



MAJOR ISSUES

% *The Department of Insurance Has Restructured the Conservation and Liquidation Division.* Under this restructuring, there are several organization and management issues that warrant legislative review. We recommend that the department report on these issues at budget hearings. (See page G-13.)

% *Legislature Needs Information on Blue Cross Restructuring Plan.* On September 15, 1994, Blue Cross of California submitted a plan to the Department of Corporations (DOC) which spun-off a majority of its activities into a for-profit business. As a result, Blue Cross is required under current law to donate the value of its assets to a charitable trust. The DOC must approve this plan in order for it to be effective. Given the magnitude of this proposal, the department should report to the Legislature on the specifics of the plan and its effects on state and local expenditures on public health programs. (See page G-29.)

% *Proposal to Expand Foreign Offices Is Not Justified.* We recommend that the Legislature not approve the proposed expansion of the foreign office program in the Trade and Commerce Agency because the agency has not clearly demonstrated the need or benefit to the state of this expansion. (See page G-46.)

% *Effectiveness of the Defense Conversion Matching Grant Program Is Uncertain.* The effectiveness of the Defense Conversion Matching Grant Program in the Trade and Commerce Agency is uncertain because the agency has not clearly demonstrated the

value the state grant funds add to California's defense conversion efforts. Current law requires the Defense Conversion Council to submit a report to the Legislature on the effectiveness of the state matching grant program. This report needs to be received and reviewed by the Legislature before it considers approving the \$8 million requested for the program. (See page G-55.)

%Administration Proposes to Eliminate the Energy Commission. The administration is currently developing a reorganization plan for various resources departments. This reorganization calls for the elimination of the Energy Commission and transferring its responsibilities to a new department. The administration's plan should be available for review before the Legislature takes action on the commission's budget. (See page G-59.)

%Eliminate the Agricultural Labor Relations Board. Due to a persistent decline in workload, we recommend that the Legislature eliminate the Agricultural Labor Relations Board and enact legislation transferring enforcement of the Agricultural Labor Relations Act to the Public Employment Relations Board. (See page G-62.)

%Labor Law Enforcement Program in Farm and Garment Industries Is Not Effective. The Department of Industrial Relations' (DIR) joint program with the U.S. Department of Labor—the Targeted Industries Partnership Program (TIPP)—for enforcing labor laws in the agricultural and garment industries has not been effective. Therefore, we recommend that the DIR report to the Legislature on the cost-effectiveness of the program and on any changes in the law or administrative process that would improve its performance. (See page G-66.)

%Workplace Safety Program Delayed. The DIR's program for targeting high hazard employers and industries for workplace safety inspections and consultations has yet to be implemented due to issues concerning program funding and the targeting of employers and industries. Therefore, we recommend that the DIR report to the Legislature on: (1) the status of program funding; (2) the effect of the delay; and (3) whether its planned program is consistent with legislative intent. (See page G-70.)






TABLE OF CONTENTS

| | |
|--|------|
| Overview | G-5 |
| Spending by Major Programs | G-5 |
| Major Budget Changes | G-6 |
| Departmental Issues | G-11 |
| Department of Insurance (0845) | G-11 |
| Department of Consumer Affairs (1111-1655) | G-18 |
| Department of Fair Employment and Housing (1700) | G-27 |
| Department of Corporations (2180) | G-29 |
| Housing and Community Development (2240) | G-32 |
| Trade and Commerce Agency (2920) | G-46 |
| Energy Resources, Conservation and Development Commission (3360) | G-59 |
| Agricultural Labor Relations Board Public Employment Relations Board (8300 and 8320) | G-61 |
| Department of Industrial Relations (8350) | G-66 |

| | |
|---|------|
| Department of Food and Agriculture (8570) | G-78 |
| Public Utilities Commission (8660) | G-80 |
| Findings and Recommendations | G-83 |

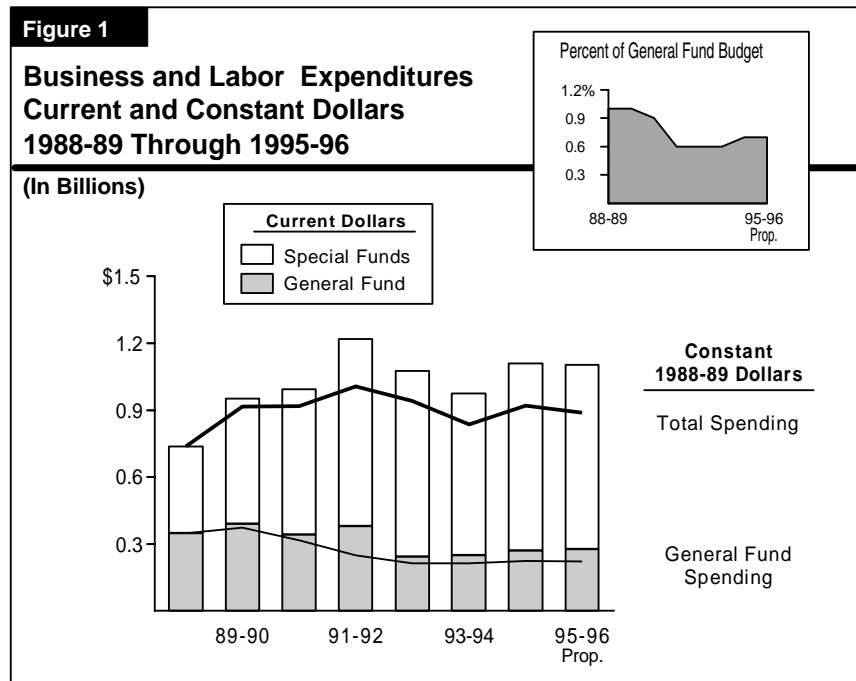


OVERVIEW

Expenditures for business and labor programs in 1995-96 are proposed to decrease by about 1 percent compared to the current year. This decrease is the net result of a variety of changes in many programs and reflects a decrease in special fund spending partially offset by a slight increase in General Fund spending.

The budget proposes total state expenditures of \$1.1 billion for business and labor programs in 1995-96. This level of spending is a decrease of \$6.9 million, or 0.6 percent, from estimated current-year expenditures.

Figure 1 (see next page) shows that expenditures for business and labor programs from all state funds reached a peak of about \$1.1 billion in 1991-92, then declined slightly through 1993-94 and are projected to approach the previous peak level in 1995-96. Over the eight-year period shown in Figure 1, expenditures increased by \$366 million, representing an annual average growth of 5.9 percent. When these expenditures are adjusted for inflation, total spending since 1988-89 has increased by an average of 2.6 percent annually. The General Fund share of program expenditures has declined from 47 percent in 1988-89 to 25 percent in the budget year. General Fund expenditures for the budget year, however, represent a slight increase compared to the current year.



SPENDING BY MAJOR PROGRAMS

Figure 2 provides the spending trends for selected major business and labor programs from 1993-94 through 1995-96. As the figure shows, only one agency (Trade and Commerce) shows a significant percentage change in proposed General Fund expenditures between the current and budget years (a 21 percent increase). Two other programs show large percentage changes in special fund expenditures: Corporations (a 28 percent increase) and the Energy Commission (a 48 percent decrease).

MAJOR BUDGET CHANGES

Figure 3 (see page 8) summarizes major budget changes proposed for business and labor programs. As shown in the figure, there are a variety of relatively small dollar increases in General Fund program expenditures. These include \$5.8 million for the Trade and Commerce Agency to increase its international trade and tourism programs and \$2.3 million for the Department of Industrial Relations to pay higher facility rental costs in San Francisco.



| Figure 2 | | | | | |
|--|---------------------------|------------------------------|-----------------------------|--------------------------------|----------------|
| Business and Labor Budget Summary | | | | | |
| Selected Program Funding | | | | | |
| 1993-94 through 1995-96 | | | | | |
| (IDollars in Millions) | | | | | |
| Programs | Actual 1993-94 | Estimated 1994-95 | Proposed 1995-96 | Change From 1994-95 | |
| | | | | Amount | Percent |
| Consumer Affairs | | | | | |
| General Fund | — | \$1.0 | \$1.0 | — | — |
| Special Fund | \$219.2 | 282.1 | 287.3 | \$5.2 | 1.8% |
| Totals | \$219.2 | \$283.1 | \$288.0 | \$4.9 | 1.7% |
| Food and Agriculture | | | | | |
| General Fund | \$62.6 | \$68.6 | \$70.2 | \$1.6 | 2.3% |
| Special Fund | 111.3 | 111.1 | 113.5 | 2.4 | 2.1 |
| Totals | \$173.9 | \$179.7 | \$183.7 | \$4.0 | 2.2% |
| Industrial Relations | | | | | |
| General Fund | \$123.9 | \$137.2 | \$136.9 | -\$3 | — |
| Special Fund | 29.9 | 46.0 | 44.5 | -1.5 | -3.3% |
| Totals | \$153.9 | \$183.2 | \$181.4 | -\$1.9 | -1.0% |
| Insurance | | | | | |
| Special Fund | \$116.1 | \$115.1 | \$111.0 | -\$4.1 | -3.5% |
| Trade and Commerce | | | | | |
| General Fund | \$38.7 | \$36.2 | \$43.8 | \$7.6 | 21% |
| Special Fund | -1.7 | 17.6 | 11.5 | -6.1 | -35% |
| Totals | \$37.0 | \$53.8 | \$55.3 | \$1.5 | 2.8% |
| Corporations | | | | | |
| General Fund | \$.2 | \$.5 | -\$2 | -\$7 | -1.4% |
| Special Fund | 26.8 | 28.5 | 36.5 | 8.0 | 28.0 |
| Totals | \$27.0 | \$29.0 | \$36.3 | \$7.3 | 25.2% |
| Energy Commission | | | | | |
| Special Fund | \$40.9 | \$40.7 | \$21.2 | -\$19.5 | -48% |
| Housing and Community Development | | | | | |
| General Fund | \$8.4 | \$11.5 | \$10.0 | -\$1.5 | -13% |
| Special Fund | 8.0 | 5.3 | 5.8 | -.5 | 5.2% |
| Total | \$16.4 | \$16.9 | \$15.8 | -\$1.1 | -7.0% |

The figure also shows proposals for several departments to decrease their expenditures for certain programs. For example, the figure shows a \$19.5 million overall decrease in the Energy Commission's proposed expenditures. This reduction reflects the administration's proposal to provide only half-year funding for the commission and transfer its



Figure 3

**Business and Labor Programs
Proposed Major Changes for 1995-96
General and Special Funds**


| | | |
|---|---------------------------------------|--|
| Department of Industrial Relations | Re- quested: Decrease: | \$181.4 mil- lion \$1.8 million (-1%) |
|---|---------------------------------------|--|

-  • \$2.3 million (\$1.7 million General Fund) to fund department's temporary relocation while a new facility is built in San Francisco
- \$1.3 million for elevator safety inspections
- \$1.1 million to combat the underground economy
-  • \$3.0 million for the expiration of one-time workers' compensation reform costs and suspension of state mandates


| | | |
|--------------------------------|---------------------------------------|--|
| Department of Insurance | Re- quested: Decrease: | \$111 million \$4.1 million (-3.5%) |
|--------------------------------|---------------------------------------|--|

-  • \$9.2 million for automobile and workers' compensation insurance fraud enforcement
- \$4.4 million unallocated reduction to address a revenue shortfall
-  • \$2.2 million to reflect the reduction of one-time costs

| | | |
|----------------------------------|---------------------------------------|---|
| Trade and Commerce Agency | Re- quested: Increase: | \$55.3 million \$2.5 million (+2.8%) |
|----------------------------------|---------------------------------------|---|

-  • \$4.3 million to expand the International Trade and Investment Office Program (General Fund)
- \$1.5 million for an increase in international tourism activities (General Fund)

| | | |
|--------------------------|---------------------------------------|---|
| Energy Commission | Re- quested: Decrease: | \$21.2 million \$19.5 million (-48%) |
|--------------------------|---------------------------------------|---|

-  • \$19.5 million reduction to provide half-year funding and transfer responsibilities to a new Department of Energy and Conservation January 1, 1996.

functions to a new Department of Energy and Conservation. The figure also shows a \$4.4 million unallocated reduction in the Department of Insurance to address a revenue shortfall and a \$1.5 million reduction to the Department of Housing and Community Development for reduced workload in housing programs.



DEPARTMENTAL ISSUES

DEPARTMENT OF INSURANCE (0845)

Insurance is the only interstate business that is regulated entirely by the states, rather than the federal government. In California, the Department of Insurance (DOI) is responsible for regulating insurance companies, brokers, and agents in order to protect businesses and consumers who purchase insurance. Currently, there are about 1500 insurers and 264,000 brokers and agents operating in the state, generating total premiums of about \$60 billion a year.

The budget proposes total expenditures of \$110 million from the Insurance Fund to support the DOI in 1994-95. This is \$4.1 million, or 3.6 percent, less than estimated current-year expenditures. This decrease is due mainly to a \$4.4 million unallocated reduction in 1995-96 and a \$2.2 million reduction to adjust for one-time costs in the current year. These reductions are partially offset by increased expenditures for fraud control.

THE CONSERVATION AND LIQUIDATION OFFICE

The Conservation and Liquidation Office in the Department of Insurance is responsible for conserving and liquidating insolvent insurance companies. Under the Insurance Code, the Insurance Commissioner has the authority to revoke the license of an insolvent insurer and, with a court order, conserve and liquidate the assets of the company. The current department policy is to make every effort to restore insolvent insurance companies (estates) to financial health or to sell them to sound insurance carriers before initiating liquidation procedures.

Reorganization of Conservation and Liquidation Division

Prior to budget hearings, the Department of Insurance should report to the Legislature on the restructuring of the Conservation and Liquidation Division.

In response to various problems with the management and operation of the Conservation and Liquidation Division, the department initiated a reorganization of the division in November 1993. The department informs us that the restructuring should be complete by July 1995. As part of the Department of Insurance, the office's status warrants the legislative oversight necessary to protect insurance policy holders in the state. The Legislature should have access to information regarding the office as it does for any other state program. Therefore, prior to budget hearings, the department should report to the Legislature on the restructuring of the office.

In reorganizing the Conservation and Liquidation Division, the department created the Conservation and Liquidation Office and the Special Receivership Bureau.

The Conservation and Liquidation Office has jurisdiction over 70 estates, with assets totaling \$409 million. (There are four other estates—with assets totaling \$1.8 billion—that are under the direction of special deputies appointed by the Commissioner). The Chief Executive Officer is charged with ensuring that the office's management of each conserved estate with assets is consistent with the office's fiduciary responsibility. The office currently has 38 employees—all non-civil service positions—and they are supported from the assets of conserved estates. In September 1994, the department announced its internal decision to move the office from Los Angeles to San Francisco.

All conserved estates without assets are assigned to the Special Receivership Bureau. This bureau is funded by the Insurance Fund and consists of five civil service positions which manage these no-asset estates.

The main objective of the reorganization is to strengthen the estate management and financial functions of the division. In our *1994-95 Analysis*, we addressed significant management and organizational problems within the division. Some of these problems have been addressed through the restructuring. For example, the department has established policies to control its hiring and salary setting. Furthermore, the department has established procedures to assure that assets from one estate do not pay for work performed on another estate.

Under the department's reorganization of these activities, however, there are still several organization and management issues that warrant legislative review. These issues are discussed below.

Department Establishes Positions Outside of the State Budget Process. The department informs us that it plans on hiring 25 staff to raise the total to 63 non-civil service positions to staff the Conservation and Liquidation office. These positions and related salaries and benefits were established outside of the state budget process. The department justifies the use of non-civil-service employees on the basis that hiring these employees is essential to meet the division's unpredictable workload. The use of such staffing may be justified in short-term or temporary workload situations. Work performed on most estates, however, takes at least five years and represents a more constant workload. Furthermore, the department's policies for determining under what conditions positions should be civil service or non-civil service generally are unclear. For example, in restructuring the division, the department placed the Conservation and Liquidation Office under the direction of a Chief Executive Officer, a private "at-will" position with a salary of \$195,000 annually. Before the restructuring, the division was run by a Division Chief, a civil-service position earning \$74,500 a year. The department needs to justify why it is necessary to establish these positions and related salaries/benefits outside of the state budget process and where it gets the authority to do so.

No Meaningful Budget. The office does not have a meaningful budget for its expenditures. While court approval is necessary for some expenditures, historically the office spends on an "as-needed" basis from the assets of conserved estates. The office has not developed an annual budget and has had no process to effectively control expenditures. The office expects to have a new cost-accounting system in place in February 1995. Hopefully, this will correct the past problems of accurately accounting for expenditures. The office, however, has not developed annual budgets for operation of the office or estates.

Workload Measures and Standards Not Available. The office does not have workload measures for determining appropriate staffing levels or for evaluating employee performance. That is, the office is without objective benchmarks to determine if employees are meeting certain workload standards. For example, currently there is no standard for the number of claims an employee should process. The office has hired an outside contractor to help it establish these measures and it expects the measures to be complete in April 1995.

Management Plans for Oversight of Estates Not Final. In the *Analysis of the 1994-95 Budget Bill*, we pointed out that the division did not have management plans for any estates under conservatorship. It is our understanding that the office is developing these management plans for all estates and is scheduled to complete them by the end of February 1995. Until these plans are in place, the office cannot adequately determine whether an estate is on a timely track for restoration. This can lead to higher-than-necessary expenditures, which in turn can lower the return

to the estate policy holder.

Over \$1 Billion in Assets Managed Outside the Office. Four large estates—with assets totaling over \$1.8 billion—are not managed by the division. Instead, these estates are managed by on-site managers appointed by the commissioner. The division expects to move two of these estates under the office's direction in 1995 and a third by the end of 1996. The future direction of the fourth estate, Executive Life, is unclear. It is also not clear why these estates should be outside of the management of the Conservation and Liquidation Office. As mentioned above, the purpose of restructuring the conservation and liquidation activities is to strengthen the estate management and financial functions of conserved estates. To realize fully the benefits of this management reorganization, all assets under state conservatorship should be placed under the office. This should occur as soon as the reorganization is final.

Department Needs to Report to the Legislature. To address the issues discussed above, the department should report to the Legislature prior to budget hearings. This report should include:

- The office's policies and authority for establishing positions, salaries, and benefits outside of the state budget process.
 - A meaningful budget for all office expenditures and an explanation of how the budget was developed.
 - Workload measures and standards for determining staffing levels and evaluating employee performance.
 - A status of each estate management plan and a discussion on how these plans will be used to improve the management of estates and benefit insurance policy holders.
 - An explanation of why certain assets are currently managed outside of the office and a timeline for bringing all conserved assets under the office's management by July 1995.
-

Budget Still Not Submitted for Legislature's Review

We recommend that the Legislature add an informational item to the Budget Bill to show the budgeted costs for the Conservation and Liquidation Office and language requiring an informational item in future Governor's Budgets and Budget Bills for a summary of the administrative and direct costs and staff associated with operating the conserved estates. Also, we recommend that the Legislature adopt Supplemental Report Language requiring the department to provide detailed budget information on each estate to the Legislature by December 1 each year.

The Legislature added language in the 1994-95 Budget Bill requiring the Governor's Budget, beginning in 1995-96, to include specific information for all costs for each estate under conservation by the division. This language was vetoed by the Governor. For the first time, however, the 1995-96 Governor's Budget does include summary information showing the number of estates and total expenditures from these estates for the budget year and the two previous years. This information indicates that expenditures for direct and administrative costs from assets of all estates totals \$16 million in 1995-96. This is a decrease of about \$1 million from the current year. These amounts, however, *do not* include expenditures from assets of the four estates that are not under the office.

Unfortunately, the limited information in the Governor's Budget does not provide the Legislature all the information it needs to undertake a meaningful oversight of these departmental activities. For example, the budget does not show the number of staff either in the office or assigned to each estate. Moreover, because the office does not have an effective budget process in place, the expenditures shown in the Governor's Budget are of little use.

We recommend that the Legislature add an informational item to the Budget Bill showing the estimated 1995-96 expenditures and include Budget Bill language requiring future Governor's Budgets and Budget Bills to include an informational item which reflects a summary of the administrative and direct costs and staff for work performed on conserved estates. Furthermore, to ensure that the Legislature receives the information it needs to gain meaningful insight of the expenditures for the Conservation and Liquidation Office, we recommend that the Legislature adopt Supplemental Report Language requiring the department to provide detailed information—on December 1 of every year—for each conserved estate.

OTHER ISSUES

Workload Measures and Standards Required

We withhold recommendation on \$7.4 million from the Insurance Fund proposed to convert 74 limited-term positions in the Fraud Division to permanent positions, pending receipt of the Department's report on workload measures and standards.

The budget proposes \$7.4 million from the Insurance Fund to convert 74 limited-term positions in the Fraud Division to permanent positions. These positions are to help the department continue its efforts in fighting workers' compensation and automobile insurance fraud.

Legislature Requested Workload Measures and Standards. The Legislature in the *Supplemental Report of the 1994 Budget Act* directed the Insurance Commissioner to report to the Chairs of the fiscal committees in both houses and to the Joint Legislative Budget Committee, no later than March 1, 1995, on (1) workload measures that provide information on the level of annual work, by activity and (2) workload standards that provide productivity or "work" rates for the department's staff. This report is essential in order to determine an appropriate level of staffing.

The Legislature also required the department to submit to the committees, no later than December 1, 1994, a status report on these measures and standards. This report has been submitted and it *defines* various workload standards for the Fraud Division. For example, the report defines one measure of work for an investigator as "the number of cases per fraud investigator." These definitions are the first step in establishing the necessary standards, which would provide expected "work" rates for the staff. For instance, a standard for a fraud investigator might be set at a given number of cases per year. Thus, we withhold recommendation on \$6.8 million for the conversion of the 74 limited positions in the Fraud Division pending receipt of the March 1 report on the department's workload measures and standards. When the report is received, we will review it and make recommendations to the Legislature, as appropriate.

Legislature Needs Details on Unallocated Reduction

We recommend that the department report prior to budget hearings on the \$4.4 million unallocated reduction and its effect on the department's programs.

The budget proposes a \$4.4 million unallocated reduction to the department in 1995-96. The Legislature should be provided details on this unallocated reduction and its effect to the department's programs. There-

fore, we recommend that the department report at least on the following issues concerning the unallocated reduction:

- The programs that will be affected by the reduction and how they will be affected.
- The potential costs and benefits to insurance policy holders in the state resulting from the reduction.

This report should be sent to the Legislature prior to budget hearings to give the Legislature sufficient time to review it before approving the department's budget.

DEPARTMENT OF CONSUMER AFFAIRS (1111-1655)

The Department of Consumer Affairs (DCA) is responsible for promoting consumerism and protecting the public from deceptive and fraudulent business practices, while supporting a fair and competitive marketplace. The department includes 32 regulatory boards, four bureaus, and two programs. These regulatory entities license and regulate over 2 million practitioners from various occupations and professions. Only four bureaus and two programs are statutorily under the direct control of the department. The others are under the statutory control of the appointed representatives (typically, board members) of the occupations and professions they license and regulate.

Expenditures for the support of the department and its constituent boards are expected to total \$272.9 million in 1995-96. This is \$5.5 million, or 2 percent, more than estimated expenditures in the current year.

Department Enters Second Year of Performance-Based Budgeting

We recommend that before the Legislature enters into a performance budgeting contract with the DCA in 1995-96 the department be required to develop and incorporate into the pilot project performance measures that assess the department's ability to mitigate consumer risk in regulated markets, and also demonstrate how operational flexibilities granted in the 1994 Budget Act are responsible for specific examples of improved performance.

Background. The Governor proposed in his 1993-94 budget to use four departments, including the DCA, for a pilot project in performance budgeting. The Legislature subsequently approved Ch 641/93 (SB 500, Hill) that included five state departments, including the DCA, in a pilot project to commence in 1994-95. During the 1994-95 budget process, the DCA negotiated a contract, contained in the 1994 Budget Act and Ch 150/94 (AB 2384, Committee on Ways and Means), with the Legislature that formally began the pilot project. The operational flexibilities authorized in the 1994-95 "contract" are in effect for one year only and expire on June 30, 1995.

The pilot project involves the four bureaus and two programs under the statutory control of the Director. None of the independent regulatory boards are included in the pilot project. Figure 4 shows the bureaus and programs participating in the pilot project. The DCA, which has not received an augmentation to fund the costs of planning, designing, and implementing performance-based budgeting, estimates that to date it has absorbed costs of \$2.6 million including consultant costs of \$305,000 on the pilot project.

Figure 4

**Department of Consumer Affairs
Performance-Based Budgeting Pilot Project**

Bureaus and Programs^a

Bureaus

- Bureau of Automotive Repair (Including Smog Check program)
- Bureau of Electronic and Appliance Repair
- Bureau of Home Furnishings and Thermal Insulation
- Bureau of Security and Investigative Services

Programs

- Arbitration Review Program
- Tax Preparers Program

^a The department and its administrative divisions are also included in the performance-based budgeting pilot project.

1995-96 Budget Proposal. Expenditures for the bureaus and programs under performance-based budgeting are expected to be \$141.3 million, a 1 percent increase over estimated current-year expenditures. The Budget Bill includes language to allow the DCA discretion to increase or decrease 1995-96 spending by up to 15 percent among the activities under program budgeting as long as expenditures do not exceed the total budgeted amount. This budget language is identical to language in the 1994 Budget Act. The budget proposal does not include any other aspects of the current-year contract. It is our understanding that the DCA will be seeking a new contract with the Legislature to expand the array of operational flexibilities in 1995-96.

Operational Flexibilities. As mentioned above, the 1994 Budget Act and Ch 150/94 granted the DCA a variety of operational flexibilities in the areas of budget, personnel and procurement. These operational flexibilities are outlined in Figure 5 (see next page) .

Figure 5

**Department of Consumer Affairs
Performance-Based Budgeting Pilot Project**

List of Operational Flexibilities

- Department has discretion to augment or decrease budgets of six participating bureaus and programs by up to 15 percent, so long as expenditures stay within the total budgeted amount.
- Positions may be administratively established without Department of Finance approval.
- Contracts under \$1 million not related to data processing services do not require Department of General Services review.
- The State Printing Plant, the Office of Support Services, and Prison Industries may be considered as competitive bidders and not sole source contractors.
- Field offices may be leased without Department of General Services approval (except for Los Angeles or San Francisco locations which require the approval of the Secretary of State and Consumer Services).
- Minority, women, and disabled veteran businesses may be prequalified for participation in DCA procurement.
- Civil service position classifications may be established or modified without the review and approval of the Department of Personnel Administration, but are subject to review by the State Personnel Board.

In exchange for these flexibilities, the department is obligated to prepare and submit to the Legislature on specific dates the documents necessary to begin implementing performance-based budgeting. Since July, the DCA has held several meetings with the Department of Finance and legislative staff to discuss the DCA's activities on the performance-based budgeting pilot project. During these meetings, the DCA administration has demonstrated its dedication to making the project a success. To date, the department has met all the dates for submitting the necessary documents to the Legislature and, in general, the documents are complete. The submittals to the Legislature include:

- A strategic plan, containing the DCA's mission statement, goals and objectives.
- Baseline performance measures including performance levels in 1993-94.
- A status report of actions to date.

The DCA still must prepare its performance targets before March 1, and a status report by May 31. If the department does not meet these deadlines, the operational flexibilities under the contract terminate.

Performance Measures Fall Short. On November 1, 1994 the DCA submitted 228 performance measures covering the department's operational functions. These measures are important management tools and provide information the DCA needs in order to efficiently manage its activities. These measures will also assist the Legislature in evaluating the DCA's efficiency in undertaking current responsibilities. The measures do not provide the Legislature (or the Administration) the information it needs to determine whether or not the efforts of the department are effective or necessary. For example, the DCA's performance measures focus on department operations, such as the time and expense of licensing and enforcement activities without any indication of whether these activities are providing consumers any value. As a result, these measures do not provide for a meaningful assessment of the department's primary mission: identifying and mitigating consumer risk in the areas regulated by the DCA. A more complete set of performance measures would assess:

- The seriousness of complaints (separating the trivial from the high priority), how the department prioritizes its response to complaints, and means to distinguish complaints about the DCA processes from complaints against licensees.
- The competency of licensees.
- The effectiveness of licensing exams.
- The effectiveness of enforcement activities.

Lacking the types of performance measures outlined above, the Legislature will not have sufficient information to assess both the efficiency *and* the effectiveness of the DCA. Consequently, we recommend that before the Legislature renews a performance budgeting contract with the DCA in 1995-96, the department incorporate these types of measurements.

Effectiveness of Operational Flexibilities and Exemptions. The DCA was given a number of operational flexibilities based on the department's contention that these flexibilities were essential for improving performance. The department, however, has yet to fully use these authorizations. Furthermore, the DCA has been unable to specify the area or amount of improved performance resulting from the flexibilities.

The Legislature needs to determine whether or not the current-year operational flexibilities were helpful or if other types of flexibilities are warranted, to make the performance-based budgeting pilot project a success. To allow this, the DCA must show how the current year flexibilities aided in improving performance. The DCA should also advise the Legislature if changes need to be made and if so how these changes will be used to improve performance. Therefore, we recommend that the

Legislature not extend or change the current-year operational flexibilities until the DCA has provided this information. The DCA has not yet proposed a budget contract for 1995-96 nor indicated the flexibilities the department will be seeking. The contract is expected to be included in the Budget Bill and/or budget trailer bill.

Proposed Augmentations Unnecessary Under Performance-Based Budgeting

We recommend that the Legislature delete \$340,000 and nine positions under Item 1111-001-702 because the DCA should accommodate these costs under the performance-based budgeting program.

Under the performance based budgeting contract, the DCA can increase or reduce participating bureaus' and programs' budgets by up to 15 percent, so long as total spending does not exceed the appropriated amount. This provision provided the DCA with the ability to quickly react to and implement necessary program changes in the bureaus and programs without delay. The Budget Bill contains the same authorization in 1995-96.

The budget proposes augmentations totaling \$340,000 and nine positions for bureaus and programs within the performance-based budgeting pilot project. Figure 6 identifies the spending proposals and the

| |
|---|
| Figure 6 |
| Department of Consumer Affairs |
| 1995-96 Budget Changes Proposed for Bureaus and Programs |
| <ul style="list-style-type: none"> • Workload adjustment to implement Ch 1091/94 (SB 1713, Hart) requiring the Bureau of Security and Investigative Services to develop minimum selection, competence and training standards for armed security guards (\$34,000 and 1 position). • Workload adjustment for the Bureau of Automotive Repair to implement Ch 725/94 (AB 2852, Escutia) that requires vehicle manufacturers to provide Smog Check stations with information to improve emission-related repairs (\$74,000 and 1 position). • Workload adjustment to implement Chapter 1135/94 (AB 3302, Speier) requiring the DCA to obtain either a federal employer identification number or social security number prior to issuing a license (\$89,000) and 3 limited-term positions). • Workload adjustment to implement Ch 906/94 (AB 923, Speier) requiring the DCA to match its list of licensees with the list provided by the Department of Social Services showing persons owing child support payments (\$64,000) and 3 limited-term positions). • Expenditure augmentation that would redirect investigation workload from the Medical Board of California to the DCA's enforcement division (\$79,000 and 1 position). |

specific amounts. One reason the Legislature approved the DCA's spending flexibility was to reduce the DCA's reliance on the budget change

proposal process. Since the total amount of the proposed augmentations is about 0.3 percent of all expenditures in the performance-based budgeting programs and bureaus, accommodating these costs should not be a problem. While we are not taking issue with any of the proposed changes, we recommend that the Legislature not approve the augmentations. Instead, the DCA should use the flexibility granted it under performance-based budgeting and handle these costs within existing resources.

Consumer Boards Scheduled to Sunset

Legislation enacted in 1994 (Ch 908/94, SB 2036, McCorquodale) puts in place a procedure and schedule for the Legislature to assess the effectiveness of, or need for, state involvement in the 32 areas currently regulated by various boards.

Pursuant to Ch 908/94, the authorizing statutes for the independent boards within the DCA become inoperative according to a specified schedule on July 1, of either 1997, 1998, or 1999. The respective statutes are then repealed six months later, on January 1 of either 1998, 1999, or 2000. Therefore, the boards and their regulatory authorities “sunset” unless the Legislature passes laws keeping the boards in existence. Figure 7 (see next page) shows this sunset schedule.

Chapter 908/94 creates the Joint Legislative Sunset Review Committee to review and analyze the effectiveness of and need for each of the boards. Each board, with the assistance of the DCA, is required to submit to the Joint Committee—15 months before January 1 of the year its authorizing legislation becomes inoperative—an analysis of its regulatory functions and the need to continue regulatory activities. (Analyses from the boards scheduled to Sunset in 1997 are due by October 1995.) For a listing of the components of the board’s analysis see Figure 8 (on page 25). The Joint Committee will then hold public hearings to solicit testimony about the boards and the regulatory need in the various professions. These hearings will provide the basis of the Joint Committee’s report to the DCA with recommended reforms. The DCA will incorporate all the preceding reports and public testimony into a final report and recommendation to the Legislature. As structured, the Legislature’s fiscal and policy committees have an opportunity to fully evaluate whether there is a need to improve the regulatory activity, or if the state regulating efforts should be discontinued.

Figure 7

**Department of Consumer Affairs
Sunset Dates for Consumer Boards**

Inoperative July 1, 1997/Repealed January 1, 1998

Board of Accountancy
Athletic Commission
Board of Barbering and Cosmetology
Cemetery Board
Court Reporters Board
Board of Funeral Directors and Embalmers
Board of Registration for Geologists and Geophysicists
Board of Guide Dogs for the Blind
Board of Landscape Architects

Inoperative July 1, 1998/Repealed January 1, 1999

Board of Architectural Examiners
Contractors State License Board
Board of Dental Examiners
Committee on Dental Auxiliaries
Board of Professional Engineers and Land Surveyors
Board of Examiners for Nursing Home Administrators
Board of Pharmacy
Board of Registered Nurses
Structural Pest Control Board
Board of Examiners in Veterinary Medicine
Board of Vocational Nurse and Psych. Tech. Examiners

Inoperative July 1, 1999/Repealed January 1, 2000

Acupuncture Committee
Board of Behavioral Science Examiners
Hearing Aid Dispensers Examining Committee
Medical Board of California
(Including Dispensing Opticians' Board)
Board of Optometry
Physical Therapy Examining Committee
Physician Assistant Examining Committee
Board of Podiatric Medicine
Board of Psychology
Respiratory Care Examining Committee
Speech Pathology and Audiology Examining Committee

Figure 8

**Department of Consumer Affairs
Sunset Provision for Consumer Boards**

Provisions of Board Analysis to Legislature

- A description of mission, goals and objectives in protecting the health, safety and welfare of the public.
- Enforcement priorities of the board, complaint and enforcement data, and budget expenditures, including average and median cost per case and age of case statistics.
- An analysis of the board's fund conditions, sources of revenues, and expenditure categories over the four most recent fiscal years.
- A description of the board's licensing process including the time and costs required to implement and administer its licensing examination.

Delete Funding of Cemetery Board and Board of Funeral Directors and Embalmers

Until the Legislature passes a bill resolving how to structure and fund the Cemetery Board and Board of Funeral Directors and Embalmers, we recommend that the Legislature delete funding proposed for the boards in the Governor's Budget. (Delete \$419,000 under Item 1180-001-717, and \$922,000 under Item 1330-001-750.)

The budget proposes 1995-96 support of \$419,000 for the Cemetery Board and \$922,000 for the Board of Funeral Directors and Embalmers. The proposed expenditures are 100 percent higher than estimated current-year expenditures.

In the 1994 Budget Act the Legislature reduced the expenditure authority for these boards by 50 percent in anticipation that legislation to consolidate the two boards would be enacted before the end of the 1994 session. The consolidation bill, however, was not passed by the Legislature.

In December, the administration, through the Section 27 process, proposed a deficiency augmentation that would have restored the funding deleted by the Legislature. In response to this proposal, the Joint Legislative Budget Committee did not concur in the request. The committee's response stated that:

- Based on an opinion from the Legislative Counsel, the Department of Consumer Affairs can assume clerical, reregistration and investigative duties of the boards.

- The department, by delegation of the boards, can assume the other responsibilities of the boards.
- The functions of those boards could be carried on during the period necessary for legislation to be enacted to clarify the responsibilities in these areas and to provide any necessary funding for the balance of this fiscal year.

In light of prior legislative actions regarding these boards, we recommend that the Legislature delete funding proposed in the budget for them. If legislation to restructure these activities is enacted, the necessary funding should be part of that legislation.

DEPARTMENT OF FAIR EMPLOYMENT AND HOUSING (1700)

The Department of Fair Employment and Housing (DFEH) enforces laws that promote equal opportunity in housing, employment, public accommodations, and that protect citizens from hate violence. Specifically, the DFEH has responsibility for enforcing the state's main equal opportunity law, the Fair Employment and Housing Act (FEHA), and resolving complaints in a timely manner.

The budget proposes expenditures of \$13.5 million (\$10.1 million General Fund) for the support of the DFEH in 1995-96. This represents a reduction of \$700,000 (5 percent) over estimated current-year expenditures.

Fair Housing Laws Now Conform With Feds

We recommend that 19 new positions related to enforcement of fair housing laws be made limited-term positions until the U.S. Department of Housing and Urban Development (HUD) extends the DFEH a permanent agreement.

State law fell out of conformity with federal fair housing standards in 1992 as a result of federal law changes. Since that time, most of the housing discrimination complaints originating in California have been filed with HUD. For example, there were about 1,700 housing discrimination complaints filed in California in 1993, of which about 1,200 were handled by HUD.

Enactment of Ch 1277/93 made the following changes which effectively restored California to substantial equivalency with federal law:

- Made unlawful discriminatory land use regulation, zoning laws, and restrictive covenants.
- Invalidated other FEHA provisions that were inconsistent with federal standards.

Now that substantial equivalency has been reached, the DFEH will process housing discrimination cases originating in California, including those filed directly with the department and those referred to the department by HUD. To deal with the anticipated new workload, the DFEH has

entered into an "Interim Agreement" with HUD that provides the state with \$1.2 million to process the anticipated growth in workload. The department is using these funds to administratively establish 19 positions, which the budget would then establish permanently. As the Interim Agreement expires three months into the budget year, the request builds in spending authority for the entire year in anticipation of receiving more HUD money in federal fiscal year 1996 (which begins October 1, 1995). If HUD determines that the DFEH has met federal performance expectations, HUD may continue to provide federal funds and the DFEH would then be responsible permanently for enforcing fair housing laws. Consequently, the availability of federal funds as of October 1995 is in question. Without taking the precaution of making the requested positions limited-term, the Legislature risks exposing the General Fund to cover the costs of the new positions.

Therefore, given that the continued availability of the federal funds is in question, we recommend that the 19 positions requested in the budget be made limited-term until the HUD funding agreement becomes permanent.

DEPARTMENT OF CORPORATIONS (2180)

The Department of Corporations is responsible for protecting the public from unfair business practices and fraudulent or improper sale of financial products and services. The department fulfills its responsibility through the following major programs: (1) investment, (2) lender-fiduciary, and (3) health care service plans. The department is supported by license fees and regulatory assessments, which are deposited in the State Corporations Fund.

The budget proposes total expenditures of \$36.3 million in 1995-96 which is \$7.3 million or 20.1 percent more than estimated current-year expenditures. This increase is due mainly to (1) a \$3 million augmentation from the Corporations Fund to implement Ch 994/94 (SB 1978, Johnston), which requires the Commissioner of Corporations to license residential mortgage lenders and mortgage loan services and (2) a \$1.4 million augmentation from the Corporations Fund to provide permanent staffing for the regulation of Workers' Compensation Medical Groups.

Blue Cross Restructuring

We recommend that the department report during budget hearings on Blue Cross of California's restructuring plan.

On September 15, 1994, Blue Cross of California submitted a plan to the Department of Corporations for developing new strategies and programs needed to update its public benefit plan. Under this plan, Blue Cross would contribute all of its assets to a new independent tax-exempt charitable foundation, called the California HealthCare Foundation. These assets are currently valued at more than \$2 billion. Given the magnitude of the public benefit plan, we believe the department should report to the Legislature on the plan.

Department Responsibilities. The Department of Corporations administers the Knox-Keene Health Care Service Plan Act, which regulates prepaid health plans. The main objectives of this regulation are to ensure (1) the financial solvency of the plan and (2) the delivery of quality, accessible and cost-effective health care to enrollees of the plan. As a prepaid health plan, Blue Cross is licensed by the department. Also, if the plan is structured as a nonprofit corporation, as in the case of Blue Cross, the

department regulates the plan to ensure that it is in compliance with the Nonprofit Public Benefit Corporation Law. This law requires nonprofit plans to donate full value of their assets to a charitable trust if they convert to for-profit status.

Blue Cross's Restructuring. Blue Cross, the state's largest nonprofit insurer, was established during the early 1930s as a nonprofit public benefit corporation. In 1993, Blue Cross underwent a major restructuring that created Well-Point Health Networks—a for-profit, publicly traded organization within Blue Cross. In effect, the nonprofit Blue Cross insurer spun off the majority of its business into a for-profit business.

As a nonprofit corporation, Blue Cross must comply with the Nonprofit Public Benefit Corporation Law, which requires nonprofit health plans to donate full value of their assets to a charitable trust if they convert to for-profit status. Because Blue Cross maintains its nonprofit corporate shell—even with the creation of the for-profit Well-Point—the Department of Corporations must ensure that Blue Cross is in compliance with the Nonprofit Public Benefit Law.

In order to show that it is in compliance with this law, Blue Cross submitted a plan to the department on September 15, 1994 which (1) separated Blue Cross's public benefit (nonprofit) activities from its commercial (for-profit) business and (2) contributed assets to a new independent tax-exempt charitable foundation, called the California HealthCare Foundation. These assets are currently valued at more than \$2 billion. Also, as part of the plan, Blue Cross committed \$105 million in 1994 to charitable activities. Figure 9 lists these commitments.

The department is currently reviewing the plan and is in negotiations with Blue Cross regarding the plan. The department must approve the plan in order for it to become effective.

Legislative Considerations. Blue Cross's plan could result in over \$2 billion turned over for charitable public purposes and could significantly affect public health policy in California. Therefore, we recommend the department report to the Legislature at budget hearings on the following issues concerning the restructuring:

- An explanation of the plan and Blue Cross's objectives in restructuring.
 - A timeframe describing the stages of the plan.
 - A description of the department's role in regulating the restructuring.
 - An explanation of the potential public benefit donations resulting from the plan and how these donations may affect state and local expenditures on public health programs.
-

Figure 9

**Department of Corporations
Blue Cross of California
1994 Charitable Gifts**

(In Millions)

| | Amount of Gift |
|---|----------------|
| Immediate Improvement in Delivery of Services | |
| Emergency Medical Systems | \$10.0 |
| Community Clinics throughout California | 12.4 |
| Drew Medical School—Urban Health Initiative | 2.5 |
| UCSF—Fresno, Rural Health Initiative | 2.5 |
| Breast Cancer Treatment Program | 12.4 |
| California Community Foundation | (3.1) |
| San Diego Community Foundation | (3.1) |
| San Francisco Foundation | (3.1) |
| East Bay Community Foundation | (3.1) |
| Loma Linda University Children's Hospital | 1.0 |
| Lucile Salter Packard Children's Hospital at Stanford | 1.0 |
| Memorial Miller Children's Hospital | 1.0 |
| Valley Children's Hospital—Fresno | 1.0 |
| Children's Hospital—Los Angeles | 1.0 |
| Children's Hospital—Orange County | 1.0 |
| Oakland Children's Hospital | 1.0 |
| Children's Hospital—San Diego | 1.0 |
| CaliforniaKids | 22.2 |
| American Cancer Society | 1.0 |
| American Heart Association | 1.0 |
| American Lung Association | 1.0 |
| March of Dimes | 1.0 |
| Pediatric AIDS Foundation | 1.0 |
| California Health Care Partnerships | 5.0 |
| | \$80.0 |
| Near-Term Improvement | |
| Health Services Research Foundation | \$2.5 |
| National Health Foundation | 2.5 |
| Health Care Education, Research & Evaluation Foundation | 0.6 |
| University of Southern California, Managed Care Chair | 2.5 |
| University of California, Berkeley, Managed Care Chair | 2.5 |
| Unified Medical Quality Commission | 2.5 |
| California Academy of Family Physicians Foundation | 2.5 |
| Emergency Response System, City of Los Angeles | 1.5 |
| Roybal Institute of Gerontology | 1.0 |
| Poison Control Centers | 5.0 |
| | \$23.1 |
| California HealthCare Foundation | |
| Needs Assessment | \$2.0 |
| Total | \$105.1 |

HOUSING AND COMMUNITY DEVELOPMENT (2240)

The mission of the Department of Housing and Community Development (HCD) is to help promote and provide decent housing for all Californians. As part of this mission, the department is responsible for implementing and enforcing building standards. The department also administers a variety of housing development and rehabilitation programs, and provides policy advice and statewide guidance on housing issues.

The budget proposes expenditures of \$173.5 million for 1995-96. This is \$33.4 million, or 20 percent, less than estimated current-year expenditures. Most of this decrease reflects reduced estimates of local assistance to be provided under various federal programs (-\$22.9 million) and the Century Freeway Program (-\$12.3 million), offset slightly by increased program administrative costs (\$3.7 million). The budget proposes General Fund expenditures of \$10 million for 1995-96, a decrease of \$1.5 million from the current year.

HCD'S LOAN MONITORING PROPOSALS

Since 1980, the HCD has made nearly 6,000 loans to assist the development, repair, or rehabilitation of 27,000 housing units. The value of the HCD's housing loan portfolio is about \$700 million.

The HCD's responsibilities for these loans continue long after the monies are provided. Specifically, the HCD has ongoing loan servicing responsibilities, including collecting any required principal or interest payments and ensuring that owners pay property taxes and maintain hazard insurance. (These activities protect the state's *fiscal* interests in the loans.) The HCD also reviews about 11 percent of the loans to verify that the property is well maintained and used in accordance with program requirements—most commonly that the housing is rented to low-income people. (These activities protect the state's *policy* interests in the loans.) The HCD refers to these wide-ranging activities as loan “monitoring and management.”

Below, we discuss two budget proposals pertaining to HCD's loan monitoring and management program. The first proposal focuses on

\$447 million of loans funded through three general obligation bond measures (the Earthquake Safety and Housing Rehabilitation Bond Act of 1988—Proposition 77, and the Housing and Homeless Bond Acts of 1988 and 1990—Propositions 84 and 107). The second proposal focuses on \$249 million of loans provided under housing programs funded by the General Fund and a variety of special funds. For simplicity, the HCD refers to the first group as “bond-funded” loans and the second group as “state-funded” loans.

Monitoring Program Costs Too Much

We recommend that the Legislature delete \$800,000 and ten positions from the bond-funded housing program administrative staff. We further recommend the Legislature direct the HCD to redesign its loan monitoring program to reduce costs and preserve the programs’ remaining administrative reserves for the longest period possible. (Reduce Item 2240-001-714 by \$400,000 and Item 2240-001-788 by \$400,000.)

Ever since passage of the three housing bond measures, the Legislature has expressed concerns regarding the HCD’s costs to administer the bond-funded housing programs. (Figure 10—see next page—provides information about these housing programs.) In January 1994, in fulfillment of a long overdue legislative request, the HCD projected the workload, staff needs, and resulting long-term administrative costs for these housing programs. In reviewing the HCD’s cost estimate in the 1994 *Analysis*, we noted that the Legislature would face difficult choices in the future because the HCD’s projected costs for these programs greatly exceeded the funds set aside from the bond acts for this purpose. We recommended that the HCD take action to reduce its long-term monitoring costs and prolong the life of the administrative reserves.

One Year Later, Administrative Cost Estimates Have Grown—Not Shrunk. As Figure 11 (see page 35) illustrates, the budget proposes 45 bond-program administrative positions for 1995-96—or 17 more positions than the HCD projected in 1994. The HCD explains that these 17 positions were excluded from its earlier estimate due to errors and optimistic assumptions in its workload analysis. In addition, although the department continues to study possible changes to its loan monitoring program, the HCD has not implemented any changes that would reduce the level of staff needed.

Administrative Funds Running Out. While all housing experts agree that some level of loan monitoring is needed during the 25- to 55-year terms of the bond-funded loans, the only monies available to pay for these activities are a series of program-specific administrative reserves. These reserves contained \$59 million when they were established between

1988 and 1990, but only \$30 million remains. Given the HCD's revised estimate of staff needs, we estimate that the department will deplete each program's remaining administrative reserves within four to 15 years.

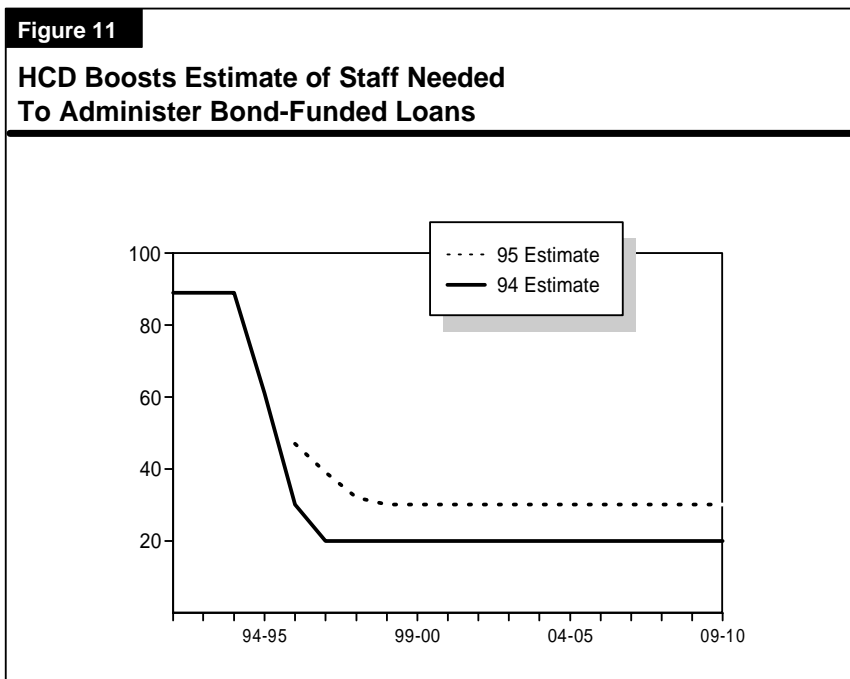
| Figure 10 | |
|---|-----------------------------------|
| Department of Housing and Community Development Overview of Housing Bond Programs Authorized by Propositions 77, 84, and 107 | |
| (In Millions) | |
| Program/Purpose | Total Bonds Authorized |
| Rental Housing Construction Program | |
| Construction of multifamily housing | \$300 |
| California Housing Rehabilitation Program | |
| Health and safety rehabilitation of multifamily and owner occupied housing | 117 ^a |
| Seismic and health and safety rehabilitation of multifamily housing | 33 ^a |
| Acquisition and rehabilitation of residential hotels | 40 |
| Family Housing Demonstration Program | |
| Construction of family housing | 15 |
| Emergency Shelter Program | |
| Construction and rehabilitation of emergency shelters | 35 |
| Office of Migrant Services | |
| Construction and rehabilitation of migrant farm worker centers | 10 |
| Total | \$550 |

^a Proposition 77 authorized a total of \$150 million for the CHRP. Of this amount, \$80 million was to be used for seismic repairs and \$70 million for health and safety rehabilitation. Because the HCD received few applications for seismic renovation funds, the Director of the HCD transferred \$47 million of the funds for seismic renovation to the funds for health and safety rehabilitation. Figure 10 shows the revised amounts provided for these programs.

After each administrative reserve is depleted, the Legislature will have two primary options to finance the continuing loan monitoring requirements:

- **Appropriate General Fund Monies.** In today's dollars, the annual cost would be about \$1 million to \$2.5 million annually for about 40 years.
- **Direct the HCD to Use Housing Loan Repayments to Pay for Loan Monitoring Costs.** This option is unlikely to generate sufficient funds on an annual basis to pay all monitoring costs. This option also runs contrary to the Legislature's intent that the loan repay-

ments be lent out again and used as a permanent source of funding for affordable housing.



Could the HCD's Monitoring Costs Be Reduced? Our review indicates that there is considerable evidence the HCD could reduce its loan monitoring costs without impairing the effectiveness of its program.

We note, for example, that the HCD's monitoring costs are very high—\$5,700 annually per loan (which equates to about \$200 per apartment unit). These costs are attributable to the HCD's choice of a very staff-intensive monitoring design (a ratio of one bond-funded staff position per 11 rental development loans)—and to the HCD's decision to send one physical inspector and one program staff expert to every rental development every year (at an average annual cost of \$1,750 per loan). Information provided to the Housing Task Force (convened at the Legislature's direction by the Business, Transportation and Housing Agency) indicates that other public and private institutions engaged in similar monitoring activities do so at lower costs.

Our review also notes that the HCD's monitoring system fails to achieve economies by reducing its level of monitoring over rental housing developments which are actively monitored by other parties. As we

discussed in last year's *Analysis*, affordable housing projects in California frequently receive financing from four or more public and private sources—and frequently are monitored by as many institutions. As an example, we reviewed the 21 developments in the City of Los Angeles which received funding through the HCD's Rental Housing Construction Program. Of these 21 projects, we found that:

- Twenty projects are also being monitored for compliance with affordable housing occupancy requirements by the California Tax Credit Allocation Committee.
- Twenty projects are also being monitored for their fiscal and physical condition by tax credit investors who face strong fiscal pressures to ensure the viability of the projects.
- Nineteen projects are also being monitored for affordable housing occupancy requirements by the City of Los Angeles.
- Ten projects are being monitored for their fiscal condition by private lending institutions.
- Eight projects are also being monitored for compliance with the HCD's Century Freeway Program affordable housing requirements.
- Two projects are also being monitored for compliance with various federal affordable housing requirements.

In our conversations with the department regarding this overlap of monitoring efforts, the HCD points out that these other parties' monitoring procedures, practices, and standards are not identical to that of the HCD. While this is true, our review indicates that the HCD simply does not have the resources necessary to independently administer an extensive and comprehensive monitoring program over all the bond-funded loans. As a result, economic reality demands that the HCD acknowledge the monitoring efforts of other parties, adopt cooperative agreements where possible, and supplement other parties' monitoring efforts only to the extent necessary to protect important state fiscal and policy objectives.

Recommendation. The HCD has proposed a loan monitoring system which is so costly that it will run out of funds decades before its obligations are complete. Accordingly, we believe it is imperative that the HCD redesign its monitoring system to reduce costs, eliminate redundancies, and focus on only those activities which are critical to protect the state's fiscal and broad policy interests in the housing loans.

In order to begin such a process, we recommend that the Legislature

set a goal for the HCD of prolonging the life of the bond-funded program administrative reserves by 33 percent over current projections. Based upon our review of organizations engaged in similar monitoring efforts, we believe this level of savings should be possible without impairing the HCD's monitoring program. To ensure that the HCD takes steps towards achieving this goal, we recommend that the Legislature reduce the HCD's funds for administering the bond-funded programs by \$800,000 and ten positions in the budget year. If sustained in the future, this level of staffing reduction would enable the HCD to pay for its monitoring costs from bond reserves for one to five years longer than currently anticipated. Prolonging the life of the bond reserves would have considerable fiscal advantages to the state.

Need to Reevaluate Monitoring Proposal for State-Funded Loans

We recommend deletion of \$1.2 million and 15 positions requested to monitor the HCD's state-funded loan portfolio because the HCD (1) should ensure that its monitoring program reflects the state's limited policy interest in many of the loans and (2) should explore less costly options for monitoring loans in which the state has broad policy interests. (Reduce Item 2240-001-001 by \$1.2 million and make corresponding reductions to subsidiary special funds.)

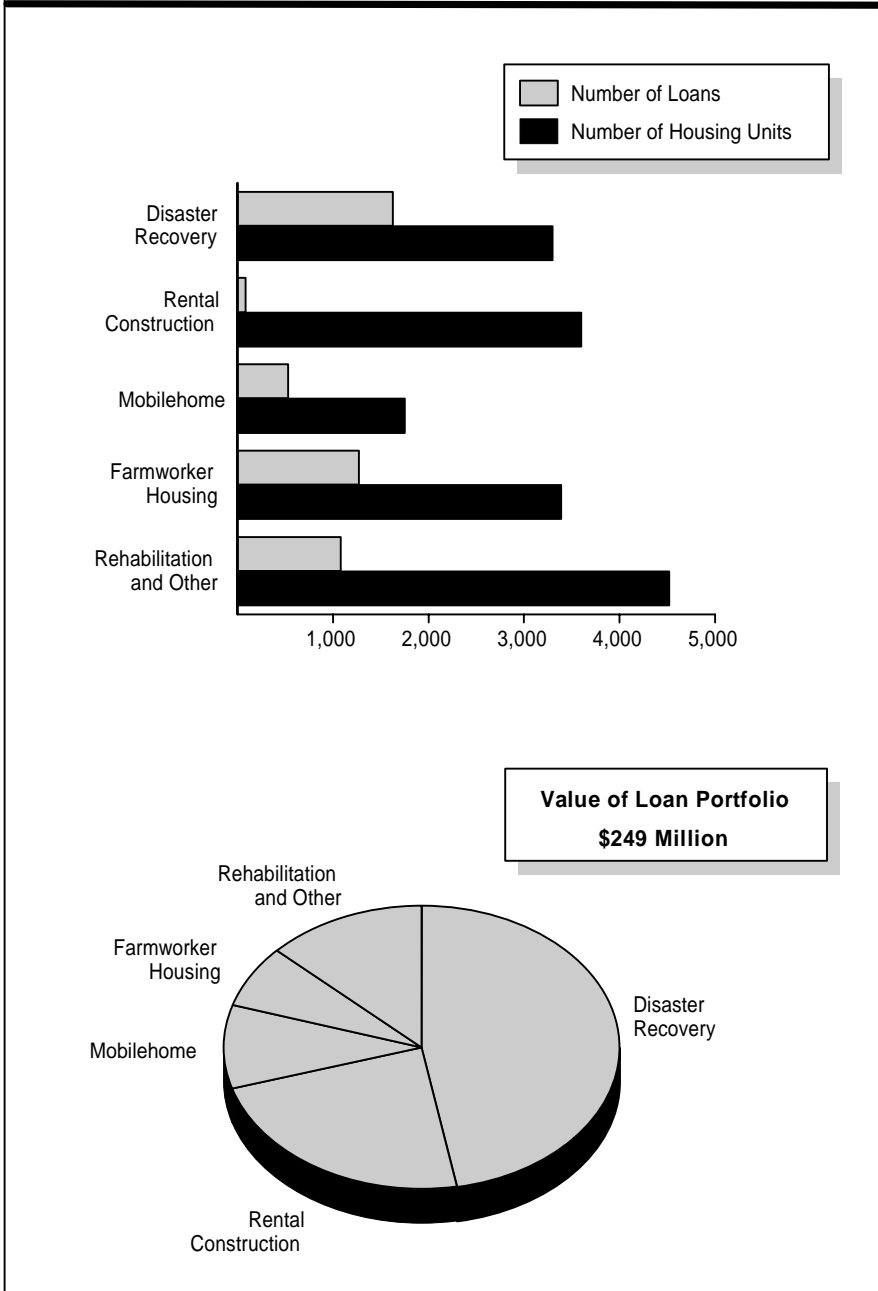
Over the last 15 years, the HCD has made over 4,600 low-interest loans under 17 state-funded housing programs. These loans have assisted over 16,500 housing units, as shown in Figure 12 (see next page).

The HCD currently has 28 staff assigned to monitoring these state-funded loans. Two additional staff in the HCD's loan monitoring and management unit inspect the construction of certain facilities for tribal organizations (under the California Indian Assistance Program—CIAP) and farm workers (under the Office of Migrant Services—OMS—program). The cost of most of these positions is paid by special funds.

Additional 16 Positions Proposed. The budget proposes to redirect 16 positions (from various programs in the HCD with declining workloads) to the loan monitoring and management unit. The HCD explains that these positions are needed "to ensure that this significant publicly funded housing resource is preserved, to protect the health and safety of low-income residents, and to protect the state's investment." To that end, 15 of the positions will monitor loans made under the state-funded loan programs—and one position will inspect facilities under the CIAP and OMS programs. All positions will be established on a three-year, limited-term basis.

Figure 12

**HCD's State-Funded Loan Portfolio
Loans, Value and Housing Units**



Our review indicates that the one inspection position for the CIAP and OMS programs appears reasonable and we recommend its approval. The rest of this analysis focuses on the 15 proposed loan monitoring positions.

HCD Analysis Does Not Ask the Right Question. To document its request for the additional loan monitoring staff, the department provided summary information on all the programs in its state-funded loan portfolio, itemized the activities it believed necessary for proper loan management, and estimated the time needed to complete each activity. This report documents the need for 15 additional monitoring positions.

While the HCD's report contains a great deal of valuable information, we note that the HCD's study fails to examine the central question: What level of monitoring is *appropriate* given the state's fiscal and policy interests in this loan portfolio?

LAO Analysis. In order to address this question, we calculated the HCD's monitoring costs by loan, by program, and by housing unit. We then reviewed the state's *fiscal* interest in the portfolio, and considered whether the state has any ongoing *policy* interest in the loans, such as the maintenance of rent affordability or other requirements.

Figure 13 (see next page) presents data from our analysis. The figure groups loans in two categories: (1) *investment loans* in which the HCD's current and future monitoring responsibilities are limited to protecting the state's fiscal investment and (2) *public purpose loans* in which the HCD's monitoring efforts seek to ensure the achievement of certain policy objectives, as well as protect the state's fiscal investment. Below, we discuss four findings which stem from our analysis.

The State Has Little Ongoing Policy Interest in Much of the State-Funded Loan Portfolio. Specifically, 91 percent of the loans—and about half the value of the loan portfolio—fall into the category of “investment loans.” In these cases, the state achieved its policy objectives when it made the loans. (These policy objectives include assisting property owners rebuild after a disaster and assisting low-income Californians build or purchase a home.) At this point, the state's only long-term interest in the loans is in the repayment of state funds (\$124.5 million in total—most of it to be deposited to the General Fund).

The State's Fiscal Stake in Most Individual Loans Is Minor. The average loan in the portfolio is about \$53,000. The average loan amount under four investment loan programs is less than \$13,000. Most of the loans earn only 3 percent simple interest per year—and the interest is frequently deferred until the end of the loan term.

Figure 13**HCD's State-Funded Loan Portfolio**

| Program | Average Loan | Number Of Loans | Annual Monitoring Costs | |
|--|-----------------|-----------------------|-------------------------------|-------------|
| | | | Per Loan | Per Unit |
| Investment Loans Program | | | | |
| California Natural Disaster Assistance Program, owner program | \$54,428 | 1,024 | \$288 | \$288 |
| Farmer Work Housing Grant, owner program | 10,212 | 1,224 | 184 | 184 |
| Mobilehome Park Resident Ownership Program, owner program | 28,039 | 510 | 365 | 365 |
| California Self Help Housing Program | 12,374 | 396 | 257 | 257 |
| State Earthquake Rehabilitation Assistance Program, owner program | 22,108 | 389 | 405 | 405 |
| Deferred Payment Rehabilitation Loan Program, owner program | 9,055 | 254 | 340 | 340 |
| California Homeownership Assistance Program | 26,020 | 196 | 405 | 405 |
| Grove Shaffer | — ^a | 80 | 56 | 56 |
| California Natural Disaster Assistance Program, rental program (16 units and fewer) | 88,333 | 58 | 1,605 | 524 |
| State Earthquake Rehabilitation Program, rental program | 208,333 | 24 | 4,186 | 353 |
| California Natural Disaster Assistance Program (17 units and more) | 1,730,918 | 4 | 5,448 | 91 |
| Public Purpose Loans | | | | |
| Deferred Payment Rehabilitation Loan Program, rental program | \$54,000 | 100 | \$2,785 | \$150 |
| Special-User Housing Rehabilitation Program, rental program | 239,344 | 61 | 6,246 | 218 |
| California Natural Disaster Assistance Program, rental program (16 units and fewer) ^b | 83,333 | 55 | 1,605 | 524 |
| Rental Housing Construction Program, original program | 1,177,551 | 49 | 6,275 | 149 |
| Farmworker Housing Grant Program, rental program | 104,082 | 49 | 5,441 | 123 |
| Rental Housing Construction Program, annuity program | — ^a | 39 | 4,742 | 120 |
| Mobilehome Park Resident Ownership Program, rental program | 422,727 | 22 | 6,275 | 110 |
| California Natural Disaster Assistance Program, rental program (17 units and more) ^b | 1,730,918 | 16 | 5,448 | 91 |
| ^a HCD provided no loan funds to these development. | | | | |
| ^b CALDAP loans without long-term affordability requirements are listed above as "investment" loans. | | | | |

HCD's Proposed Monitoring Costs Are Significant, Long Term, and—in Some Cases—May Exceed Special Fund Revenues Available for This Purpose. The HCD proposes to spend \$3.4 million in 1995-96 to monitor its state-funded loan portfolio. Of this amount, \$1.5 million would be spent monitoring investment loans and \$1.9 million will be spent monitoring public purpose loans. A substantial portion of these monitoring costs will continue annually for 15 to 30 years. Our review indicates that it is likely that some program's special fund resources will be inadequate to pay for this proposed level of monitoring. Thus, additional General Fund monies or statutory changes (to permit sharing of special fund resources) would be needed.

The Cost of Some Loan Monitoring Appears Unnecessarily High. The HCD's proposed monitoring for public purpose loans costs up to \$6,275 annually per loan, or up to \$524 per apartment unit. As in the bond-funded portfolio, the HCD proposes to send a construction inspector and program expert to each rental development annually—and does not propose to reduce the level of monitoring over developments which are actively monitored by other institutions. The HCD's costs for monitoring investment loans are lower, but sometimes are very high in relation to the state's fiscal interest in the loan.

Recommendation. Given the findings outlined above, we believe that the HCD's proposal to expand its monitoring program must be thoroughly reevaluated. Accordingly, we recommend the Legislature reject the HCD's proposal to add \$1.2 million and 15 monitoring positions and direct the HCD to:

- Assess the level of staff needed to monitor investment loans on the basis of maximizing the state's fiscal return.
- Analyze the potential for reducing state monitoring costs by offering attractive early loan retirement options, selling all or part of the \$124.5 million investment loan portfolio, or contracting with the private sector or the California Housing Finance Agency for loan servicing.
- Prepare an assessment, by program, of proposed monitoring costs and revenues expected to be available for this purpose.
- Pursue greater efficiencies in the monitoring of public purpose loans, such as described in the previous analysis of the bond-funded loan portfolio.

Finally, information regarding the allocation of cost by subsidiary fund for this proposal was not available at the time this analysis was prepared. The department should submit this information, prior to

budget hearings, so that changes to the appropriate items in the Budget Bill can be reflected.

OTHER ISSUES

Farm Worker Housing Programs: Progress, but More Work Needed

Two housing programs that primarily serve farm workers—the seasonal housing communities operated through the Office of Migrant Services (OMS) and the Employee Housing Program (EHP)—have long had serious budgetary problems. The budget proposes increasing the OMS’s annual revenues, but proposes no solutions to the EHP’s budgetary problems. We recommend the department report before the time of budget hearings on its recommendations for funding the Employee Housing Program.

In last year's *Analysis*, we reviewed two HCD programs that primarily serve farm workers: (1) the Office of Migrant Services (OMS), which operates seasonal farm worker housing communities throughout the state, and (2) the Employee Housing Program (EHP), which provides for annual health and safety inspections and permitting of privately owned housing for farm workers and other employees. We found these programs had serious budgetary problems that threatened program performance. Below, we review our findings from last year—and discuss the HCD's progress in finding solutions.

Office of Migrant Services. In the *Analysis* last year, we commended the HCD for launching a \$50 million five-year program to reconstruct or rehabilitate nearly 2,000 seriously dilapidated farm worker housing units. We noted, however, that the program's ongoing resources were not sufficient to pay for program costs—including the cost of routine maintenance needed to ensure that the housing units do not fall to substandard conditions once again. We estimated that the program's funding gap was approximately \$1 million annually and recommended the department modestly increase farm worker rents to offset part of this amount.

The budget proposes two actions to increase revenues to the OMS. First, the budget proposes to increase rents charged to farm workers, beginning after each housing unit is repaired or reconstructed. The rent increase, which would not exceed traditional housing affordability guidelines, should raise \$400,000 in 1995-96 and somewhat higher amounts in future years. Second, the budget proposes a \$600,000 General Fund baseline increase for the OMS program. Our review indicates that these ac-

tions should place the OMS program on sound financial footing and, accordingly, we recommend approval.

Employee Housing Program. In the *Analysis* last year, we noted that the department was failing to fully carry out its inspection and local government oversight responsibilities and that the EHP's annual report to the Legislature was rife with errors. Because we found that many of the EHP's problems stemmed from an imbalance between program responsibilities and revenues, we recommended that the department develop a proposal for increasing program revenues—or modifying program responsibilities. We also recommended that the department improve program management and correct the errors in its report.

Over the course of 1994, the department hired a manager for the EHP, took steps towards addressing the errors in its report, and modestly increased its inspection activities. While these changes are commendable, they do not solve the serious program shortcomings identified in the 1994 *Analysis*. The department informs us that it is considering a legislative proposal to revamp the EHP, but has not provided any details on the elements of its proposal. In order for the Legislature to have the information it needs to review the proposed budget-year expenditures for the EHP, we recommend the department submit a report to the Legislature outlining its proposal for this program.

How Much Should it Cost to Provide Housing Assistance?

Many proposals are being debated which would reduce federal Housing and Urban Development program expenditures—and send significant housing resources to states and localities. If such a proposal is enacted, the Legislature and administration will need to evaluate alternative ways to use these resources to provide housing assistance to needy Californians. We review the costs of California's last major housing effort—the bond-funded programs—and discuss options for providing assistance at lower costs.

The HCD's 1994 report on long-term costs to administer the bond-funded housing programs represented the Legislature's first look at the *full* cost of state administration of housing programs—from the development of program regulations to the completion of loan monitoring. In this analysis we:

- Update the HCD's 1994 cost estimate to reflect the department's actual costs and current staffing plan.
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- Suggest options for designing less costly ways of providing housing assistance.

LAO Estimate of Long-Term Costs. Figure 14 presents our estimate of the HCD's long-term costs to administer the three large bond-funded rental housing programs: the Rental Housing Construction Program, the California Housing Rehabilitation Program (rental component), and the Family Housing Demonstration Program. (Unlike the HCD's 1994 estimate, future cost data in Figure 14 are *not* adjusted for inflation.)

| Figure 14 | |
|--|-----------|
| Department of Housing and Community Development Projected Long-Term Administrative Costs for Three Bond-Funded Programs | |
| (Dollars in Thousands) | |
| Total loans provided | \$429,200 |
| Long-term administrative costs ^a | 107,041 |
| Administrative costs as a percent of loan amount | 25% |
| ^a Future costs not adjusted for inflation. | |

As Figure 14 indicates, we estimate the full cost of administering the three housing bond programs to be over \$100 million—or approximately 25 percent of the amount issued as housing loans. Another way to think about these estimates of administrative costs is to view them as *roughly* the amount of money that would need to be placed into an account—earning interest at a rate equal to inflation—and spent only for administration. For these three rental programs, we estimate that approximately \$400,000 per rental housing development—or \$10,000 per apartment unit—would need to be placed into such an administrative reserve at the time the program was created. (Of course, should the interest earned on the monies in the reserve account *exceed* inflation, the amounts placed into the account could be somewhat lower.)

What Do These Data Suggest for Future Housing Programs? In terms of future programs, these cost data suggest that if the federal government transfers additional housing resources to the states as is currently proposed, the Legislature should:

- Evaluate the *full* costs of administering housing assistance as it reviews alternative program designs.

- Examine a wide range of options for providing housing assistance including vouchers, grants to housing developers, and contracts with private apartment owners. Many analyses have shown these options to have administrative costs considerably lower than the state's current bond-funded programs.
- Consider transferring federal housing assistance resources to local communities as block grants. This would promote flexibility in meeting local housing needs—and would enable local governments to provide larger subsidies to affordable housing developments. (Providing larger subsidies would, in turn, reduce the number of financing sources developers must assemble to fund affordable housing developments—and help eliminate unproductive legal and administrative costs associated with this financial “layering.”) Local government use of these block grant revenues could be measured by appropriate performance standards.

TRADE AND COMMERCE AGENCY (2920)

The Trade and Commerce Agency is designated as the state's primary economic development entity for promoting the establishment, retention, and expansion of business, employment, and international trade in California. It promotes tourism and foreign investment as well. The Agency also has been designated as the entity leading the state's efforts in defense conversion.

The budget proposes expenditures of \$72 million from various funds (\$43.8 million General Fund) for the Trade and Commerce Agency in 1995-96. This is \$0.5 million, or 0.7 percent, more than estimated current-year expenditures. This includes a \$7.6 million increase from the General Fund (21 percent over current-year expenditures). The General Fund increase is offset by both increases and decreases in various special funds, including: (1) a \$6.4 million reduction in the Small Business Expansion Fund, which is used to make loans, guarantees and restricted investments to small businesses, and (2) a \$4.5 million increase in the Rural Economic Development Infrastructure Bond Fund, which is used to provide loans to local governments for infrastructure projects.

Agency Budget Requests. The budget for the Agency includes requests to increase General Fund appropriations by \$7.6 million and add 75 positions. In nearly every instance where the agency has requested these increases, the supporting documents fall far short of substantiating the need or benefit for the request. In general, the agency expresses a desire to undertake certain new tasks or increase an effort in existing tasks but does *not* identify a specific problem or quantify how the proposed increases will improve the agency's operations. Our recommendations reflect the agency's inadequate documentation submitted in support of these requests.

Agency's Request to Expand Foreign Offices Not Justified

We recommend that the Legislature delete \$2.4 million in General Fund expenditures and 23 positions requested for the expansion of the Foreign Office Program because the agency has not justified the need for additional staff and five new field offices. (Reduce Item 2920-001-001 by \$2.4 million.)

The budget proposes \$2.4 million and 23 positions to expand the state's Foreign Office Program. Of this amount, \$1.4 million and 13 positions would be added to existing foreign offices. The remaining \$1 million and ten positions would be used to establish five new offices.

Background. Currently, there are six foreign offices located in Mexico, Hong Kong, London, Frankfurt, Japan, and Taiwan. Another office in Sub-Saharan Africa that was approved by the Legislature in the 1994-95 Budget Act has not been established. The combined budget for these offices is \$2.6 million and 25 positions, which includes the six director positions (one for each office—including one authorized for Sub-Saharan Africa—with one director for both London and Frankfurt). The purpose of these offices is to attract foreign investment to California by establishing “in-country” relationships with foreign businesses or potential investors.

Additional Staff for Existing Offices Is Not Justified. The proposal for existing offices represents more than a 50 percent increase in the current budget and staff. The agency claims that the purpose of adding the positions—trade specialists—to existing locations is based on the business potential for small and medium-sized California companies to export products to foreign countries. The agency determines “business potential” by the growth of California exports by country and by industry. It claims that, in general, one trade specialist is necessary to cover “basic marketing activities”, handle a basic level of “trade lead collection”, and organize promotional events.

The agency, however, has not defined what these positions are to do and what can be expected from their efforts. For instance, the agency has not clearly defined “basic marketing activities” and to what degree they need to be covered to benefit the state, nor has it quantified the amount of trade lead collections that should be handled by each position or what “handling” these leads means. While the agency claims that it is reasonable to expect two successful clients for each new staff member it has not clearly defined who the clients are or the basis on which they would be deemed successful. Basically, the agency has proposed additional staff at existing foreign offices without developing any substantive justification for the need or benefit to the state.

New Locations for Offices Not Yet Determined. The agency informs us that it is conducting an analysis of the best sites for the new foreign offices and that this report is scheduled to be completed at the end of March 1995. Thus, at the time this *Analysis* was prepared, the data to support the request for a \$1 million General Fund augmentation to establish five new offices was still being developed. However, based on the agency's information concerning expansion of existing offices, the benefit of the *existing*

offices, let alone *new* offices, is questionable. Until the agency can clearly demonstrate the benefit of the existing offices *and* the need/benefit of any new offices, the Legislature should not expand the number of offices.

In view of the above, we recommend that the Legislature delete \$2.4 million and 23 positions included in the budget for expansion of the program.

Funding for Foreign Offices Should Be Clearly Displayed in Budget Bill

We recommend that the Legislature add an item to the Budget Bill to clearly identify the amount of funds budgeted for each foreign office. (Reduce Item 2920-001-001 by \$6 million and add Item 2920-012-001 in the amount of \$6 million.)

The budget includes \$6 million for 12 foreign offices. There is no clear Budget Bill display of the costs associated with the distinct out-of-country operations of each office. Each office operates separately within a foreign country, and a clear distinguishable budget for the General Fund support of these offices is warranted. Therefore, we recommend the Legislature add an item to the Budget Bill identifying the budget for each foreign office.

Proposal to Expand Foreign Investment Program Not Justified

We recommend that the Legislature delete \$342,000 from the General Fund and 4.5 positions for the expansion of the Office of Foreign Investment (OFI) program because the agency has not demonstrated the value this additional staff will add to the program. (Reduce Item 2920-001-001 by \$342,000.)

The budget proposes \$342,000 and 4.5 positions for expansion of the OFI staffing in the agency's in-state field offices. The mission of the OFI, currently comprised of 5.5 positions, is to attract foreign companies to California. The field offices, comprised of a total of 30 positions, act as the regional coordinators in facilitating business start-ups or retentions. For example, if a regional office is informed of a business threatening to leave California, it will try to prevent this business from leaving by setting up discussions among key players in the business environment, such as government regulators and local chambers of commerce.

The agency proposes this additional staffing of international specialists for the four regional offices to identify existing foreign businesses in the state, review any plans these businesses may have for leaving the state and design action plans to retain those businesses. In addition, the agency proposes that the office will expand “inbound investor missions” and increase the number of “site tours.” Inbound investor missions are structured events where a delegation of potential foreign investors travel to California, at their own expense, to visit the state’s key industrial and academic offerings in a selected industry. Site tours are conducted when an individual investor travels to California to visit specific locations that meet their project requirements.

Unclear Workload Indicators for Additional Staff. The agency does not have workload indicators for the additional positions so that it can ensure these positions add value to the program. For example, the agency claims that there is a large number of “plans” for businesses threatening to leave California that need to be reviewed by agency staff. However, the agency has not quantified the number of plans, indicated how many plans each position would review or how this review would be effective in convincing a business to stay in California. Also, the agency hasn’t justified the value added by increasing office staff for more inbound investor missions and site tours. If the expenses of these activities are supported by private businesses, it isn’t clear why General Fund-supported positions should be involved in these activities. Because the agency has not shown that these positions add value to the existing program, we recommend that the Legislature delete \$342,000 under Item 2920-001-001 and the 4.5 positions.

General Fund Increase for International Tourism Program Not Justified

We recommend that the Legislature delete \$1.8 million in General Fund expenditures and eight positions for expansion of the international tourism program because the agency has not demonstrated how it would effectively use the monies. (Reduce Item 2920-001-001 by \$1.8 million.)

The budget proposes a \$1.8 million General Fund augmentation and eight positions for the agency to implement a marketing plan to increase international tourism to the state. The agency indicates that the objective of this plan is to facilitate and increase the use of California as a “travel product” on the part of tour operators, travel agents and travel writers in foreign countries. The plan has two components, as discussed below.

Expanded Program Not Justified. As part of its new international tourism marketing plan, the agency first proposes \$375,579 and six positions (five full-time and two half-time positions in seven foreign offices) for handling consumer inquiries, mainly telephone calls, about travel to California. The agency claims that the foreign offices do not have the resources to handle these inquiries and such inquiries are interfering with the offices' primary operations. The agency, however, has not shown what operations are impaired or how the offices' operations will be improved by adding this staff.

The agency should pursue more cost-effective options for addressing this issue. For example, rather than add permanent positions for answering telephone calls, the agency could set up telephone answering machines that could provide information either by recording or fax. The agency currently has a tourism information system like this in the United States. Also, below we discuss the agency's contracts with travel representatives. One service these contractors provide is answering consumer inquiries. If the agency is already paying for this service, it is not clear why they need additional resources for this purpose.

Increase for Tourism Contracts Not Justified. Also as part of this marketing plan, the agency proposes to use \$1.5 million to increase contracts for travel trade representation services abroad. Currently, the Division of Tourism has contracts with travel representatives in Japan, the United Kingdom and Germany. The annual cost for the Japan contract is \$150,000, and the other two are \$130,000 each. The agency pays these contractors for what it calls "essential day-to-day contact" with the travel trade in these countries. The contacts include conducting educational seminars for travel, answering consumer inquiries about travel to California, and marketing California as a travel product to the travel industry.

The agency proposes to increase these three contracts by \$280,000 in total, as well as establish contracts—totaling \$1.1 million—with representatives in Mexico, Australia-New Zealand, Asia, South America and Korea. In addition, the agency proposes \$140,000 and two positions, an Associate Tourism Specialist and an Office Technician for the Sacramento Division of Tourism to liaison and manage the contractors and overseas office involvement in tourism activities.

Contract Increases Lack Justification. The agency claims that increasing contract amounts and establishing new representatives can be expected to result in at least an average of one additional tour night in California among two percent of the tour passengers per market/country. The agency, however, has not provided a methodology for how it arrived at this expectation, such as showing that a specific increase for a contract was the direct cause of an extra

night's stay by a tour passenger in California. In short, the agency has not indicated benefits directly resulting from the specific contract increases it proposes.

Moreover, the agency claims that expanding the work of existing overseas contractors and establishing new ones necessitates the addition of two positions—an Associate Tourism Specialist and an Office Technician in California. The agency has not clearly defined the additional workload to justify these positions.

In summary, we recommend the Legislature delete \$1.8 million under Item 2920-001-001 and eight positions for expansion of the international tourism program.

General Fund Augmentation for Currency Fluctuation Not Justified

We recommend that the Legislature delete \$199,000 in General Fund expenditures proposed for the adjustment of foreign office budgets according to currency exchange rates because the basis for this augmentation is not justified. (Reduce Item 2920-001-001 by \$199,000.)

The budget includes \$199,000 from the General Fund to adjust the operating and equipment expenses for four foreign offices—London, Japan, Hong Kong and Germany—according to currency exchange rates. The agency arrived at this amount by comparing the exchange rate on January 3, 1993 to the rate on December 15, 1994, for the four respective countries. In requesting the \$199,000 General Fund augmentation, the agency has not identified the exact uses of the monies or the detrimental effect on office operations as a result of currency fluctuations. Moreover, because exchange rates fluctuate daily and can result in a higher purchasing power of the dollar rather than lower, these fluctuations can also result in increased *savings* to certain foreign office budgets rather than increased costs. It is not clear why the agency cannot work within its existing budget to address these fluctuations. Therefore, we recommend that the Legislature delete the \$199,000 augmentation.

Agency's Request to Convert Oversees Contractors is Not Needed

We recommend that the Legislature not approve \$385,000 in General Fund expenditures for the agency to establish 19 state exempt employee positions in place of consultant contracts at foreign offices because the agency can continue the contracts for less cost to the General Fund. (Reduce Item 2920-001-001 by \$385,000.)

The budget proposes \$385,000 in General Fund expenditures for the agency to convert 19 independent contractors to exempt state employee status. These nineteen independent contractors currently serve as staff in the seven foreign offices. The directors of the offices are exempt state employees who serve at the pleasure of the Governor. As with any state agency, the consultant contracts are subject to annual approval by the Department of General Services.

Conversion is Not Justified. The agency claims that there are legal problems in having independent contractors (1) housed in agency offices, and (2) take direct supervision from an employee of the state. The agency states, however, that it would be possible to contract with these individuals under a “true independent contractor” status but this would entail giving up certain “controls” over these individuals that the agency currently maintains to ensure they act in a manner the agency requires. The agency has not specified what problems this loss of “controls” would create. Furthermore, the agency has not now (nor in the past years) identified any programmatic problems caused by the current independent contractor status. Under these circumstances we find no basis to increase the costs of the program by \$385,000 to change the positions to exempt state employee status. Moreover, it is not clear why the agency has chosen to convert these positions to *exempt* employee status rather than regular state employee status. Consequently, we recommend that the Legislature reduce Item 2920-001-001 by \$385,000 and 19 positions.

Increase in Administrative Staff Not Needed

We recommend that the Legislature delete \$260,000 in General Fund expenditures and five positions for the agency’s administrative services because the agency justifies the need for the positions based on the proposed expansion of the International Trade and Investment Program which we recommend the Legislature should not approve. (Reduce Item 2920-001-001 by \$260,000.)

The budget proposes \$260,000 and five positions to increase administrative staff as a result of the expansion of the international trade and investment foreign office programs. Above, we recommend that the Legislature delete the General Fund expenditures for this proposed expansion. Accordingly, we recommend that the Legislature delete the \$260,000 General Fund augmentation and the five positions requested for administration associated with the expansion.

General Fund Expenditures for Loan Guarantee Program are Not Effective

We recommend that the Legislature delete \$3.5 million in General Fund expenditures for the Small Business Loan Guarantee Program because the use of this appropriation is not cost-effective. (Reduce Item 2920-001-001 by \$670,000 and delete Item 2920-011-001 (c)).

The budget proposes \$3.5 million in General Fund expenditures for the Small Business Loan Guarantee Program, which includes a \$1.5 million augmentation for 1995-96. These expenditures are used to pay for loan defaults, and support staff.

Historically, the program has had difficulty leveraging state funds available for loan guarantees much beyond a 1 to 1 leverage factor (that is, one dollar of a loan is guaranteed for every one dollar of state funds). This problem results from a combination of (1) the banks' (or conventional lenders') reluctance to lend to high-risk businesses applying for guarantees under the program, and (2) the program's inability to find enough businesses that need loan guarantees *and* which are considered likely to succeed so that banks are comfortable lending to them with a leverage ratio beyond 1 to 1.

The agency's use of General Fund appropriations for the program does not address this problem of the program's inability to maximize state funds for loan guarantees. Instead, it makes the problem worse by establishing some inappropriate incentives and exposing the General Fund to a large expense.

Program Background. The Small Business Loan Guarantee Program uses the Small Business Expansion Fund—a trust account—to finance operating costs and to provide loan guarantees to small businesses who cannot get conventional financing. The program (established in 1968) received an initial appropriation of \$30 million from the General Fund to establish the trust account. The agency allocates the funds in the trust account among eight Regional Development Corporations that administer the loan guarantee program. Historically, the corporations use interest earnings on their portion of the trust account to finance operating costs and cover loan default payments. Loan defaults and low interest earnings have brought the total trust account to its current balance of \$29.2 million.

Current law allows the corporations to guarantee 90 percent of a loan—up to a maximum guarantee of \$500,000. The average guarantee is currently 80 percent of the loan. The corporations are also authorized to leverage the trust fund to a maximum of 4 to 1. Currently, however, the fund is at a 1.6 to 1 ratio. It has not reached the maximum 4 to 1 ratio because lenders are reluctant to make these “higher-risk” loans unless

there are sufficient funds to guarantee them on, or close to, a 1 to 1 basis. Currently, the amount of this fund (\$29.2 million) provides loan guarantee authority of \$46.2 million.

General Fund Augmentation. The agency proposes to use the General Fund—instead of the trust accounts—to pay for loan defaults and administrative costs associated with these defaults so that the corporations can guarantee more loans. To do this, the Governor's Budget proposes \$1.2 million to pay for loan defaults, \$1.6 million to pay for loan analysts and business development officers for the regional corporations and \$670,000 to add agency employees to market the program and to take over (from the regional corporations) the responsibility of recovering losses on loan defaults. The agency's plan calls for annual General Fund increases until the total *annual* appropriation reaches \$7.6 million in 2000-2001.

Proposed General Fund Expenditures Worsen Program Incentives. Our main concern with the program is that the agency's proposal to use \$7.6 million from the General Fund *on an annual basis* to pay loan defaults and staff expenses creates the wrong type of incentives for the regional corporation. Specifically, the regional corporations currently have an incentive to make solid loans because defaults reduce the amount of funds they have to loan. Under the budget proposal, there is really no fiscal discipline imposed on the corporations because they would not have to bear the costs of poor loan decisions. The proposal instead, encourages increasingly marginal loans that are more likely to default.

It's also not clear why the budget proposes to shift administrative costs from the regional corporations to the General Fund. The program was set up to be self-supporting within the trust fund.

Agency Should Make Better Use of Existing Resources. The regional corporations were created to operate as nonprofit businesses and to be self-sustaining. Each corporation was allocated a portion of the trust fund for loan guarantees and was to use the interest earned on this fund source to pay for its operations. The program's viability is dependent on market factors such as interest rates and the willingness of conventional lenders to lend to "higher risk" small businesses. Rather than use annual General fund appropriations, the agency should (1) develop a strategy for making maximum use of the trust fund that is responsive to these market forces, and (2) then hold the regional corporations accountable for their operations.

Moreover, more options are emerging for small business to obtain credit. For example, in Los Angeles a for-profit organization is lending to "non-bankable" small businesses wanting to expand. Also, the Small Business Administration has a new program to issue lines of credit guar-

antees to small businesses. These organizations can supplement the state's program to increase loan activity to small businesses in California without new General Fund appropriations.

For these reasons, we recommend the Legislature delete the \$3.5 million General Fund appropriation for the Small Business Loan Guarantee Program.

Effectiveness of Defense Conversion Program Is Uncertain

We withhold recommendation on the transfer of \$8 million from the General Fund to the Competitive Technology Fund for the Defense Conversion Matching Grant Program pending receipt of the agency's report on the effectiveness of the program.

The budget proposes to transfer \$8 million from the General Fund to the Competitive Technology Fund. This is \$2 million higher than the transfer made in the 1994-95 Budget Act. The agency uses the Competitive Technology Fund, supported completely by the General Fund, for the Defense Conversion Matching Grant Program. Under the program, the agency approves grants to match private and federal dollars for defense industry conversion projects.

Effectiveness of Program Is Uncertain. Beginning in 1993-94, the agency has approved a total of \$12.1 million for 50 defense conversion projects. The average grant amount is approximately \$250,000. The agency claims that this amount can add value to the proposals it receives from California businesses and institutions requesting state matching funds for defense conversion projects.

Our review indicates that, in many cases, this grant amount is insignificant. For example, in several instances the state has committed \$250,000 for multi-million dollar projects that were likely to go ahead without the state match. Also, the state's 1993 Defense Conversion Act requires the agency to consider job creation as a factor for measuring the effectiveness of state funds used for California's defense conversion. The agency, however, claims that because job creation is not a specific goal or objective of the federal government, the agency does not assess projects involving federal funds or other projects according to the number of jobs created or retained as a result of the project.

Report to Legislature Is Overdue. Current law requires the Defense Conversion Council to submit to the Legislature a report on the effectiveness of the state matching grant program, on or before January 1, 1995 and again on January 1, 1997. At the time this *Analysis* was prepared, this report had not yet been submitted to the Legislature. Because the effectiveness of the Defense Conversion Matching Grant Program is uncertain,

and the report to the Legislature is not yet available, we withhold recommendation on the \$8 million General Fund transfer to the Competitive Technology Fund. When the report becomes available, we will review it and, as appropriate, make recommendations to the Legislature.

General Fund Support For Defense Adjustment Program Is Premature

We recommend that the Legislature delete \$1.1 million in General Fund expenditures for the Defense Adjustment Matching Grant Program because the agency has not justified the effective use of this appropriation. (Reduce Item 2920-101-001 by \$1.1 million.)

The budget proposes \$1.1 million in General Fund expenditures for the Defense Adjustment Matching Grant Program. This program provides grants to local agencies seeking federal funding for defense conversion planning and program implementation, as well as military base reuse planning.

Program Background. During 1993-94, the agency established the Defense Adjustment Matching Grant Program. The agency received permission from the U.S. Economic Development Administration (EDA) to fund the program with the remaining portion of the California Economic Development Grant and Loan Program Fund. The fund was established in the late 1970s with money from the EDA and was used primarily for business loans. The Trade and Commerce Agency has used all available funds—\$1.5 million—to approve twenty grants.

General Fund Appropriation Is Premature. Because federal monies are no longer available for the agency to use for this program, the agency is requesting a \$1.1 million General Fund appropriation to continue their efforts in this area. However, the agency has not yet evaluated the effectiveness of the twenty grants it has already approved. The agency claims that it is too soon to evaluate the job growth and revenue impact of the matching grant expenditures at this time since most of the grantees have just begun their planning activities. Because the agency can't be certain of the benefits resulting from these grants, we believe the General Fund request to award additional grants is premature. Therefore, we recommend that the Legislature delete the \$1.1 million proposed for the Defense Adjustment Matching Grant Program.

New Regulation Review Unit Would Duplicate Efforts

We recommend that the Legislature delete \$600,000 in General Fund expenditures and eight positions for a new regulation review unit because the establishment of this unit would duplicate current state efforts and the review of particular regulations, if needed, should be done within existing resources. (Reduce Item 2920-001-001 by \$600,000.)

The budget proposes \$600,000 and eight positions for the agency to establish a regulation review unit. The agency proposes to establish this unit in response to Ch 418/93 (SB 1082, Calderon), which gives the agency the discretion to review and evaluate the findings by any state agency proposing regulations.

Establishment of New Unit Is Not Justified. Chapter 418 does not require the agency to evaluate proposed regulations, yet the agency requests eight positions in order for the new unit to review *all* proposed regulations. The agency's review of these regulations would be in addition to the review given them concurrently by the public, the Office of Administrative Law and the government agencies responsible for developing and administering the proposed regulations. The new unit would duplicate existing efforts and simply add another layer of administrative review. If there are particular regulations that need the agency's input, there are sufficient means currently available within the administration to assure that any such regulations are directed to the agency. Any such review should be conducted within existing resources on a priority basis. An augmentation of \$600,000 from the General Fund and the addition of eight positions is not warranted. Thus, we recommend that the Legislature delete the \$600,000 under Item 2920-001-001 for establishment of the regulation review unit.

General Fund Augmentation for Business Advertising is Not Justified

We recommend that the Legislature delete a \$500,000 General Fund augmentation for business advertising because there are no measurable benefits to the state. (Reduce Item 2920-001-001 by \$500,000.)

The budget proposes a \$500,000 General Fund augmentation to increase California's visibility as the premier place to do business. The agency currently spends \$500,000 specifically for this purpose. Thus, the augmentation increases expenditures by 100 percent to \$1 million annually. The agency intends to increase visibility by circulating more information, such as brochures or news articles, around the country to promote California as a business location. The agency claims that this augmentation will ensure that the agency has enough publications and other

material (such as videos) to meet demand. Yet the agency hasn't defined what the demand is, how it will be met, or how the business climate will improve in California as a result of the appropriation. Because the agency has not shown that the state can reasonably expect commensurate benefits from these additional expenditures, we recommend that the Legislature disapprove the \$500,000 augmentation for business marketing.

ENERGY RESOURCES, CONSERVATION AND DEVELOPMENT COMMISSION (3360)

The Energy Resources Conservation and Development Commission—(commonly referred to as California Energy Commission) is responsible for siting major power plants, forecasting energy supply and demands, developing and implementing energy conservation measures and conducting energy-related research and development programs.

The budget proposes commission expenditures of \$35.6 million from various state and federal funds in 1995-96. This is \$44.1 million or 55 percent less than current-year expenditures. This reduction reflects half-year funding for the commission due to the Governor's proposal to abolish the commission and transfer its functions to a new Department of Energy and Conservation effective January 1, 1996. Major program changes within the commission's functions include (1) a \$5.7 million augmentation from the Petroleum Violation Escrow Account (PVEA) for various development, research and demonstration projects and (2) an increase of \$5.4 million for the Katz Safe School Bus Clean Fuel Efficiency Demonstration Program from the Katz Schoolbus Fund (supported by PVEA monies.)

Budget Proposes to Eliminate the Energy Commission

At the time this analysis was prepared, it was not possible to determine if the Governor's reorganization proposal for various resources departments has merit because the details of the plan had not been provided to the Legislature. If it appears that the Governor's Reorganization Plan will not be submitted to the Legislature in time for full consideration before the Budget Act is adopted, we recommend that the Legislature provide full-year funding for the Energy Commission in the Budget Bill. If legislation to eliminate or restructure the commission is subsequently enacted, that legislation could amend the Budget Act accordingly.

The budget proposes to eliminate the Energy Commission and transfer its functions to a new Department of Energy and Conservation (Item 3350). To implement this proposal, the budget proposes to fund the commission for the first half of 1995-96. For the second half of the year, all

commission functions are funded under the new department. The budget shows a \$763,000 savings and the reduction of 7.5 personnel-years from abolition of the commission. A detailed discussion of this proposed reorganization is provided in the Crosscutting Issues portion of the Resources Section in this *Analysis*.

When this *Analysis* was prepared, the administration was developing a reorganization plan to submit to the Legislature. However, a time-frame for submitting the plan to the Legislature had not been established. Consequently, we recommend that the Secretary for Resources report to the Legislature at budget hearings on the plan and its status. If it appears at that point that the plan will not be submitted to the Legislature in time for consideration before the Budget Act is adopted, then we recommend that the Legislature provide full-year funding for the commission. If legislation is subsequently enacted to consolidate or restructure the commission, the Budget Act could be amended accordingly at that time.

Issues for Legislative Consideration Regarding Reorganization. In order for the Legislature to determine if the Governor's plan meets the Legislature's goals, objectives, and priorities for the state's energy policy, the administration must identify how the commission's current duties would be improved under the reorganization. Therefore, we recommend that the Legislature, at a minimum, consider the following when reviewing the reorganization plan:

- What are the benefits, savings and costs realized to the state and to utility rate payers resulting from the reorganization?
- Has the plan addressed all energy-related state programs to ensure an efficient and comprehensive reorganization? For example, current overlapping responsibilities between the commission and Public Utilities Commission's (PUC) should be addressed in the plan.
- How will the reorganization improve the state's regulation of the rapidly changing energy industry. For example, in April 1994 the PUC proposed to deregulate the electric services industry. Will the reorganization lead to improved state coordination and implementation of proposals of this type?

AGRICULTURAL LABOR RELATIONS BOARD PUBLIC EMPLOYMENT RELATIONS BOARD (8300 AND 8320)

Agricultural Labor Relations Board. The Agricultural Labor Relations Board (ALRB) protects the rights of agricultural workers to join employee unions, bargain collectively with their employers, and engage in activities through labor organizations of their own choosing. In order to accomplish its work, the agency is split into two divisions: (1) the General Counsel, whose employees run elections and investigate charges of unfair labor practices, and (2) the board, which certifies elections, and adjudicates and mediates unfair labor practices.

The budget proposes General Fund expenditures of \$4.4 million for the support of the ALRB in 1995-96, the same expenditure amount as estimated for the current year.

Public Employment Relations Board. The Public Employment Relations Board (PERB) protects the rights of public education and state employees to join employee organizations and engage in collective bargaining with their employers regarding salaries, wages, and working conditions. It does so by administering three state laws: (1) the Education Employment Relations Act, covering K-14 school employees; (2) the Ralph C. Dills Act, covering state civil service employees; and (3) the Higher Education Employer-Employee Relations Act, covering University of California and California State University employees. Like the ALRB, the PERB reviews, mediates, and, if needed, adjudicates charges of unfair labor practices and conducts employee union elections.

The budget proposes expenditures of \$4 million for support of the PERB in 1995-96, the same expenditure amount estimated for the current year.

Eliminate the ALRB and Transfer Its Remaining Duties to the PERB

In view of ALRB's persistently light workload, we recommend legislation eliminating the board and transferring its duties to the PERB. This would result in budget-year savings to the General Fund of \$942,000 and future annual savings of at least \$1,884,000. (Reduce Item 8300-001-001 by \$2,196,000 and Increase Item 8320-001-001 by \$1,255,000.)

The ALRB was created in 1975 with the passage of the Agricultural Labor Relations Act (Ch 1/75, Third Extraordinary Session). The ALRB's workload consists of (1) certifying farm worker union elections, (2) adjudicating unfair labor practices, and (3) collecting restitution from farm employers found guilty of violating the state's collective bargaining laws. The ALRB was created because federal collective bargaining laws specifically denied coverage to agricultural workers.

Light Workload. Our review of the board's two major workloads—election certification and unfair labor practice complaints—shows a dramatic falloff after an early flurry of cases in the years immediately following passage of the Agricultural Labor Relations Act in 1975. For example, Figure 15 shows that ALRB election certifications peaked in the years immediately following creation of the ALRB (1975-1977), then declined sharply and permanently. The ALRB certified nine elections in 1993-94, an all-time low. Figure 16 illustrates the same phenomena in the issuance of complaints by the board (31 in 1993-94). Through November of the current year, the ALRB has held 12 elections, and issued nine unfair labor practice complaints.

Jurisdictional Conflicts. As noted above, federal law specifically excludes collective bargaining for agricultural workers. In November 1992, the National Labor Relations Board (NLRB) Regional Director in Oakland issued an opinion stating that when a worker in the field packs already-cut agricultural produce into a package, the worker is no longer an agricultural laborer, and comes under the jurisdiction of the NLRB. This is the case even though the "packer" may have just hours or minutes earlier been cutting the produce—an activity that would have put the worker under the jurisdiction of the ALRB. This decision, referred to as the "Produce Magic" decision, was appealed to the federal board, which upheld the decision. The ALRB board has asked the NLRB to reconsider the decision.

If upheld, this decision would decrease the number of workers covered by state law, reducing ALRB's already slight workload even further. The amount of the decrease, however, cannot be determined due to differing interpretations of how broad the case's impact will be.

Figure 15

**Agricultural Labor Relations Board
Elections Held
1975-76 Through 1993-94**

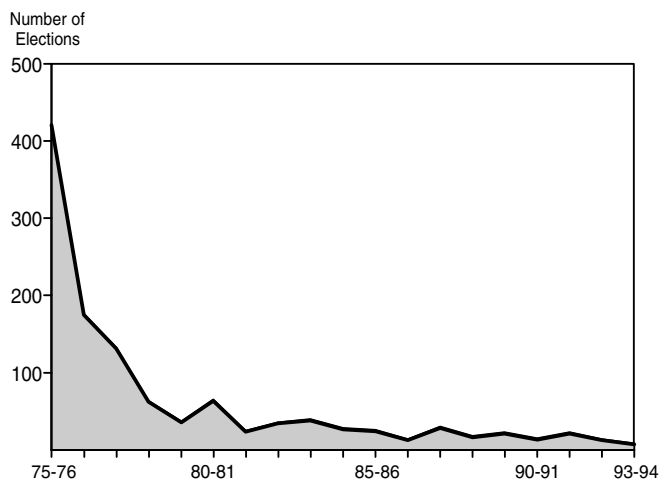
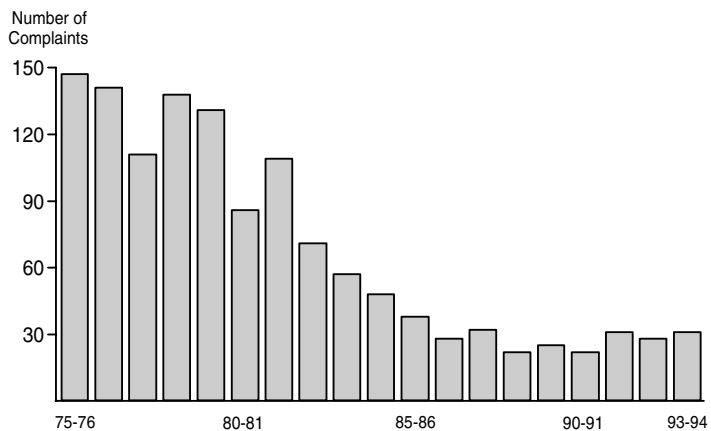


Figure 16

**Agricultural Labor Relations Board
Complaints Issued
1975-76 Through 1993-94**



For example, some say that the case's significance will be limited to one activity (packing) of one crop (lettuce), while others believe the ruling could apply to work crews in other crops. Regardless, the implications for ALRB are clear—less workload.

Given this light workload, we believe greater efficiencies would be achieved by eliminating the ALRB and transferring enforcement of the state's farm labor collective bargaining laws to the PERB. Specifically, our review indicates that the work of the ALRB board members and their legal and administrative support positions could be absorbed by the PERB. The ALRB currently spends almost \$1.9 million on these functions. Furthermore, additional savings should be available through the elimination of duplicative administrative positions (such as personnel and budgeting positions).

Recommendation. In view of the above, we recommend that the Legislature enact legislation to eliminate the ALRB—as of January 1, 1996—and move its residual functions and workload, with necessary staff, to the PERB. Accordingly, we recommend the Legislature reduce Item 8300-001-001 by \$2,196,000 (half-year funding) and increase Item 8320-001-001 by \$1,255,000. This recommended consolidation would save the General Fund at least \$942,000 in 1995-96, with annual savings of at least \$1,884,000 in future years, due to the elimination of the ALRB board and related staff. We also recommend that the legislation include those changes needed to conform the Agricultural Labor Relations Act with the transfer of enforcement to the PERB.

Deposit Undisbursed Unpaid Wages Into the General Fund

We recommend the Legislature enact legislation requiring that unpaid wages collected from an employer found guilty of unfair labor practices be deposited into the General Fund when the worker eligible to receive these wages cannot be located.

The ALRB is required (pursuant to Labor Code Section 1148) to follow the practices and procedures of the NLRB in carrying out its duties. Under NLRB policy, no penalty fine is assessed to an employer found guilty of committing an unfair labor practice. Instead, the employer must compensate the worker for unpaid wages plus interest. If the ALRB does not locate the workers within two years, however, the funds are returned to the employer. The amounts returned to employers varies greatly from year-to-year. In 1993-94, for example, \$4,493 was returned to employers, while in 1992-93 the amount was \$138,526.

Under this policy, some employers who break the law are not held accountable. In contrast to the ALRB laws, the Labor Code provisions

relating to the Department of Industrial Relations (DIR) require that unpaid wages either be returned to the appropriate workers or deposited into the General Fund. None of the unpaid wages collected by the DIR are returned to the employer. We believe the DIR approach is more appropriate, and therefore recommend that the Legislature enact legislation to require the deposit of any undisbursed revenue into the General Fund.

DEPARTMENT OF INDUSTRIAL RELATIONS (8350)

The mission of the Department of Industrial Relations (DIR) is to protect the workforce of California, improve working conditions, and advance opportunities for profitable employment. These responsibilities are carried out through three major programs: the adjudication of workers' compensation disputes; the prevention of industrial injuries and deaths; and the enforcement of laws relating to wages, hours, and working conditions.

In addition, the department (1) regulates self-insured workers' compensation plans, (2) provides workers' compensation payments to injured workers of uninsured employers and other special categories of employees, (3) offers conciliation services in labor disputes, (4) promotes apprenticeship programs, and (5) conducts and disseminates labor force research.

The budget requests an appropriation of \$181.4 million in 1995-96, a 1 percent decrease over estimated current-year expenditures. The request includes a \$136.9 million General Fund appropriation, a \$323,000 decrease over estimated current-year expenditures. Most of the decrease is attributable to the temporary suspension of state mandates.

TARGETED INSPECTION PARTNERSHIP PROGRAM

DIR Should Report on Program Alternatives

To date, the DIR's joint program with the U.S. Department of Labor for enforcing labor laws in the agricultural and garment industries has not been effective. We recommend that the DIR report to the Legislature (1) on the cost effectiveness of the program, and (2) on any changes in the law or administrative processes that would improve the program's effectiveness. If the program is not shown to be effective or modifications would not improve enforcement, the Legislature should eliminate the program.

The Governor's Budget proposes 15 positions and expenditures of \$913,000 from the Industrial Relations Unpaid Wage Fund to support the Targeted Industries Partnership Program (TIPP) in 1995-96, a 2 percent increase over estimated current-year expenditures.

Since November 1992, the DIR has teamed with the U.S. Department of Labor (DOL) to coordinate the enforcement of federal and state labor laws in the garment and agricultural industries. Widespread violations of workplace safety, and wage and hour laws (unpaid overtime, paying below the minimum wage, and no workers' compensation insurance coverage) in these two industries have made them the focus of special state and federal government enforcement efforts.

Under the TIPP, staff from the DIR's Division of Labor Standards Enforcement (DLSE) and Division of Occupational Safety and Health (DOSH), along with DOL investigators, make unannounced "sweeps" at farms and garment workshops that have been the subject of complaints. By coordinating resources and joining forces, the two DIR divisions and the DOL attempt to provide comprehensive enforcement of federal and state wage and hour, and occupational safety laws.

Small Percentage of Assessments Actually Collected. Since its inception, the TIPP administrators have been unsuccessful in collecting assessments for violations such as paying wages below the minimum wage, not paying for overtime, and operating without workers' compensation insurance. Assessments go uncollected because employers: (1) appeal the assessment, (2) go bankrupt, or (3) retreat into the underground economy or otherwise avoid detection. Figure 17 shows the TIPP inspections, assessments and collections in 1994. The figure shows that TIPP collections represented 8.5 percent of assessments in calendar year 1994. In 1993, TIPP collections represented 7.1 percent of assessments. The Franchise Tax Board, which has stronger revenue collecting tools and authorities, has been collecting the TIPP assessments, pursuant to an inter-agency agreement, since June 1, 1994. It is not apparent whether the FTB will be more successful than the DIR in collecting assessments.

Figure 17

**Department of Industrial Relations
TIPP Inspections, Assessments, and
Collections, 1994**

| | Agricultural | Garment | Total |
|-------------|--------------|-------------|-------------|
| Inspections | 589 | 500 | 1,089 |
| Assessments | \$998,300 | \$4,546,000 | \$5,544,300 |
| Collections | \$97,108 | \$372,224 | \$469,332 |

Coordinated Labor Law Enforcement. A typical TIPP sweep includes approximately six teams comprised of (1) a DOL wage and hour investigator to review minimum wage records, (2) a DOSH inspector to review workplace safety laws, and (3) a DLSE investigator to review overtime records and assure that employers have valid workers' compensation insurance. These teams make unannounced inspections at garment workshops and farms where the DIR has received complaints about the employer. The investigators conduct a thorough review of the workplace and the employer's payroll records, and share the appropriate information. The concept of a coordinated program such as the TIPP makes sense. In fact, such a program should also include, or be closely coordinated with, other departments and public entities (such as the Employment Development Department, and local law enforcement agencies).

Program Results Lacking. Despite the positive coordination aspects, the evidence appears to indicate that the TIPP is ineffective. This conclusion is based on two sets of indicators. First, labor law violators are assessed but most of the funds are never collected. Consequently, the assessments are virtually meaningless. Second, it appears that the TIPP offers little deterrence. The nature of the agricultural and garment industries is that they are both labor intensive and thrive on the presence of an abundant supply of labor willing to work for low wages. Employers recognize this and are presently taking advantage of the large supply of inexpensive labor. For example, departmental records indicate that many garment industry employers routinely violate labor laws and are cited by the TIPP. Based on conversations with department staff it is believed that many of these employers resurface in new locations under new names while continuing to operate in the same way—without workers' compensation insurance, paying below the minimum wage, and violating overtime wage provisions. In addition, the TIPP staff does not conduct thorough follow-up investigations to assure that problems identified in the sweeps are permanently corrected. In short, the current program does not appear to provide meaningful sanctions or deterrence to remedy violations of labor laws in the agricultural and garment industries.

Tougher Penalties. The TIPP could be more effective if penalties were made tougher. Examples of penalties that could provide a stronger deterrent to violating the law include:

- Confiscating goods, including agricultural products grown by farmers, of employers who violate the law.
 - Closing the businesses of employers who violate the law.
 - Make willful and egregious violations criminal offenses.
-

- Make garment manufacturers jointly liable for back wages owed by bankrupt contractors.

The TIPP Should Either Be Improved or Eliminated. As discussed above, the TIPP is not effectively addressing and remedying labor law violations in the garment and agricultural industries. Above, we have suggested some ways to help the department improve its enforcement of the laws. In addition, to help the Legislature assess the effectiveness of the current program and ways to improve it, we recommend that the DIR report to the Legislature during budget hearings on what specific benefits the existing TIPP program provides, and how working conditions have changed in comparison to the situation before the TIPP was created. The DIR should also advise the Legislature of changes in the law and/or administrative processes that would make the program more effective. Unless an improved TIPP can start achieving better results, the Legislature should eliminate the program and return enforcement of labor laws in these industries to a high priority within the regular DLSE and DOSH programs.

TIPP Funding Source Is Inappropriate

We recommend that if the Legislature continues the TIPP, it be funded from the General Fund. The current funding from unpaid wages is inappropriate because it creates a conflict between locating the workers who are owed unpaid wages and using the money to fund the program.

When an employer violates state wage and hour laws, and becomes obligated to pay workers unpaid wages, the funds are deposited in the Industrial Relations Unpaid Wage Fund (UWF). The DIR subsequently pays workers out of this fund. If a worker owed unpaid wages cannot be located, the funds are deposited in the General Fund. Any balance in the fund over \$200,000 is transferred to the General Fund. If the balance of \$200,000 or less in the UWF is insufficient to pay all the workers, the General Fund makes up the difference.

The Governor's Budget estimates unpaid wage collections of \$1.6 million in 1995-96. The DIR budgets \$500,000 to pay workers (\$194,000 of which is projected to be unallocatable and returned to the General Fund) and \$913,000 to fund the TIPP. The difference, about \$200,000, is the UWF reserve.

By funding the TIPP administrative costs out of unpaid wages (that is money paid to workers that can be located), the DIR could have an incentive to hold back its effort in locating workers owed backpay in order to assure that support funding is adequate. We have no evidence suggesting

that the DIR is not using the appropriate resources or effort to locate workers owed backpay. Nonetheless, this funding source creates an inherent conflict between locating the workers who are owed this money and using the money to finance the DIR program. This is an undesirable conflict that should not exist. Therefore, we recommend that if the Legislature continues the TIPP program, it fund the program from the General Fund.

HIGH HAZARD INSPECTION AND CONSULTATION PROGRAM

The budget includes \$9 million in 1995-96 for the second year of the Targeted Inspection and Consultation program. Under this program, the Division of Occupational Safety and Health (DOSH) is required to target the highest hazardous employers in the most hazardous industries for either workplace safety compliance inspections or consultation services, if the employer so chooses. In the 1993 workers' compensation reform legislation, Ch 1241/93 (SB 147, Johnston), the Legislature provided the DIR a \$4 million General Fund loan as start-up funds for the program. This loan is to be repaid by June 30, 1995.

Employer Assessments Fund Program

To pay for the inspection and consultation workplace safety program, the Legislature approved levying user fees on employers who have the highest rate of workers' compensation claim losses. The legislation, Ch 121/93 (AB 110, Peace), targets any employer with an "experience modification" (ex-mod) factor of 1.25 or above, or an equivalent rating for uninsured employers, to pay a fee to fund the workplace safety program. An ex-mod factor measures the occurrence of employer loss due to workers' compensation claims among similar groups of employers. A factor of 1.0 equals the statistical average within a specific industrial classification, factors below 1.0 identify companies safer than average, and factors above 1.0 identify companies more hazardous than average.

By using ex-mod factors, there is no penalty placed on employers in inherently dangerous lines of work. Construction firms, for example, are measured against construction firms to take into consideration the occupational safety characteristics of that industry. Ex-mods are used by insurance carriers to help calculate an employer's premium. For example, a company with an ex-mod of 1.0, the statistical average, pays the basic insurance premium established for that industry. A company with an ex-mod of 1.25, however, will pay a premium that is 25 percent higher than average, while a company with an ex-mod of 0.9 will pay a premium that is 90 percent of the average.

There are nearly 530,000 employers in the state that purchase workers' compensation insurance. Of this total, only 130,000 (25 percent) currently receive an ex-mod rating. This is because the Workers' Compensation Insurance Rating Bureau (WCIRB), the organization that calculates ex-mod ratings, only provides ratings to companies that paid a total annual premium over a predetermined amount in prior years. In 1994, for example, this premium threshold was \$16,968. Consequently, 75 percent of the employers (those paying less than \$16,968 annually for insurance premiums) at this time are not assessed a fee for this program. Of the 130,000 employers with ex-mod factors, 13,000 have ratings above the 1.25 threshold. These employers will be assessed the fee to pay for the workplace safety program. Regulations proposed by DOSH, and currently implemented on an emergency basis, require an affected employer's workers' compensation insurance carrier to collect the high hazard assessments, and distribute the money to DOSH.

In addition to the ex-mod rated companies, Ch 121/93 requires the DIR to create an equivalent rating for self-insured companies, and assess them an appropriate fee. There are about 1,200 private employers and 2,500 public employers, out of the 530,000 employers in the state, that self-insure their workers' compensation liability. The DIR regulations creating an equivalency rating for self-insured employers are based on the *severity* of workers' compensation loss, as opposed to the ex-mod rating, which measures *frequency* of loss. Under the DIR regulations for self-insured employers, employers who have had only one or two workers' compensation claims filed against them may be assessed fees because the *dollar* amount of the claims exceeded a historical average claim loss. Employers assessed a fee based on the ex-mod rating system, however, are included because they have had more than the average *number* of claims.

The legislation requires DOSH to target the highest hazard employers in high hazard industries and provides indices the DOSH may use, including ex-mod factors, in identifying which employers to target. The law is silent, however, on the procedures for identifying targeted industries. In addition, the law provides the DOSH with the discretion to notify these employers by mail that they are a high hazard employer and that the company could be subject to compliance inspections. These employers can avoid an inspection if they submit a workplace safety plan and seek consultation services from the DOSH.

Issues For the Legislature to Consider. Our analysis of the DOSH's implementation of this program indicates that there are two general issues for the Legislature to consider. First, we have several concerns regarding the way employers are assessed fees for the program. Second, we have concerns about the way the department proposes to spend the fees on compliance efforts. These issues and our recommendations are

discussed below.

Assessment Issues Need to Be Addressed

Delays in the collection of employer assessments have stalled implementation of the DOSH's targeted workplace safety program, and made it impossible for the DOSH to repay a \$4 million General Fund loan in 1994-95. We recommend that the DOSH report to the Legislature during budget hearings on the appropriateness of basing program assessments on ex-mod ratings, the status of its assessment regulations, the effect the delay in collections has had on the program, and when the General Fund loan will be repaid.

As discussed above, state law requires that the DOSH assess all employers with an ex-mod of 1.25 and above, or the equivalent for self-insured employers. The DOSH proposes to collect the assessments from insured employers by requiring workers' compensation insurance carriers to collect the funds when the affected employers make their premium payments. (The DIR bills self-insured employers.) Some insurance companies oppose this collection method, and have taken legal actions to stop the DOSH from adopting the regulations. While the legal issues remain unsettled, the DOSH has implemented emergency regulations allowing for the collection of the assessments. The effect of this controversy, however, is that the DOSH has been unable to collect much of the assessment against the ex-mod rated companies.

The budget shows estimated collections of \$11.3 million in the current year. From this amount the DIR would use \$4 million to repay the General Fund loan and \$7.2 million for this program. Because of the delays, however, the budget amounts are significantly overstated. Specifically the DOSH expects to assess and collect only \$2 million in 1994-95. As of January 1995, for example, the DOSH had only been able to collect \$275,172 from insured employers whose insurance carriers were not party to the lawsuit. In addition, the DOSH had collected \$768,444 from self-insured employers, for a total 1994-95 collection of \$1,043,618 (9 percent of estimated collections).

Because the DOSH has been unable to collect most of the assessment, staffing delays have occurred and program implementation has been significantly affected. The DOSH has only hired 62 of the 123 positions authorized in the 1994 Budget Act. Furthermore, the DOSH has not yet inspected any high hazard employers in high hazard industries, as called for under the program. In addition, the DOSH's inability to collect assessments makes it impossible for the DOSH to repay the \$4 million loan by June 30, 1995.

Method for Assessing Employers is Problematic. Funding this pro-

gram through assessments on employers with ex-mods of 1.25, and self-insured employers with an equivalent rating, creates a number of issues.

- Most privately insured employers (75 percent) are not even rated, regardless of their safety record, because their payrolls are not large enough. These employers are not assessed. The DOSH, however, still plans to target some of these employers for special compliance efforts.
- Ex-mod ratings are assigned based on an employer's safety record standing relative to the other employers in the same industry, regardless of how hazardous that industry may be. For example, some employers in the retail industry have ex-mods at 1.25 or above because they have had workers' compensation claims that exceed the statistical average of that industry. These employers will be assessed despite the fact that retailing is not a high hazard industry. The DOSH, however, will not target inspections under the program to such employers.
- The DOSH regulations propose that the assessments on employers with ex-mods of 1.25 or above be based on the size of the employer's payroll, not the degree of risk that the employer poses. For example, two employers with the same payroll will pay the same assessment even if one has an ex-mod rating of 1.25 and the other has an ex-mod rating of 1.50.
- The self-insured employer rating methodology proposed by the DIR's Self-Insurance Plans office and adopted by the department is not "equivalent" to ex-mod ratings, as required under law, because it measures severity of accidents, not the frequency of accidents measured by ex-mods.

Given the assessment collection delay, and problems with the method used for identifying employers to assess, we recommend that the DOSH report to the Legislature during budget hearings on the appropriateness of basing program assessments on ex-mod ratings, the status of its collection efforts, the effect the delays have had on the program, and when the General Fund loan will be repaid.

Program Issues Need Clarification

We recommend that the DOSH report to the Legislature during budget hearings to ensure that program implementation is consistent with legislative intent, and address issues concerning (1) the overlap, if any, between assessed employers and targeted employers, (2) the means for identifying high hazard industries and employers, and (3) the process for assigning work to compliance staff and to consultation staff.

In implementing the targeted inspection and consultation program, the DOSH is planning to focus on high hazard employers and industries regardless of whether they are included in the program assessments. The DOSH is planning to target employers and industries based on several workplace safety determinations (such as Cal-OSHA Advisory Board recommendations and the Occupational Injuries and Illness Survey) rather than whether the employer has an ex-mod rating of over 1.25. As discussed earlier, about 13,000 of the 530,000 employers in the state have ex-mod factors of 1.25 or higher. About 400,000 do not have an ex-mod factor. Consequently, because the DOSH will *not* use the ex-mod rating as the determining factor for targeting a high-hazard employer the population of assessed employers and the population of targeted employers will not bear much, if any, resemblance to each other. The law does not require that the DOSH limit its targeting to assessed employers, and the DOSH plan of including all employers as potential targets may make sense. The Legislature, however, may not be aware that the two groups share so little overlap.

Most Assessed Employers Not Covered. As discussed earlier, those employers with the highest ex-mod ratings and self-insured equivalency rating may receive a letter from the DOSH informing them that consultation services are available to them. (A similar letter will not be sent to all the other employers.) If these employers fail to respond to the DOSH—by not submitting a workplace safety plan for review, and consultation—the employer is placed on a mandatory compliance inspection list. The DIR assumes that most employers who receive a letter will respond to the letter and seek consultation rather than be subject to the fines and penalties that can result from a compliance inspection. The DOSH indicates that its compliance inspection staff will be able to absorb the workload from the small number of employers who are likely not to respond and will be placed on the primary inspection list.

The DOSH is sending out letters to the highest rated employers in batches of 50 letters every 45 days. The size of the mailing and time lag between mailings allows the DOSH consultant staff to manage its workload. It also means, however, that a very small percentage of the 13,000 employers assessed fees under the program will receive anything in

return. (At the rate of 50 letters every 45 days it will take 32 years just to send a letter to 13,000 employers. Moreover, the mix of employers assessed a fee will change annually.)

In light of the disparity between the population of assessed and targeted employers, and the uncertainty of the proper procedures for targeting high hazard employers and industries, we recommend that the DOSH report to the Legislature to ensure that its proposed program implementation is consistent with legislative intent. Specifically, the DOSH should address (1) the overlap between assessed employers and targeted employers, (2) the means for identifying high hazard industries and employers, and (3) the process for assigning work to compliance and consultation staff.

1993 WORKERS' COMPENSATION REFORM IMPLEMENTATION CONTINUES

Comprehensive workers' compensation reform, enacted in 1993, began to take effect in 1994-95. The Legislature approved the reforms to reduce employer workers' compensation costs while increasing the basic benefits paid to injured workers. To implement the reforms, the Legislature approved 350 positions and augmentations of \$26 million. Recognizing that the DIR could not hire all the additional approved positions at the beginning of the 1994-95 fiscal year, the 1994 Budget Act provided an across the board 30 percent salary savings requirement on unfilled positions, creating current year savings of \$1.3 million (\$1 million General Fund).

Managed Care Workload Does Not Meet Projections

We recommend that the Legislature reduce the managed care program budget by \$750,000 and delete 12 positions because of existing workload, and the unlikely prospect of significant workload growth in the future. (Reduce Item 8350-001-132 by \$750,000.)

One element of the reform is to bring the cost containment techniques of the primary health care industry to the workers' compensation system. Managed care, as envisioned by the reform, could potentially provide injured workers with quality industrial injury medical care, and the convenience of access to the same doctors that provide primary health care. Moreover, it was anticipated that managed care could potentially result in large savings in employers' workers' compensation costs.

The reform legislation required the DIR to certify managed care pro-

viders as "health care organizations" (HCOs). In order to be certified as an HCO, the health care provider must first be certified by either the Department of Corporations (DOC) or the Department of Insurance (DOI). Thus, a Knox-Keene primary care health maintenance organization or a workers' compensation health care provider organization must be certified by DOC, and a disability insurer must be certified by DOI, before being eligible for certification as an HCO by the DIR.

The managed care program is funded out of fees paid by health care providers seeking certification as an HCO. The DIR is scheduled to collect a \$25,000 fee from HCO applicants in 1995-96. The program is currently funded from a General Fund loan of \$1.7 million and the budget proposes loaning the program another \$850,000 in 1995-96. Budget language requires both loans to be repaid by June 30, 1997.

In 1994-95, the DIR requested 27 positions in order to certify an estimated 50 HCO applications in 1994-95. The 1994 Budget Act authorized 22 of the positions, of which 10 are currently filled. The budget proposes to continue these positions in 1995-96.

Through January 1995 the DIR had only received nine HCO applications and certified three as HCOs. Another 20 potential applicants are awaiting certification by the DOC. Given this workload, it appears that the existing 10 positions will be able to handle the current workload under the program. Therefore, we recommend the Legislature maintain the managed care program's staff at the current level, for a reduction of \$750,000 and 12 positions.

Delete 91 Positions from Claims Adjudication Unit

We recommend that the Legislature reduce the Claims Adjudication Unit budget by \$4.25 million and delete 91 positions because projected workload has not occurred. (Reduce Item 8350-001-001 by \$3.4 million and 8350-001-223 by \$850,000.)

The 1994 Budget Act added 121 positions to the DIR's Claims Adjudication Unit based on workload estimates the DIR presented to the Legislature. More workers' compensation cases were projected to be disputed and require adjudication before workers' compensation referees because the reform legislation provided increased reliance on treating physician disability reports. As of December 1994, however, only 30 of the 121 new positions had been filled. The DIR indicates that future hires will depend on revised workload estimates.

The Claims Adjudication Unit's workload to date is much lower than the DIR expected when it requested funds from the Legislature in 1994. At that time, the DIR did not have specific workload data that would

result from the reform legislation. Instead, the DIR based the new workload on the expectation that more disputed cases would be sent to the adjudication unit. This has not occurred at the rate projected by the DIR. Furthermore, the DIR has not identified any pending increase in claims adjudication workload. Consequently, the actual new workload only supports the 30 positions that have been filled. Therefore, we recommend that the Legislature reduce the Claims Adjudication Unit budget by \$4.25 million and delete 91 positions.

Delete Positions Currently Funding Operating Expenses

We recommend that the Legislature reduce the Division of Workers' Compensation budget by \$4.5 million and delete 93 positions to reflect amounts being redirected to fund operating expenses and equipment purchases. (Reduce Item 8350-001-001 by \$3.6 million and Item 8350-001-223 by \$900,000.)

The DWC budget includes \$4.5 million and 93 positions (in addition to the 91 positions for the Claims Adjudication Unit discussed above) that the DWC is keeping vacant. These positions are spread throughout the division. These funds are being redirected to DWC operating expenses and equipment purchases. The 93 positions the DWC is keeping vacant were authorized by the Legislature to meet program needs. By purposely keeping the positions vacant, however, it appears that the program need originally cited to justify the positions does not exist. If additional operating expense and equipment purchase funds are needed, the DWC should submit an appropriate request with justification for review by the administration and the Legislature. Therefore, we recommend that the Legislature delete these 93 positions and the related \$4.5 million.

DEPARTMENT OF FOOD AND AGRICULTURE (8570)

The Department of Food and Agriculture (DFA) promotes and protects the state's agriculture industry, develops California's agricultural policies, and assures accurate weights and measures in commerce. The department also supervises the county agricultural commissioners and county sealers of weights and measures.

The budget requests \$200.8 million for the DFA in the budget year, an increase of \$4.7 million (2.4 percent) over estimated current-year expenditures. The budget total includes General Fund expenditures of \$70.2 million, a 2.3 percent increase over estimated General Fund expenditures.

Reduce General Fund Support of Lease-Payment Revenue Bond Repayment

We recommend that the Legislature reduce the General Fund portion of debt repayment on a new laboratory facility by \$452,000 and increase the Agriculture Fund portion by a corresponding amount to parallel the funding of the program activities housed in the facility. (Reduce Item 8570-003-001 by \$452,000 and increase Item 8570-003-111 by \$452,000.)

In the 1992 Budget Act the Legislature authorized the use of lease-payment bonds for the DFA to construct a facility in Sacramento. The project was completed in 1994 and debt service payments on the bond debt begins in 1995-96 and will run through 2013. The total budget-year bond debt payment is \$1.9 million.

The new facility was constructed to undertake activities on behalf of the Agricultural Plant Pest and Disease Prevention program and the Chemistry Laboratory. The Agricultural Plant Pest and Disease Prevention program is funded by the General Fund (70 percent), the Agriculture Fund (26 percent), and other special funds, federal funds and reimbursements (4 percent). Chemistry Laboratory funding is provided by a distributed charge to the various programs within the DFA. The debt payment is shared by the program and the laboratory based on activities undertaken at the facility.

The budget proposes that \$1.6 million of the Agricultural Plant Pest

and Disease Prevention program's \$1.64 million share of the debt service payment be provided from the General Fund, and the remainder from the Agriculture Fund. The proposed General Fund augmentation represents 98 percent of the Agricultural Plant Pest and Disease Prevention program's debt service obligation. As noted above, however, the General Fund only supports 70 percent of the Agriculture Plant Pest and Disease Prevention program. In light of this disparity, we recommend that the Legislature reduce the General Fund portion of the debt service by \$452,000 (to \$1,148,000) and augment the Agriculture Fund appropriation by \$452,000. Adopting this recommendation would make the debt service payment proportional to program expenditures, and create budget-year General Fund savings of \$452,000. The savings to the General Fund over the nearly 20 years of the debt repayment would be approximately \$9 million.

PUBLIC UTILITIES COMMISSION (8660)

The Public Utilities Commission (PUC) is responsible for regulation of privately owned "public utilities," such as gas, electric, telephone, trucking, bus, and railroad corporations. The commission's primary objective is to ensure adequate facilities and services for the public at equitable and reasonable rates, consistent with a fair return to the utility on its investment. Through its various regulatory decisions, the commission also promotes energy and resource conservation.

The budget proposes total expenditures for the PUC of \$85.7 million from various state special funds (\$79.9 million), federal funds (\$0.5 million), and reimbursements (\$5.3 million) in 1995-96. This is about \$0.2 million, or 0.3 percent, more than estimated current-year expenditures.

Federal Preemption of Trucking Regulation

We recommend that the Legislature delete \$12.7 million from the Transportation Rate Fund and 67 positions because the federal government has preempted the PUC's responsibility for economic regulation of intrastate trucking. (Reduce Item 8660-001-412 by \$12.7 million.)

Under the provisions of H.R. 2739 (effective January 1, 1995), the federal government has preempted the state's rate regulation of most intrastate trucking operations. This preemption effects the PUC in two ways. First, the PUC workload is significantly reduced. Second, the Transportation Rate Fund revenues and expenditures will be \$12.7 million less in 1995-96. Therefore, the PUC budget should be adjusted to reflect the reduction in workload and expenditures resulting from the federal preemption.

H.R. 2739 generally preempts states from enacting or enforcing laws or regulations related to prices, routes, or service of the intrastate trucking industry, with the exception of household good carriers. In short, this law strictly limits the PUC's responsibility for regulating the trucking industry. The PUC's main function in this area of regulation has been to monitor the industry to assure fair pricing and services throughout the state. For example, the PUC has required certain motor carriers to file their rates quarterly in order to closely monitor their pricing. These regulation activities are eliminated by the federal preemption. A total of 67 positions and \$12.7 million, however, are included in the budget for these activities.

Given the federal preemption, we recommend that the Legislature reduce Item 8660-001-412 by \$12.7 million and eliminate 67 positions in the Transportation Division.

Task Force on Trucking Regulation

A task force established by the Governor in January 1995 is to submit a report by March 5, 1995 on interim and permanent strategies for regulating intrastate trucking.

There are 214 positions in the PUC's Transportation Division that are not affected by the federal preemption. These positions are for safety regulation of the transportation industry as well as for the economic regulation of household carriers.

To assess how to best handle the remaining state regulatory responsibilities for the trucking industry, the Governor issued Executive Order W-115-95 on January 5, 1995. The executive order charges the Secretary of the Business, Transportation and Housing Agency to convene and chair a task force consisting of representatives from six state agencies (including the PUC), the trucking industry, and the Senate and Assembly Transportation Committees. The task force is to report to the Governor no later than March 5, 1995 on interim and permanent strategies to improve and streamline the remaining state responsibilities for regulation of the trucking industry. The order requires the report to include (1) the effective uses of state resources for this regulation and (2) processes that would ensure appropriate levels of trucking safety regulation. In addition, the order directs the California Highway Patrol to adopt a leadership role in the state's regulation of the trucking industry.

The task force report should be available to the Legislature during the budget hearing process. When the report is available, we will review it and, as appropriate, make recommendations to the Legislature regarding any budget implications.

LIST OF FINDINGS AND RECOMMENDATIONS

Analysis
Page

Department of Insurance

1. **Reorganization of Conservation and Liquidation Division.** Recommend the department report on restructuring prior to budget hearings. G-13
2. **Budget for Conservation and Liquidation Office Not Submitted for Legislature's Review.** Recommend the Legislature (1) add an informational item to the Budget Bill to show budgeted costs for the office and (2) adopt Supplemental Report Language requiring the department to provide detailed budget information annually on each conserved estate. G-15
3. **Workload Measures and Standards Are Incomplete.** Withhold recommendation of \$6.8 million and 74 permanent positions pending receipt of the department's report on workload measures and standards. G-16
4. **Legislature Needs Details on Unallocated Reduction.** Recommend the department report prior to budget hearings on the unallocated reduction and its effect on the department's programs. G-16

Department of Consumer Affairs

5. **Performance Measurements Fall Short and the DCA Needs to Demonstrate How Budget Flexibilities Aid Performance.** We recommend that before the Legislature enters into a performance budgeting contract with the DCA in 1995-96, the department incorporate specified performance measurements into the pilot project, and be able to explain how operational flexibilities aid performance. G-18
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- | | Analysis
Page |
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| 6. Augmentations Proposed for Performance-Based Budgeting Should Be Absorbed. We recommend that the Legislature direct the DCA to utilize the flexibility granted under performance based budgeting and absorb budget augmentations proposed for the participating boards and programs. (Delete Item 1111-001-702 by \$340,000.) | G-22 |
| 7. Schedule for Reviewing Need of Regulatory Boards Is Useful and Appropriate. Recent legislation establishing a procedure and timetable during which the authorizing legislation of the 32 consumer boards sunsets provides the Legislature with an appropriate and useful schedule for considering whether specific professions should be regulated. | G-23 |
| 8. Delete Funding of Cemetery Board and Board of Funeral Directors and Embalmers. In light of prior legislative action regarding these boards, we recommend that the Legislature delete funding proposed for the boards in the Governor's Budget. If legislation to restructure the boards is enacted, the necessary funding should be part of that legislation. (Delete \$419,000 under item 1180-001-717, and delete \$922,000 under Item 1330-001-750.) | G-25 |

Department of Fair Employment and Housing

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| 9. Positions should be limited-term. We recommend that the 19 positions requested in the budget be made limited-term positions until the HUD funding agreement becomes permanent. | G-27 |
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Department of Corporations

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| 10. Report to Legislature on Blue Cross's Restructuring Plan. Recommend that department report, during budget hearings, detailed information on Blue Cross's restructuring plan. | G-29 |
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Housing and Community Development

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| 11. Monitoring Program Costs Too Much. Recommend that the Legislature delete \$800,000 and ten positions from the bond-funded housing program administrative staff. Fur- | G-33 |
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**Analysis
Page**

ther recommend the Legislature direct the HCD to redesign its loan monitoring program to reduce costs and preserve the programs' remaining administrative reserves for the longest period possible. (Reduce Item 2240-001-714 by \$400,000 and Item 2240-001-788 by \$400,000.)

- 12. **Need to Reevaluate Monitoring Proposal for State-Funded Loans.** Recommend deletion of \$1.2 million and 15 positions requested to monitor the HCD's state-funded loan portfolio because the HCD (1) should ensure that its monitoring program reflects the state's limited policy interest in many of the loans and (2) should explore less costly options for monitoring loans in which the state has broad policy interests. (Reduce Item 2240-001-001 by \$1.2 million and make corresponding reductions to subsidiary special funds.) G-37

- 13. **Farm Worker Housing Program Budget Problems: Progress, but More Work Needed.** We recommend the Legislature approve the budget proposal to increase rent and General Fund revenues for the Office of Migrant Services by a total of \$1 million. We recommend the department submit a report to the Legislature outlining its proposal for addressing the imbalance between revenues and responsibilities for the Employee Housing Program. G-42

- 14. **How Much Should it Cost to Provide Housing Assistance?** Many proposals are being debated for reducing federal Housing and Urban Development programs and sending increased housing resources to states and localities. We evaluate the costs of California's last major housing effort—the bond-funded programs—and discuss options for providing assistance at lower costs. G-43

Trade and Commerce Agency

- 15. **Agency's Request to Expand Foreign Offices is Not Justified.** Recommend that the Legislature delete \$2.4 million because the agency has not justified the need for additional staff and five new field offices. G-46

| | Analysis Page |
|---|--------------------------|
| 16. Funding for Offices Should be Clearly Displayed in Budget. Recommend that Legislature add an item to the Budget Bill to clearly identify the amount of funds budgeted for each foreign office. | G-48 |
| 17. Proposal to Expand Domestic Foreign Program is Not Justified. Recommend that the Legislature delete \$342,000 for the expansion of the Office of Foreign Investment program because the agency has not demonstrated the value the additional staff will add to the program. | G-48 |
| 18. General Fund Increase for International Tourism Program Is Not Justified. Recommend that the Legislature delete \$1.8 million for expansion of the international tourism program because agency has not demonstrated that this proposal would be an effective use of \$1.8 million. | G-49 |
| 19. General Fund Augmentation to Address Currency Fluctuation Is Not Justified. Recommend that the Legislature delete \$199,000 for the adjustment of the foreign office budgets because this adjustment is not justified. | G-51 |
| 20. Agency Request to Convert Overseas Office Contracts Is Not Needed. Recommend that the Legislature delete \$385,000 to establish 19 exempt state positions in place of consultant contracts at foreign offices because the agency can continue the contracts for less cost. | G-51 |
| 21. Increase in Administrative Staff Not Needed. Recommend that the Legislature delete \$260,000 because the administrative positions are for the proposed expansion of the International Trade and Expansion Program which we recommend the Legislature delete. | G-52 |
| 22. General Fund Expenditures for Loan Guarantee Program are Not Effective. Recommend that the Legislature delete \$3.5 million for the Small Business Loan Guarantee Program because the use of this appropriation is essentially used for loan defaults and independent corporation staff. | G-53 |
| 23. Effectiveness of Defense Conversion Program is Uncer- | G-55 |

| | Analysis Page |
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| <p>tain. We withhold recommendation on the \$8 million for the Defense Conversion Matching Grant Program because the effectiveness of the program is uncertain and the agency's report to the Legislature on the effectiveness of the program was not available.</p> | |
| <p>24. General Fund Support for Defense Adjustment Program is Premature. Recommend that the Legislature delete \$1.1 million for the Defense Adjustment Matching Grant Program because the agency has not justified effective use of this appropriation.</p> | G-56 |
| <p>25. New Regulation Review Unit Would Duplicate Efforts. Recommend that the Legislature delete \$600,000 for a new regulation review unit because the establishment of this unit would duplicate existing state efforts and the review of particular regulations, if any, should be done within existing resources.</p> | G-57 |
| <p>26. General Fund Augmentation for Business Advertising is Not Justified. Recommend that the Legislature delete \$500,000 for business advertising because there are no measurable benefits to the state as a result of this augmentation.</p> | G-57 |

Energy Resources, Conservation and Development Commission

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| <p>27. Proposed Abolition of the Energy Commission. At the time this <i>Analysis</i> was prepared, it was not possible to determine if the Governor's reorganization proposal for various resources departments has merit because the details of the plan had not been provided to the Legislature. If it appears that the Governor's Reorganization Plan will not be submitted to the Legislature in time for full consideration before the Budget Act is adopted, we recommend that the Legislature provide full-year funding for the Energy Commission in the Budget Bill. If legislation to eliminate or restructure the commission is subsequently enacted, that legislation should amend the Budget Act accordingly.</p> | G-59 |
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Agricultural Labor Relations Board

28. **Eliminate the ALRB and Transfer Enforcement of Farm Labor Issues to the PERB. Reduce Item 8300-001-001 by \$2,196,000 and Increase Item 8320-001-001 by \$1,255,000.** G-62
Due to a persistent decline in the ALRB workload, we recommend legislation eliminating the board and transferring its duties to the PERB.
29. **Deposit Undisbursed Unpaid Wages in General Fund.** G-64
We recommend that the Legislature enact legislation to require the deposit of any undisbursed unpaid wage revenue into the General Fund.

Department of Industrial Relations

30. **Weak Labor Law Enforcement in Garment and Agricultural Industries.** G-66
Recommend that the DIR report to the Legislature on the effectiveness of its program to target labor law violations in the agricultural and garment industries, and if the program is not shown to be effective or that modifications cannot improve enforcement, that the Legislature should eliminate the program.
31. **Inappropriate TIPP Funding Source.** G-69
Recommend that if the Legislature continues this program that it be funded from the General Fund because of the conflict between returning unpaid wages to workers, and using the money to fund the program.
32. **Legal Challenges Delay Assessments on Employers and Workplace Safety Program.** G-72
Recommend that the DOSH report to the Legislature during budget hearings on the appropriateness of basing program assessments on ex-mod ratings, the status of its collection efforts, the effect the delays have had on the program, and when the \$4 million General Fund loan provided in 1993 will be repaid.
33. **Workplace Safety Program Issues Need Clarification.** G-74
Recommend that the DOSH report to the Legislature to
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| | Analysis Page |
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| ensure that its proposed program implementation is consistent with legislative intent given the disparity between the population of assessed and targeted employers, and the uncertainty of the proper procedures for targeting high hazard employers and industries. | |
| 34. Managed Care Workload Does Not Meet Projections. Recommend that the Legislature reduce the DWC's managed care program's budget by \$750,000 and delete 12 positions given existing workload, and the uncertainty of future workload levels. (Reduce Item 8350-001-132 by \$750,000.) | G-75 |
| 35. Claims Adjudication Positions Not Needed. Recommend that the Legislature reduce the DWC's Claims Adjudication Unit by \$4.25 million and delete 91 positions because projected workload has not occurred. (Reduce Item 8350-001-001 by \$3.4 million and Item 8350-001-223 by \$850,000.) | G-76 |
| 36. Delete DWC Positions Left Vacant. Recommend that the Legislature reduce the DWC budget by \$4.5 million and delete 93 positions to reflect positions the DWC is keeping vacant to fund operating expense and equipment purchases. (Reduce Item 8350-001-001 by \$3.6 million and Item 8350-001-223 by \$900,000.) | G-77 |

Department of Food and Agriculture

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| 37. Reduce General Fund Support of Debt Service. We recommend that the Legislature reduce the General Fund support of laboratory facility bond debt payments and increase the amount from the Agriculture Fund to parallel the proportional funding of the programs housed in the facility. (Reduce Item 8570-003-001 by \$452,000 and increase Item 8570-003-111 by \$452,000.) | G-78 |
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Public Utilities

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| 38. Federal Preemption of Trucking Regulations. We recommend that the Legislature delete \$12.7 million from the Transportation Rate Fund and 67 positions because the federal government has preempted the PUC's responsibility | G-80 |
|---|------|

**Analysis
Page**

for economic regulation of intrastate trucking. (Reduce Item 8660-001-412 by \$12.7 million.)

39. **Task Force Report.** A task force established by the Governor in January 1995 is to submit a report by March 5, 1995 on interim and permanent strategies for regulating intrastate trucking. G-81