters. FPPC is particularly concerned about the ability of parties (or nonparties) to FPPC rulemaking to freely engage in *ex parte* contacts with the OAL staff and director during the regulatory review process. (See CRLR Vol. 8, No. 4 (Fall 1988) pp. 8-12 for background information.) The FPPC seeks declaratory relief determining whether it is subject to current APA procedures and an injunction prohibiting OAL from reviewing its rulemaking.

In *California Chapter of the American Physical Therapy Ass'n et al., v. California State Board of Chiropractic Examiners, et al.*, Nos. 35-44-85 and 35-24-14 (Sacramento County Superior Court), petitioners and intervenors challenge the Board's adoption and OAL's approval of section 302 of the Board's rules, which defines the scope of chiropractic practice. Following the court's August 1989 ruling preliminarily permitting chiropractors to perform physical therapy, ultrasound, thermography, and soft tissue manipulation, the parties have engaged in extensive settlement negotiations. A status conference is scheduled for August 2. (See CRLR Vol. 9, No. 4 (Fall 1989) p. 127; Vol. 9, No. 3 (Summer 1989) p. 118; and Vol. 9, No. 2 (Spring 1989) p. 112 for background information on this case.)

## OFFICE OF THE AUDITOR GENERAL

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The Office of the Auditor General (OAG) is the nonpartisan auditing and investigating arm of the California legislature. OAG is under the direction of the Joint Legislative Audit Committee (JLAC), which is comprised of fourteen members, seven each from the Assembly and Senate. JLAC has the authority to "determine the policies of the Auditor General, ascertain facts, review reports and take action thereon...and make recommendations to the Legislature...concerning the state audit...revenues and expenditures...." (Government Code section 10501.) OAG may "only conduct audits and investigations approved by" JLAC.

Government Code section 10527 authorizes OAG "to examine any and all books, accounts, reports, vouchers, correspondence files, and other records, bank accounts, and money or other property of any agency of the state...and any public entity, including any city, county, and special district which receives state funds...and the records and property of any public or private entity or person subject to review or regulation by the agency or public entity being audited or investigated to the same extent that employees of that agency or public entity have access."

OAG has three divisions: the Financial Audit Division, which performs the traditional CPA fiscal audit; the Investigative Audit Division, which investigates allegations of fraud, waste and abuse in state government received under the Reporting of Improper Governmental Activities Act (Government Code sections 10540 et seq.); and the Performance Audit Division, which reviews programs funded by the state to determine if they are efficient and cost effective.

RECENT AUDITS:

*Report No. P-852 (January 1990)* criticizes the administration of California's ten-year-old statewide