



# An Initial Assessment of The California Performance Review

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On August 3, 2004, the California Performance Review (CPR) released its report on reforming California's state government, with the aim of making it more efficient and more responsive to its citizens. This report provides our initial comments on the CPR report. Specifically, we: (1) provide an overview of its reorganization framework and other individual recommendations, (2) discuss the savings it assumes from its major proposals, and (3) raise key issues and considerations relating to CPR's various proposals. ■

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### Acknowledgments

This report was prepared by Brad Williams and Michael Cohen with the assistance of staff throughout the Legislative Analyst’s Office (LAO). The LAO is a nonpartisan office which provides fiscal and policy information and advice to the Legislature.

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## INTRODUCTION

On August 3, 2004, the California Performance Review (CPR) released its report to the Governor on reforming California government. The report lays out a framework for reorganizing and consolidating state entities, and contains 278 issue areas and 1,200 individual recommendations aimed at making state government more modern, efficient, accountable, and responsive to its citizens. The CPR also adopted the 239 proposals included in a report recently issued by the Corrections Independent Review Panel. The CPR asserts that the state would achieve about \$32 billion in savings over the next five years if all of its recommendations were fully adopted.

The CPR has four volumes. The first sets forth its major goals, the second lays out a reorganization plan for state government, the third provides a budget and financial review of California state government, and the fourth contains CPR's individual proposals.

**LAO's Bottom Line.** The CPR provides the state with a valuable opportunity to comprehensively examine how it does business. It has made a serious effort at rethinking the current organization of state government and how it delivers services to the people of California. We find that many of its individual recommendations would move California toward a more efficient, effective, and accountable government.

At the same time, the rationale for some of its reorganization proposals is not clear, it does not examine whether the state should continue

to perform certain functions, and many of its fiscal savings estimates are overstated.

For these reasons, it will be important for the Legislature to evaluate the merits of the proposals individually, looking at their policy trade-offs, their likely effectiveness, and their fiscal implications. The Legislature also may wish to consider broadening the scope of reforms offered by CPR to include a more comprehensive examination of the state and local tax system, the role of constitutional officers, the state's system of funding education, and the relationship between state and local government.

**Organization of This Report.** This report, which provides our initial reaction to the CPR report, has three sections:

- "Section 1" provides an overview of CPR's reorganization plan and its other proposals, reviews CPR's estimated savings from its proposals, and discusses key issues for the Legislature to consider in reviewing the plan.
- "Section 2" looks at the *reorganization framework* in more detail and discusses key principles that should guide a reorganization.
- "Section 3" reviews CPR's *key proposals* in each of the major areas of the budget, providing some context for the proposals and our initial reaction to them.

## SECTION 1: OVERVIEW

### CPR's MAJOR COMPONENTS

The CPR has two major components—a reorganization of state entities and other individual recommendations. Below we briefly describe both of these components.

#### Reorganization of State Entities

The CPR proposes a major reshuffling of the state's agencies, departments, boards, commissions, and other entities. In reorganizing state government, the CPR proposal focuses on aligning similar programs and consolidating administrative functions in order to eliminate duplication of effort and improve customer service. The major components of the reorganization are:

- **Creation of 11 Mega-Departments.** The core of the CPR reorganization is the creation of 11 large, mega-departments. These mega-departments would merge the policy-setting function of agencies with the program administration function of departments.
- **Office of Management and Budget.** The CPR reorganization would also consolidate the state's policy and budget oversight agencies into a unified Office of Management and Budget (OMB). The OMB would be responsible for oversight on budgetary, state employment and retirement, technology, and regulatory matters.
- **Tax Commission.** The CPR proposes to merge three of the state's principal tax collections agencies—the Franchise Tax

Board, Employment Development Department, and the Department of Motor Vehicles. The Board of Equalization (BOE), however, would be retained as an independent entity.

- **Discontinuation of Many Boards and Commissions.** The report recommends discontinuing 117 independent boards, commissions, and task forces—including the Air Resources Board, Energy Commission, Student Aid Commission, Board of Prison Terms, and Youth Authority Board. For the majority of these discontinuations, the CPR consolidation would move these entities' activities under one of the new mega-departments.

#### Individual Recommendations

As noted above, the CPR identifies 278 issue areas and contains about 1,200 specific proposals affecting a wide range of government programs. Although the proposals cover a vast number of individual areas, they can be generally placed into one or more of the following five broad categories.

- **Enhancing Program Efficiencies and Service Levels.** Some major examples in this area are: (1) a major proposal to consolidate the eligibility determination process for California Work and Responsibility to Kids (CalWORKs), Medi-Cal, and food stamps; (2) both general and specific proposals relating to the state's workforce; (3) proposals to expand use

of new technologies, such as SMART cards for Medi-Cal, and electronic benefit transfer cards; (4) proposals to increase reliance on the Internet for such things as motor vehicle fee payments and benefit and licensing applications; and (5) various contracting and procurement reforms.

- **Shifting Program Responsibilities and Funding.** These include a targeted realignment of state and local health and social services programs, as well as several proposals to shift costs away from state government to other entities. These include (1) seeking additional federal funds, (2) shifting property taxes from enterprise special districts for the benefit of the state, (3) shifting responsibility for certain highways from the state to local governments, and (4) increasing student fees on out-of-state residents.
- **Privatization.** These include the contracting out to the private sector such functions as child support administration, job training, and health care for prison inmates.
- **Changes in Governance.** These include the elimination of boards and commissions, the consolidation of county offices of education into regional bodies, the elimination of the community colleges' Board of Governors, and a new structure for overseeing the state's use of information technology.
- **Changes in Policy.** While CPR primarily focuses on issues related to efficiencies

and service delivery, it does include several proposals that involve significant changes in underlying policies. Examples include the imposition of a sales tax credit for new business investment, changes in the regulation of timber and other natural resources, expanded use of high occupancy toll lanes, allowing community colleges to offer bachelor degrees, expanding the lottery, and changing the cutoff age for kindergarten enrollment.

## CPR'S SAVINGS ESTIMATES

The CPR indicates that its proposals, if fully adopted, would generate savings of slightly over \$1 billion in 2004-05 and \$32 billion over the next five years combined. According to CPR estimates, about one-third of the cumulative savings would accrue to the General Fund and the remaining two-thirds would accrue to special funds, federal funds, and local funds. Figure 1 (see next page) shows that on an annual basis, savings to the General Fund are projected to be in the range of \$2 billion to \$3 billion per year starting in 2005-06, while annual savings to other funds are projected to average \$5 billion to \$6 billion.

## Proposals With Major Fiscal Effects

As shown in Figure 2 (see page 7), proposals in 15 issue areas account for almost 88 percent of the total savings estimated by CPR for the next five years. Nearly one-half the total is related to just three broad proposals: one to maximize federal grants (\$8.2 billion), another to transform eligibility processing for Medi-Cal, CalWORKs, and food stamps (\$4 billion), and

the third related to the creation of a workforce plan for California state employees that would result in fewer employees (\$3.3 billion). Significant savings are also scored for transportation funding proposals which include seeking higher federal taxes on fuels containing ethanol, changes in enrollment cutoff dates for kindergarten, biennial vehicle registration (mostly one-time revenues from the acceleration of fees paid by motorists), increased lottery sales, and increases in college and university tuition for out-of-state residents.

**Savings Overstated.** In many instances, the CPR was conservative in scoring savings from its individual proposals—acknowledging that actual savings, while likely, simply could not be estimated. However, in other instances, the CPR scored savings that are uncertain or overstated. This is especially the case with regard to many of the proposals with the largest identified savings shown in Figure 2.

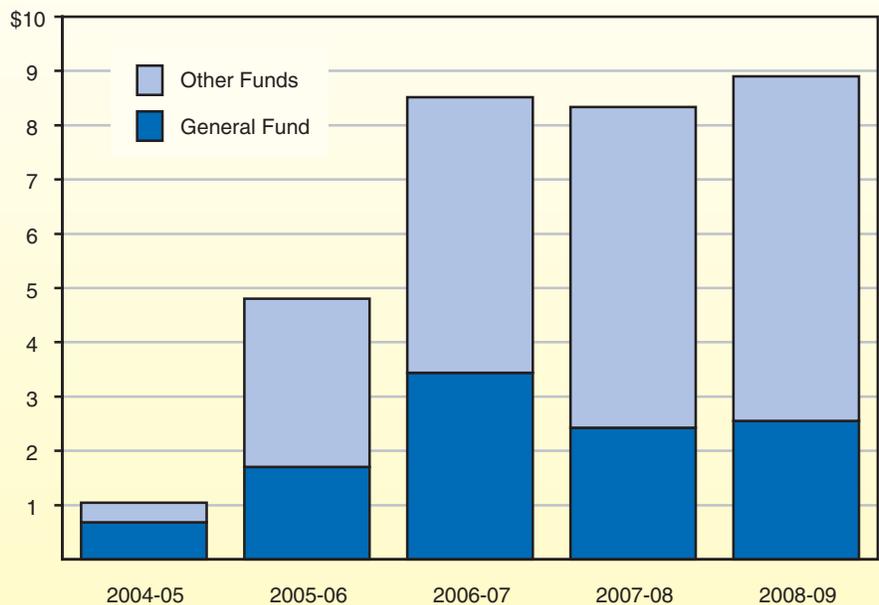
Specifically, we found that:

- **Many of the Proposals Not Fully Developed.** This is particularly the case for the third proposal in Figure 2, where the CPR scores over \$3 billion in cumulative savings from the development of an as-yet unspecified workforce plan.

- **Savings Depend on Federal Actions Rather Than Specific CPR Recommendations.** This applies to the proposal to maximize grant funds from the federal government, as well as the proposal to seek a higher federal tax rate on fuels containing ethanol (which would result in added transportation-related distributions to California). California has long argued for additional federal grants to recognize such factors as its higher-than-average poverty levels and its higher-than-average costs associated with illegal immigration. However, significant increases in federal funds would require changes in federal funding formulas, with potentially negative implications for other states. California is already lobby-

**Figure 1**  
**CPR Estimate of Savings From Its Proposals**

(In Billions)



ing Congress for increased federal taxes on fuels containing ethanol. It is not clear how the process change recommended by CPR will result in the report’s assumed level of federal funds.

- **The Potential Savings Are Beyond What Is Reasonably Achievable.** This applies to several proposals involving consolidations of eligibility determination and procurement processes, lottery savings, and the proposed tax relief for new business equipment investment.
- **Offsetting Costs Not Consistently Recognized.** This is the case for many proposals which would require an initial expenditure of funds in order to realize future savings. Implementation of new

information technology systems is one such example.

- **Savings From Similar Proposals Have Already Been Adopted in the 2004-05 Budget.** This is the case for the tax amnesty, surplus property, nonresident student fee, and several corrections proposals.

Taking into account these factors, we believe that a more realistic savings assumption *attributable to state actions* would be less than one-half of the \$32 billion shown. While any estimate of savings is highly uncertain, we believe that a more reasonable cumulative estimate for all funds over the next five years would be roughly \$10 billion to \$15 billion. In annual terms, this translates into \$3 billion or less per year, divided

**Figure 2**  
**Fifteen CPR Proposals With Largest Fiscal Effects**

*(CPR Estimates, Dollars in Millions)*

Rank	CPR Reference	Issue	Five-Year Savings			Cumulative Percent of Total
			General Fund	Other Funds	Total	
1	GG 07	Maximize Federal Grant Funds	—	\$8,200	\$8,200	26%
2	HHS 01	Transform Eligibility Processing	\$1,548	2,471	4,018	39
3	SO 43	Work Force Plan for California State Employees	1,646	1,646	3,293	49
4	ETV 11	Change Enrollment Entry Date for Kindergartners	1,880	820	2,700	58
5	INF 15	Transportation Funding Initiatives	—	1,960	1,960	64
6	GG 36	Biennial Vehicle Registration	1,259	—	1,259	68
7	GG 06	Lottery Reforms	—	1,024	1,024	71
8	ETV 18	Increase College and University Tuition for Non-Resident Students	—	1,004	1,004	74
9	SO 71	Performance-Based Contracting	485	485	970	77
10	SO 72	Strategic Sourcing	427	427	855	80
11	INF 30	Decentralize Real Estate Services	410	410	819	83
12	INF 13	Relinquish Highway Routes to Local Agencies	—	432	432	84
13	GG 01	Tax Amnesty	384	15	399	85
14	INF 11	Selling Surplus Property Assets	379	—	379	86
15	GG 17	Tax Relief on Manufacturing Equipment	343	—	343	88
		All Other CPR Proposals	2,029	1,921	3,950	100
<b>Totals, All CPR Proposals</b>			<b>\$10,791</b>	<b>\$20,815</b>	<b>\$31,606</b>	<b>100%</b>

roughly evenly between the General Fund and other funds. Regarding the revised General Fund total, nearly one-half of the savings would be attributable to a single proposed change—the delay in the enrollment entry date for kindergartners who are less than five years old at the beginning of the school year.

Our lower overall savings estimate does not make the goals or proposals offered by the CPR any less valid. The state would clearly benefit from changes that enhance workforce productivity, improve and streamline services, and reduce inefficiencies in government—even if the savings were only a fraction of the CPR estimates. At the same time, it is important to recognize that even if all the CPR's recommendations were adopted, the fiscal savings would only cover a relatively small portion of the large structural shortfall facing California's budget in the future. Stated another way, even if the proposals were adopted, the state will continue to face hard choices regarding program funding levels and taxes in order to balance its future budgets.

## ISSUES AND CONSIDERATIONS

The CPR has developed an impressive list of proposals in a relatively short timeframe, which provides the state with a valuable opportunity to examine many aspects of how it does business. At the same time, the report raises a large number of important policy issues which need to be considered.

### Does a Massive Reorganization Make Sense?

California's past successes and failures with reorganization plans strongly suggest that reorganizations should be undertaken only when (1) there is a clearly defined problem with

the existing system and (2) there is a convincing reason to believe that the new system will address the problem and, more generally, enable the state to provide services more efficiently and effectively. We believe there are a number of areas that the CPR has identified where these fundamental criteria may apply. For instance, in the health area, the proposed centralization of a number of public health programs could improve their effectiveness.

Yet, in many other areas, the reorganization plan lacks a strong rationale. As we discuss in more detail in "Section 2," among the problems we identify are:

- The reorganization proposal often lacks sufficient detail to evaluate whether a proposed consolidation would improve state government.
- In some cases, functions are proposed to be joined that are not particularly compatible.
- In some cases, existing departments are divided—with their component functions distributed among several new departments. This may create new coordination problems.
- By moving to mega-departments which would have wide-reaching responsibilities, the CPR risks making departments so large that they become unmanageable.
- The proposed reorganization would result in significant implementation costs, particularly in the short term. In many cases, the fiscal estimates of the CPR do not take into account these expenses.

Given these concerns, we recommend that the Legislature not focus its attention on the large-scale statewide reorganization that the CPR envisions. Instead, the Legislature should seek out more specific opportunities to pursue consolidations on a smaller scale. Many of the current problems that CPR identified could be solved with simpler solutions. A combination of limited consolidations and other types of solutions (such as improved leadership, policy changes, better coordination between departments, interagency agreements, and cross-departmental training) offers a better chance of improving the effectiveness of state government while limiting the risks involved.

### **Should the Scope of Reforms Be Broadened?**

The CPR's proposals encompass a broad range of issues. However, there are a number of fundamental issues that were not considered in the analysis. For example, while the CPR reorganization plan regroups and consolidates a vast number of existing functions of state government, the CPR does not examine the more fundamental question of which functions should continue to be provided by the state. In addition, although the CPR presents a modest realignment proposal, the report does not comprehensively address the state-local system of service delivery. Similarly, while including a single tax incentive proposal, the CPR does not examine California's overall system of state and local taxes.

Finally, while the plan proposes specific changes to the Constitution as it relates to transportation and a biennial budget, it does not address many other constitutional issues, such as the role of constitutional officers and agencies in the restructured government. The latter is a

significant consideration in the context of the CPR's proposed reorganizations. As noted in "Section 2" and "Section 3" of this report, the future roles of the Superintendent of Public Instruction and the BOE—two constitutionally created entities—are left somewhat undefined in the context of the restructured government proposed by the CPR.

Addressing these more fundamental issues may have been beyond the scope of what the CPR believed was its mission, especially given the relatively limited time it had to complete its review. However, the lack of reforms in these areas inherently limits the amount of improvement in governmental services that can be achieved through the CPR.

For example, while some of the CPR proposals may improve efficiency and coordination of state functions, citizens may continue to be faced with the fragmentation of services between state and local governments. Similarly, while the creation of a new tax commission may result in some added efficiencies in the collection and auditing of certain taxes, the exclusion of the BOE from the consolidation means that the state's two largest taxes—the personal income tax and sales tax—will continue to be administered by separate agencies. To address these issues, the Legislature may wish to broaden the scope of reforms it considers.

### **What Is Next?**

The release of the CPR is intended to be a first step in a dialog on governmental reform. Its specific proposals have not yet been embraced by the administration. Rather, the Governor has directed the CPR commission to hold public hearings to seek input on the report's recommendations.

Ultimately, the reorganization plan could be proposed by the Governor through the specific reorganization process provided for in state law (and discussed in “Section 2”). Some of the other recommendations—such as those requiring departments to develop performance measures—could be implemented administratively by the Governor. Other recommendations could be included in the Governor’s 2005-06 or later budgets, or proposed through separate legislation.

Thus, while some of the 1,200 CPR proposals can be adopted administratively, many of them will require legislative approval in order to be implemented. The merits of each proposal would need to be weighed on its own. In “Section 3” we review some of the CPR’s key proposals in major program areas and offer our initial comments on them. Some of the recurring issues raised by our analyses are:

- **More Details Needed.** While many of the more modest proposals are highly detailed, many major proposals are less so. Also, the fiscal estimates associated with many of the proposals—including their start-up costs—have not been developed. As specific proposals are put before the Legislature, these details will need to be included in order to be able to measure the proposals’ true costs and benefits.

- **Key Policy Tradeoffs.** As noted earlier, some of the CPR proposals would involve significant changes in state policies in the areas of education, environmental regulation, and transportation funding, which would need to be weighed by the Legislature.
- **Oversight and Control.** Some of the proposals would significantly reduce legislative oversight and control in key budget and policy matters. Examples include the CPR’s proposal to eliminate numerous boards and commissions and its proposal to consolidate information technology (IT) investments into a single “IT Investment Fund” which would receive continuous appropriation of state funds. Along similar lines, some of the proposed changes to the education governance structure would have impacts on state versus local control regarding community college spending.

For these reasons, it will be important for the Legislature to weigh the merits of each proposal—taking into account its fiscal effects, its policy implications, and whether it represents the most effective way of achieving the fundamental goals of state government.

## SECTION 2: CPR REORGANIZATION

One of the major components of the CPR report is a reorganization of the state’s departments, agencies, boards, and other entities. Below, we describe this reorganization plan and then provide some of our initial observations.

### PRINCIPLES OF THE CPR REORGANIZATION

The CPR report puts forth two principles that are at the center of its approach to reorganizing state entities:

- ***Programs Should Be Aligned by Function.*** The report attempts to combine entities that work in the same policy area or provide similar services. This approach aims to eliminate duplication and improve the performance of state programs.
- ***Administrative Services Should Be Consolidated.*** In addition, the report aims to unify support services within each new department such as human resources, legal affairs, and purchasing—with the goals of greater efficiencies and achieving “economies of scale.”

In addition to these principles, the report also emphasizes improving customer service and ensuring that the best and most effective practices of individual departments are used throughout state government.

### COMPONENTS OF THE REORGANIZATION

***Mega-Departments.*** Currently, the state is organized with both agencies and departments. Agencies generally perform policy-setting and

oversight roles in a particular policy area. Under an agency’s supervision, departments implement programs. For instance, the Department of Financial Institutions (DFI) regulates banks and credit unions under the guidance of the Business, Transportation, and Housing Agency. The core of the CPR reorganization is the creation of 11 large, mega-departments. The proposed 11 departments are listed in Figure 3 (see next page). These mega-departments—called “departments” by CPR—would merge the policy-setting function of agencies with the program administration function of departments.

In most cases, these new departments would represent the merger of several existing departments. For instance, both DFI and the Department of Corporations would merge as a new Financial Services Division within the proposed Commerce and Consumer Protection Department. Other divisions within the same department would include most functions from existing departments such as the Department of Motor Vehicles (DMV) and the Department of Real Estate. In other cases, existing departments are divided—with their component functions distributed among several new departments. For example, functions from the Department of Fish and Game would be distributed to the Environmental Protection, Natural Resources, and Public Safety and Homeland Security Departments.

***Discontinuation of Many Boards and Commissions.*** The state has hundreds of boards, commissions, and task forces which serve a variety of roles—including administering grant programs, regulating industries, and providing policy advice. These entities generally are governed by a board appointed by the Gover-

nor, Legislature, or other state officials. Some board members receive full-time salaries while many others only receive reimbursements for their travel and other expenses. The CPR identified 339 existing boards, commissions, and task forces across state government. The report recommends discontinuing 117 of these entities, including the Air Resources Board, State Lands Commission, Energy Commission, State and Regional Water Quality Boards, Student Aid Commission, Victims Compensation and Government Claims Board, Board of Prison Terms, and Youth Authority Board. For the majority of these discontinuations, the CPR consolidation would move these entities' activities under one of the new mega-departments. In other words, the government activity would continue but be governed by a departmental secretary, rather than an independent board. On the other hand, the CPR would eliminate both the function and the entity in about four dozen cases. Most of these entities entirely eliminated provide policy advice to the state (such as the Rural Health Policy Council and the 911 Advisory Board) rather than administer programs. The report notes that the elimination of these advisory boards could

be replaced with ad-hoc advisors on an as-needed basis.

**Other New Entities.** In addition to the creation of the mega-departments, the CPR proposes to create several other new entities in state government, including:

- **Office of Management and Budget.** The state currently has a number of “control” agencies which provide policy and fiscal oversight to the state’s other entities. For instance, the Department of Finance (DOF) is the state’s fiscal and budget review department. Likewise, the Department of Personnel Administration (DPA) provides departments with services related to state employment. The

**Figure 3**  
**CPR’s 11 Mega-Departments**

Proposed Department	Major Departments Transferred
Commerce and Consumer Protection	Financial Institutions, Consumer Affairs, Motor Vehicles
Correctional Services	Corrections, Youth Authority, Board of Prison Terms, Office of Inspector General
Education and Workforce Preparation	Community Colleges Chancellor, Board of Education, Student Aid Commission
Environmental Protection	Water Quality Control Boards, Air Resources Board, Pesticide Regulation
Food and Agriculture	Food and Agriculture
Health and Human Services	Health Services, Social Services, Mental Health, Developmental Services, Child Support
Infrastructure	Transportation, State Water Project, Energy Commission, Bay-Delta Authority
Labor and Economic Development	Industrial Relations, Employment Development
Natural Resources	Conservancies, Fish and Game, Forestry (Resource Management), Parks and Recreation
Public Safety and Homeland Security	Emergency Services, Highway Patrol, Forestry (Fire Protection)
Veterans Affairs	Veterans Affairs

CPR proposes to consolidate these types of entities into a single Office of Management and Budget (OMB). The OMB would be responsible for oversight on budgetary, state employment and retirement, technology, and regulatory matters. Functions from DOF, DPA, the state's data centers, Department of General Services, and the Office of Administrative Law would be transferred to the OMB.

- **Tax Commission.** The CPR proposes that the state's principal tax collection agencies be consolidated into the California Tax Commission. The commission would include components of the Franchise Tax Board, Employment Development Department, and DMV. The report, however, indicates that the Board of Equalization would be retained as an independent agency.

**Some Entities Largely Unaffected.** In some areas, the CPR proposes few, if any, changes to existing department structures. For instance, constitutional officers are left largely unaffected. In addition, the Military Department would remain an independent entity outside of the mega-department structure. The Departments of Food and Agriculture and Veterans Affairs would be elevated to mega-departments, but their roles and responsibilities would remain largely unchanged.

## IMPLEMENTATION

The report acknowledges that fully implementing its governmental reorganization is an "ambitious" undertaking. The report provides few details on a timeframe for implementation

but suggests the use of a centralized performance review team to coordinate any consolidations.

**The Reorganization Process.** State law provides a specific process for the Governor to propose reorganizations to the Legislature. Since 1968, various Governors have submitted 29 reorganization plans through this process. The Legislature approved 18 of these plans. Figure 4 (see next page) lists these plans, and the box (see pages 18-19) provides a historical perspective on reorganizing state government as it relates to the health and social services area.

Figure 5 (see page 15) provides a sample timeline for the reorganization process. In total, a reorganization plan can take 90 days to become effective. Among the key components of the process are:

- **Goals.** State law encourages the Governor to seek reorganizations which reduce expenditures, increase efficiency, and eliminate duplications of effort.
- **Little Hoover Commission.** As part of the process, the Governor submits any plans to the Little Hoover Commission for review and public hearings. The Commission has 60 days to report any findings to the Governor and the Legislature.
- **Civil Service Transition.** Plans must provide for the transfer of existing state employees from their original department to a new entity carrying out the same function.
- **Legislative Review.** The statute provides for a 60-day legislative review period and calls for policy committees in each house to issue a report on a plan. A plan

**Figure 4****Previous Executive Branch Reorganization Proposals**

Year	Governor	Description	Outcome
1968	Reagan	<ul style="list-style-type: none"> <li>Establish four agencies: Business and Transportation, Resources, Human Relations, and Agriculture and Services.</li> </ul>	Approved
1969	Reagan	<ul style="list-style-type: none"> <li>Eliminate various boards and commissions and transfer some functions to other departments.</li> <li>Change the names of the Department of Harbors and Waterways and the Harbors and Watercraft Commission.</li> <li>Change staff titles and organization names in the Department of Professional and Vocational Standards (DPVS).</li> </ul>	Approved Approved Approved
1970	Reagan	<ul style="list-style-type: none"> <li>Create the Department of Health and consolidate three departments.</li> <li>Change DVPS to the Department of Consumer Affairs.</li> </ul>	Approved Approved
1971	Reagan	<ul style="list-style-type: none"> <li>Change the names of some of the water quality control boards.</li> <li>Eliminate the State Board of Drycleaners.</li> <li>Change the name of the Resources Agency to Environment and Resources Agency and create the Department of Environmental Protection.</li> </ul>	Failed Failed Failed
1975	Brown	<ul style="list-style-type: none"> <li>Consolidate air, water quality, and solid waste programs into the Environmental Quality Agency.</li> <li>Consolidate the Divisions of Labor Law Enforcement and Industrial Welfare into the Department of Industrial Relations (DIR).</li> </ul>	Failed Approved
1976	Brown	<ul style="list-style-type: none"> <li>Consolidate air, water quality, and solid waste programs into the Environmental Quality Agency.</li> <li>Consolidate the Office of Alcoholism with the Department of Alcoholic Beverage Control (ABC) and transfer ABC to the Health and Welfare Agency.</li> </ul>	Failed Failed
1977	Brown	<ul style="list-style-type: none"> <li>Transfer functions from the Office of Narcotics and Drug Abuse to a new Department of Health Services (DHS) and create an Advisory Council on Narcotics and Drug Abuse.</li> </ul>	Approved
1978	Brown	<ul style="list-style-type: none"> <li>Transfer industrial safety and occupational health functions from DHS to DIR.</li> </ul>	Approved
1979	Brown	<ul style="list-style-type: none"> <li>Transfer employment functions from DIR to State and Consumer Services Agency and create the Department of Fair Employment and Housing.</li> <li>Create new central agency for personnel administration.</li> <li>Create the Youth and Adult Correctional Agency.</li> </ul>	Approved Withdrawn Approved
1980	Brown	<ul style="list-style-type: none"> <li>Transfer mobilehome functions to the Department of Housing and Community Development.</li> </ul>	Approved
1981	Brown	<ul style="list-style-type: none"> <li>Create the Department of Personnel Administration (DPA).</li> </ul>	Approved
1984	Deukmejian	<ul style="list-style-type: none"> <li>Transfer position classification functions from State Personnel Board to DPA.</li> </ul>	Approved
1985	Deukmejian	<ul style="list-style-type: none"> <li>Create the Department of Waste Management, State Waste Commission, and three regional waste boards.</li> <li>Create a cabinet-level Department of Waste Management.</li> </ul>	Failed Failed
1991	Wilson	<ul style="list-style-type: none"> <li>Create the Environmental Protection Agency and transfer several departments and functions into the new agency.</li> </ul>	Approved
1995	Wilson	<ul style="list-style-type: none"> <li>Reorganize the California Energy Commission.</li> <li>Consolidate the State Police with the California Highway Patrol.</li> <li>Consolidate the State Fire Marshal with the Department of Forestry and Fire Protection.</li> </ul>	Failed Approved Approved
1998	Wilson	<ul style="list-style-type: none"> <li>Eliminate the Department of Corporations, create the Department of Managed Care, and rename the Department of Financial Institutions.</li> </ul>	Failed
2002	Davis	<ul style="list-style-type: none"> <li>Create the California Labor and Workforce Development Agency and transfer several departments into the new agency.</li> </ul>	Approved

goes into effect after the 60-day period unless the Legislature takes action to reject it. Either house can reject a plan by passing a resolution by a majority vote. The vote is “yes” or “no”—the plan cannot be amended by the Legislature.

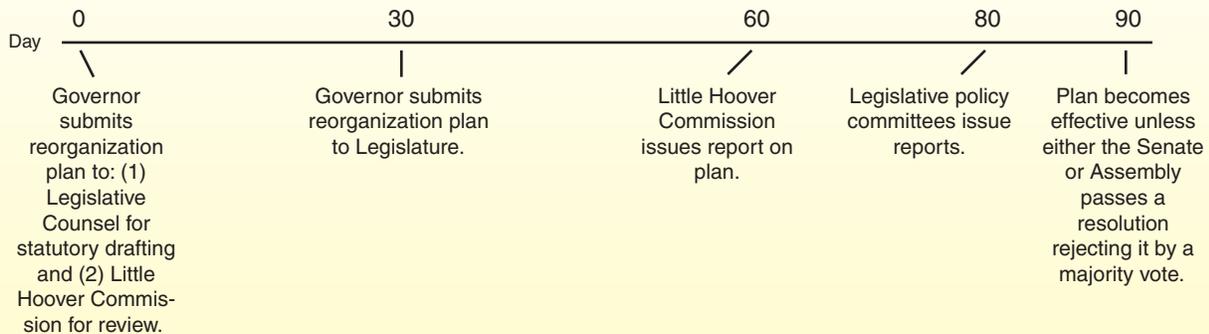
**LAO COMMENTS/KEY CONSIDERATIONS**

In reviewing the CPR reorganization plan, there are many considerations for the Legislature. Figure 6 (see next page) lists some of the criteria that we would suggest the Legislature use in evaluating any proposed reorganization. Below, we outline some additional considerations specific to the CPR and offer our initial comments on the proposed reorganization. Later in this report, we provide more program-specific comments on some of the more significant components of the reorganization.

**Opportunities for Greater Efficiencies Exist, But More Details Needed.** Consistent with the CPR, we believe that many aspects of state government’s organization can be improved. Our initial review of the CPR’s consolidation proposal finds that the report has correctly identified some good candidates for consolidation. For instance, in the health area, the proposed centralization of a number of public health programs could improve their effectiveness. Likewise, the merger of the Departments of Mental Health and Alcohol and Drug Programs could allow the state to better coordinate services to those dually diagnosed patients who are currently served by both departments. At this stage, however, the reorganization proposal often lacks sufficient detail to evaluate whether a proposed consolidation would improve state government. Until the full details of a proposed reorganization are put forth, drawing conclusions about many of CPR’s suggestions is difficult.

Figure 5

**Timeline for Reorganization Plans<sup>a</sup>**



<sup>a</sup> Pursuant to Government Code Sections 8523 and 12080 through 12081.2.

**Reshuffle or Change the Scope of Government?** For the most part, the CPR reorganization is a reshuffling of existing state activities. Examining the organization of government services is a necessary and important task. It is not always clear, however, that CPR asked a more fundamental question—*should the state continue to perform its current functions and provide its current services?* As such, the reorganization plan may have missed the opportunity to rethink what level of government should be responsible for each service or if certain government services are still necessary.

**Is Changing the Organizational Structure the Solution?** As noted above, some of the proposed consolidations offer promise to improve the quality of government services. In other cases, there may be more simple solutions to a massive reorganization. For instance, to increase coordination between two departments, interagency agreements could be developed in place of a full merger. In addition, the administration could use cross-departmental training to spread those management and other practices it has identified as particularly effective.

**Possible Unintended Consequences.** We recognize that any proposed overhaul of state government on the scale of CPR would invite many questions regarding why certain entities are proposed to be placed in one department versus another. In many instances, reasonable minds can differ over in which location a program would be most effective. That said, our initial review raised some concerns with a number of CPR’s choices. The full implementation of the CPR reorganization could lead to some unintended negative consequences. The examples noted below are illustrative that the

**Figure 6**

### Criteria for Considering the Merits of a Reorganization Proposal

As the Legislature considers the CPR and other future reorganization proposals, it may want to consider the following questions to help determine a proposal’s merits.

- ✓ **Effectiveness.** Would the reorganization make the programs more effective? Would the public receive better services as a result of the reorganization?
- ✓ **Accountability.** In the current and the new structures, who is responsible for the program’s outcomes? Is the new structure likely to improve program accountability?
- ✓ **Oversight.** Will the new structure provide for effective, independent oversight by the executive and legislative branches?
- ✓ **Efficiency.** Would the reorganization improve the use of limited resources? Are there reasons to believe that the programs can be administered more efficiently? Do existing programs exhibit duplication of effort or lack of coordination?
- ✓ **Other Options.** What is the problem that is being addressed? Is a reorganization the best approach to solve that problem? Could improved leadership, changes in policy, better coordination between departments, or other solutions provide a better result?
- ✓ **Implementation.** Do the expected long-term benefits outweigh the short-term costs and disruptions from the implementation of the reorganization? Will the public experience a disruption in services? Does the implementation need to occur now, or can it be phased in over time?

Legislature will need to carefully examine each consolidation component in detail.

- **Functions May Not Be Compatible.** In its reshuffling of state departments, the CPR in some cases may have joined functions that are not particularly compatible. For example, the CALFED Bay-Delta Program (overseen by the California Bay-Delta Authority) is designed to approach the Delta from a variety of resource protection perspectives. By moving the authority from the current Resources Agency to the new Infrastructure Department, the CPR could shift the program's focus towards water infrastructure issues and away from other resources issues. Such a shift would represent a significant policy choice for the Legislature. In addition, the CPR proposes to integrate the Department of Managed Health Care (DMHC) with other health programs within the new Health and Human Services Department. These other health programs contract for services with health maintenance organizations (HMOs). These are the same HMO entities that the DMHC regulates. By having a single department regulate and conduct business with HMOs, there is a potential for conflicting goals.
- **Possibility of Creating New Coordination Problems.** In some cases, the CPR proposes to divide current departments and send their various components to multiple mega-departments. In doing so, the CPR aims to better align various functions. The splintering of existing departments, however, could create new

coordination problems. For example, the DMV's investigators, who focus on identity theft and fraud, would be sent to the Public Safety and Homeland Security Department and separated from the rest of the department. As a result, these investigators could become disconnected from the DMV field offices that can often help prevent such problems from developing in the first place.

- **Mega-Departments May Become Unmanageable.** By moving to mega-departments which would have wide-reaching responsibilities, the CPR risks making departments so large that they become unmanageable. In particular, some of the mega-departments would have such expansive goals, missions, and "span of control" that they may find it difficult to administer their day-to-day responsibilities.

**Missed Opportunities.** While the CPR reorganization affects most state entities, the Legislature should not consider the plan an exhaustive list of possibilities. In some areas, there appears to be additional room for consolidations to improve state government. For instance, by keeping the Department of Veterans Affairs outside of most of the reorganization plan, CPR may not have considered the option of merging the veterans' homes with the state's other 24-hour care facilities. Similarly, CPR aimed to consolidate all education programs within the Education and Workforce Preparation Department. Yet, the CPR maintains the existing roles and responsibilities of the Superintendent of Public Instruction (SPI). Maintaining the overlapping responsibilities of the SPI and other

education administrators represents a missed opportunity to repair a central governance issue in K-12 education.

***Considering the Merits of Independent Boards.*** The CPR reorganization emphasizes a transition away from independent boards and commissions and towards executive program management. In evaluating these types of decisions, the Legislature should consider both the benefits and drawbacks regarding the use of independent boards. Among the benefits of independent boards are:

- Boards can include experts in the policy field and offer a variety of policy perspectives.
- Boards may offer more independent, forward-thinking proposals than might be typical from a state department.
- Board meetings are more open to the public than the department decision-making process.

## REORGANIZATIONS: A HISTORICAL PERSPECTIVE

### Reorganizations: Then and Now

Reorganizing state government by consolidating departments, or breaking them apart, is not new. One of the major differences between prior reorganizations and the CPR proposal is its sheer scope. Previous reorganization proposals have focused on a limited number of related departments and programs. These have included, for example, combining labor and employment departments under one agency in 2002; placing various environmental departments under one agency in 1991; and merging health and certain social services programs into a single department in 1970. The CPR proposal, by contrast, envisions a reorganization of the entire state government, involving virtually every state department and generally consolidating them into larger state entities.

### Health and Social Services Experience

***Consolidation of Departments in 1973.*** The CPR's proposal to reorganize health and social services departments into one mega-department is similar—but larger in scope—to one adopted by the Legislature and then subsequently disbanded in the late 1970s. In 1970, Governor Reagan proposed the creation of a unified Department of Health in order to improve the integration of health and related programs, reduce program fragmentation, and further program coordination. In submitting his reorganization plan to the Legislature, Governor Reagan noted: "The Plan that I am submitting to you will enable us to eliminate much of the fragmentation that exists in such fields as mental retardation, alcoholism, and facilities licensing. . . . It will encourage integration of health and related services, replacing the present system under which the consumer must find his way through a maze of uncoordinated services."

- The Legislature often has the ability to oversee a board's management through the nomination approval process. In other cases (such as the High Speed Rail Authority), the Legislature has the authority to appoint board members directly.

On the other hand, independent boards also may have some disadvantages, including:

- Boards may cost more to operate, due to the salaries and associated costs of board members.
- A department can often shuffle resources among multiple programs as dictated by workload. In contrast, since they administer individual programs, boards typically do not have the same degree of flexibility.
- Boards may have difficulty in coordinating their work with state departments when their program responsibilities overlap. When programs all report to the same director under a single department, coordination may improve.

In response to Governor Reagan's proposal, the Department of Health was created effective July 1, 1973 by combining the former Departments of Mental Hygiene, Public Health, and Health Care Services together with the social service functions of the Department of Social Welfare. Among other programs, the new department was responsible for: Medi-Cal, public health, mental health, drug and alcohol, developmental disabilities, licensing and certification of health facilities, and various social services for welfare recipients. (The department was not responsible for providing welfare cash grants, which was assigned to a new Department of Benefit Payments.)

**Separation of Departments in 1978.** For a variety of reasons, the unified Department of Health was unable to fulfill its promise, leading to the enactment of Chapter 1252, Statutes of 1977 (SB 363, Gregorio), which created five new departments and one new office. In enacting Chapter 1252, the Legislature declared that it was separating the Department of Health into distinct departments in order "to increase individual program visibility, to improve program policy direction and to provide needed public accountability." The new departments were Health Services, Social Services, Mental Health, Developmental Disabilities, and Alcohol and Drug Abuse. The new office was the Office of Statewide Health Planning and Development.

**Implications for CPR Proposal.** The fact that a large consolidated department did not work the last time around does not mean that the current CPR proposal to establish a consolidated Health and Human Services Department should be rejected automatically. Rather, it provides a cautionary warning that reminds the Legislature and administration that they will need to (1) determine whether there are any lessons to be learned from the state's previous experience, and (2) assess how the new proposed reorganization meets their criteria for improving the delivery of state services.

**Unknown Implementation Costs.** The proposed reorganization, if implemented, would result in significant implementation costs, particularly in the short term. In many cases, the fiscal estimates of the CPR do not take into account these expenses, such as the costs for integrating data and budget systems and relocating offices. As an example, the recent closing of the Technology, Trade, and Commerce Agency cost millions of dollars in shutdown expenses—

nullifying most of the savings for the first year. While these types of implementation costs typically do not provide sufficient justification on their own to dismiss a proposed reorganization, the Legislature should be aware of them in making its decisions. This is particularly true in the cases when the recommendations are being implemented primarily to generate budget savings.

## SECTION 3: REVIEW OF KEY PROPOSALS BY PROGRAM AREA

This section discusses key CPR proposals in major program areas. Given the number of recommendations included in the CPR report, we have identified the recommendation by the number used in the report to the Governor (such as GG 05 referring to General Government recommendation 5) to assist the reader. In the case of criminal justice, CPR has incorporated the recommendations of the Corrections Independent Review Panel (CIRP) and we have referenced chapter numbers in the CIRP as appropriate. Following each programmatic discussion is a figure summarizing the fiscal effect, as estimated by CPR, for the key proposals discussed. When the CPR could not make an estimate, we have adopted its nomenclature of “cannot be estimated” (CBE) for consistency purposes. We offer initial comments on the major proposals to assist legislative consideration of these proposals.

### K-12 EDUCATION

The CPR makes 14 recommendations that affect K-12 education. These recommendations

cover a variety of policy areas. Seven of the fourteen recommendations seek changes to help the state department or school districts operate in a more cost-effective manner. Four recommendations propose specific K-12 policies that are designed to help districts meet student needs more effectively. The remaining three recommendations would make structural changes to the roles and responsibilities of state and county educational agencies.

**Restructure the Role of the Secretary for Education.** The CPR proposes to expand the role of the Secretary for Education by assigning it policy and coordinating responsibilities as the head of a new Department of Education and Workforce Preparation (ETV 01). The recommendation would place six existing state departments under the Secretary, including the State Department of Education, California Community Colleges (CCC), California Student Aid Commission (CSAC), and Commission on Teacher Credentialing. The Secretary would focus on developing educational policy (pre-kindergarten through college), implementing higher educa-

tion policy, and aligning education with workforce needs. The Superintendent of Public Instruction (SPI) would remain an elected position.

**LAO Comments.** Reorganizing state government with the aim of increasing system coherence is a worthy goal. The Governor has little institutional capacity to plan and coordinate educational policies. In the social services area, for instance, these functions are provided by the Health and Human Services Agency. The creation of the Secretary for Education addressed this capacity issue to some extent. Because many of the state’s educational agencies report to independent boards or constitutional officers, however, the Secretary has little institutional leverage to ensure cooperation over policy matters from these entities.

The report, however, does not adequately address a central governance issue in K-12 education. By maintaining the existing roles and responsibilities of the SPI, the CPR recommendation fails to untangle overlapping responsibilities for policy making that are statutorily assigned to the elected SPI and the Governor-appointed State Board of Education. In our 1999 report, *A K-12 Master Plan*, we recommended restructuring the SPI’s scope of responsibilities to take advantage of the office’s independent voice to promote accountability and local control. Under our master plan, the Secretary for Education would assume most program responsibilities currently administered by the SPI. By creating complementary roles for the SPI and the Governor, the Legislature could create greater accountability for state K-12 policies and take advantage of the independence of the SPI to represent the interests of districts and parents.

**Regionalize K-12 Educational Infrastructure.** The CPR proposes to eliminate county superintendents and county boards of education from the State Constitution and, instead, statutorily create a system of regional superintendents and boards to provide services currently administered by county offices of education (ETV 05). The report questions the need for a county aligned structure, based on the number and configuration of counties in California, the number of counties with fewer than 6,999 K-12 students, and the variability of services provided by the different county offices.

**LAO Comments.** The report does not discuss what role county offices—or regional agencies—should play in the provision of K-12 services. This is an important omission, as the structure of the service delivery system should support the desired program objectives of the system. Current law assigns a wide variety of functions to county offices, including:

- Direct student services (such as alternative education programs for expelled or probation-referred students).
- Direct services to districts (such as accounting and payroll).
- Technical assistance to districts (educational technology, for example).
- State oversight functions (such as review of district budgets and finances).

In general, we agree with the 1996 recommendation of the California Constitutional Revision Commission to make districts responsible for obtaining most services currently provided by county offices from whatever source is most efficient and effective. This would

give districts more latitude to purchase the types and levels of services that best meet each district's needs. In addition, it would strengthen district accountability for students who currently are served in county office programs.

Such an approach would leave a relative handful of services that county offices or regional agencies would provide for the state. This includes educational services for students residing in juvenile court, district budget and fiscal review, and adjudicating student expulsion appeals and district reorganizations. We think county offices could effectively provide these services with appropriate state oversight. While it is possible that regional agencies could function at a lower cost, the size of the CPR's estimated savings—\$18 million a year, or an average of \$300,000 per county—are not large enough to justify the regional approach based solely on cost savings.

**Performance-Based Contracts.** The CPR proposes to test whether distributing K-12 categorical support as part of a performance-based contract between the state and K-12 school districts would provide greater local flexibility and encourage districts to meet student needs more effectively (ETV 10). The report finds the existing system of categorical programs is “inequitable, ineffective, burdensome” and “focuses on spending rather than on student outcomes.” It proposes a five-year pilot program in which categorical funds would be merged into one block grant.

**LAO Comments.** The CPR's emphasis on flexibility (a block grant in lieu of individual programs) in exchange for greater outcome accountability (through a performance contract) is an appropriate approach to reform. Categorical reform requires understanding and improving

the fiscal and program incentives of districts. Greater local flexibility can be afforded when districts are clearly accountable for their decisions. A larger state role is needed when districts can shift the consequences of local decisions to others.

The report does not provide any details on how the performance contract would work. Without specifics on the proposed performance contract, however, we are unable to assess the merits of the CPR recommendation. Even with a well-specified contract, however, we are skeptical that combining all categorical funds into one block grant makes sense. This is because restricting funding to specific uses is central to altering district incentives in some cases. This is not a fatal flaw—combining funds into several block grants (with appropriate accountability features) does not significantly weaken the CPR's approach. In fact, we made a very similar recommendation in our *Analysis of the 2003-04 Budget Bill*, where we encouraged creation of five block grants that combined funding from 62 programs. Each block grant focused on a broad K-12 program area (compensatory education, school improvement, etc.) and contained outcome measures designed to increase district accountability for services funded from the block grant.

**Change Kindergarten Enrollment Entry Date.** The CPR proposes to change the kindergarten entry date (that is, the date by which a child must have reached five years of age) from December 2 to September 1. The CPR proposes to implement this change in 2005-06 (ETV 11). The CPR estimates five-year savings from its proposal of \$2.7 billion. The date change would create two types of savings. First, the change would reduce the Proposition 98 minimum funding guarantee by \$1.88 billion over the five-year period, resulting in savings to the General

Fund. Second, an additional \$820 million (about \$200 million annually) in savings within the Proposition 98 guarantee would be “freed-up” and available for other K-14 purposes.

**LAO Comments.** In our view, actual Proposition 98 savings during the first year of implementation would be less than the CPR projects. Many districts already are experiencing declining elementary school enrollments, and state law allows one-year “hold-harmless” funding for districts experiencing enrollment reductions.

While we think the CPR proposal has merit, several other issues warrant further discussion. The report bases its recommendation on studies showing that students who are older when they enter kindergarten are more likely to succeed in school. It further notes that 38 states have kindergarten entry dates prior to California’s December date. Research on the merits of changing the kindergarten entry date, however, is more mixed than suggested by the report.

In addition, the report excludes any discussion of the impact of the date change on school districts and on families. The CPR’s proposal presents difficult logistical issues for districts, and magnifies the fiscal issues districts face from declining student enrollment. If the change in entry date is adopted, the Legislature should consider giving districts flexibility to implement the change in one year or to phase-in the change over a longer period (up to three years).

Changing the kindergarten entry date may also create additional demand for preschool or child care for those students whose birth dates fall between September 1 and December 2. The Legislature could choose to redirect all or part of the \$200 million annual Proposition 98 savings to provide child care for children displaced by the change in the kindergarten entry date. Using

the average cost of half-day preschool programs administered by the State Department of Education, \$200 million would be sufficient to fund an additional 63,000 child care “slots” annually, or about 65 percent of the displaced students.

**Balance Career Technical Education and College Preparation in High Schools.** The CPR recommends strengthening high school vocational programs by creating two paths to high school graduation—one focused on admission to a four-year college or university and a second that prepares students for employment or post-secondary vocational study (ETV 25). The report estimates that these changes would cost about \$300,000 annually.

The report suggests two major changes to implement this recommendation. First, the CPR recommends modifying the state law that specifies the courses students must take to graduate from high school. Both the university and career “pathways” would require students to take more core academic courses than existing law. The career pathway would require students to take at least five vocational—or career technical—courses. The university pathway course requirements are consistent with the admissions criteria set by the University of California (UC) and California State University (CSU).

Second, the report recommends including career technical education in the state’s Academic Performance Index (API). The API is part of the state’s accountability system and is used to rank school and district performance based on student test scores.

**LAO Comments.** Vocational education is an important part of secondary education. For many students, high school is their last formal educational opportunity. Moreover, many college students work while in school. Voca-

tional education can give an advantage to both groups of students in the labor market. It is not a cure-all remedy, though, and the CPR may overstate the benefits from its proposed recommendations. A 2004 federal report on vocational education, for instance, concluded that typical vocational education courses have no effect on academic achievement, little or no effect on graduation rates, and only a modest increase in post-graduation earnings (due to higher levels of employment, not higher earnings).

High schools face tremendous challenges. A large proportion of entering 9<sup>th</sup> grade students are ill prepared or motivated to engage in a rigorous high school education. Another large percentage of students enroll in college despite the fact they have not achieved the minimum

academic skills required of university students. Reinvigorating vocational education is part of the solution to these problems—and the CPR recommendations warrant consideration. By themselves, however, it is unlikely that altering the “seat time” requirements for high school graduation will achieve the report’s goal. In addition, school districts would likely experience significant mandated costs to restructure local course offerings. These costs would be supported with Proposition 98 funds, and therefore would not increase state General Fund costs.

## HIGHER EDUCATION

The CPR recommendations concerning higher education generally involve a major proposal to consolidate various higher educa-

**Figure 7**

### Major K-12 Recommendations

CPR Reference	CPR Recommendation	CPR 2004-05 Fiscal Effect	CPR Five-Year Cumulative Fiscal Effect
ETV 01	<b>Restructure the Role of the Secretary for Education</b> —Strengthen the role of the Secretary in developing and coordinating K-12 education, higher education, and workforce preparation policies.	None	None
ETV 05	<b>Regionalize K-12 Educational Infrastructure</b> —Replace county offices of education with regional agencies.	None	Savings of \$45 million Proposition 98
ETV 10	<b>Establish Performance-Based Contracts Between State and K-12 School Districts</b> —Test whether providing categorical funds as part of performance-based contracts improves student outcomes.	CBE	CBE
ETV 11	<b>Change Enrollment Entry Date for Kindergartners</b> —Enroll in kindergarten only children who reach age 5 by September 1.	None	Savings of \$820 million Proposition 98 \$1.9 billion non-Proposition 98
ETV 25	<b>Balance Career Technical Education and College Preparation in High Schools</b> —Alter graduation and accountability policies to strengthen high school vocational education programs.	Costs of \$100,000 Proposition 98	Costs of \$1.7 million Proposition 98

tion agencies and various proposals concerning student enrollment and higher education finance.

### **Organizational Structure**

***Consolidation of Higher Education Agencies (ETV 03).*** One of the most significant structural changes proposed for higher education is to consolidate the Chancellor's Office of the CCC, the California Postsecondary Education Commission (CPEC), CSAC, and the Bureau for Private Postsecondary Education (BPPE) into a single, unified "Higher Education Division." The division would be led by a Deputy Secretary for Education, appointed by the Governor and reporting to the Secretary for Education. The division would be responsible for strategic planning and policy coordination among the four consolidated entities. This recommendation is expected to result in annual savings of about \$1.5 million in General Fund support and another \$1.5 million in special funds, largely due to the elimination of staff positions.

***LAO Comments.*** Parts of this recommendation have been proposed before or are being considered in legislation. For example, in the 2003-04 May Revision the previous administration had proposed the consolidation of CPEC and CSAC. Although that budget-related proposal was rejected by the Legislature, the Legislature considered a bill (AB 655, Liu) that would have consolidated CPEC, CSAC, and BPPE into a single entity. All provisions relating to that consolidation, however, were amended out of AB 655 in July 2004. Other legislation, some of which was pending at the time this report was written, would make significant changes to the structure of and mission of CPEC and CSAC, and would extend the BPPE beyond its current 2005 sunset date.

Three of the agencies to be consolidated (CPEC, CSAC, and CCC Chancellor's Office) are currently governed by boards or commissions that are appointed by the Governor and the Legislature. It is unclear what role, if any, those boards and commissions would retain under this proposal.

While the Legislature has in recent years expressed interest in reorganizing the agencies targeted by this CPR proposal, there have been no significant efforts to combine higher education agencies that perform statewide functions with an office that governs a public segment of higher education. It is unclear why the CCC Chancellor's Office was included as part of the CPR's proposed consolidation, especially when the other two public segments (the UC and the CSU) were not included. At the same time, the report raises important questions about the structure and function of CCC's Chancellor's Office and the Board of Governors to which it currently reports. This topic has also been raised by the Joint Committee to Develop a Master Plan for Education and other legislative committees and Members.

### **Modifying Policies Concerning Student Enrollment**

The CPR report includes a number of proposals affecting student enrollment. Major recommendations include:

***CCC Concurrent Enrollment (ETV 08) and Enrollment Priorities (ETV 19).*** The CPR report proposes various policy changes concerning the enrollment of high school students at community colleges. The CPR proposal would both remove some limitations on concurrent enrollment (such as the requirement for high school permission to be granted) and impose some

new ones (such as limiting the number and type of student concurrent enrollments).

In a separate recommendation (ETV 19), the report calls on CCC to adopt enrollment priorities that would give preference to students who have not taken an “excessive” number of units, ensuring that limited course spaces be available to newer students who have not yet made extensive use of higher education opportunities.

**Facilitating Student Transfer (ETV 15).** The CPR report proposes the development of lower division, general education, and major requirements that would be common to all public universities. Such standardization would be intended to help students transfer among the various segments and campuses of higher education without facing varying course requirements.

**LAO Comments.** The objectives of the above proposals merit legislative consideration. In general, there is a need to better ensure that students are enrolling in appropriate classes consistent with their educational objectives and that the entire higher education system is sufficiently integrated and coordinated.

### **Modifying Policies Concerning Fees and Financial Aid**

The CPR report makes a number of recommendations concerning student financial aid, student fees, and tuition. Major proposals include:

**Cal Grant Programs (ETV 16).** The CPR report recommends that portions of the existing Cal Grant program (which provides funds to students for fees and other higher education expenses) be replaced with a fee waiver program at UC and CSU. Administration of Cal Grant awards for community college students would also be decentralized to the CCC campuses.

**Increase Nonresident Tuition (ETV 18).** The report recommends that nonresident students at all three segments be charged tuition that is 45 percent higher than the 2003-04 level.

**Contract Out CSAC’s Loan Guarantee Function (ETV 22).** The CPR report calls for CSAC to contract with a private entity to perform CSAC’s federally imposed administrative obligations concerning student loan guarantees. It would also seek legislation to permit EdFund to compete as a provider of student loan guarantee services.

**LAO Comments.** In recent publications we have recommended reforms to the state’s financial aid programs and the adoption of a long-term student fee policy. We believe that, because fees and various financial aid programs are interlinked, modifications to individual elements of these programs should be considered in the broader context of affordability and access.

As regards the recommendation to raise nonresident tuition 45 percent above the 2003-04 level, we note that for 2004-05, nonresident tuition at UC and CSU increased 20 percent above the 2003-04 level. Concerning the proposed changes to the Cal Grant programs, it is unclear what would happen to the nonfee (subsistence) portions of the Cal Grant B awards. Specifically, would students still receive funding to help cover related costs such as books and housing?

### **Other Major Proposals**

The CPR report makes a number of other proposals concerning higher education, the most significant of which are identified below.

**Higher Education Accountability (ETV 21).** The report recommends that the Governor set

clear statewide goals and expectations for higher education through an executive order. It further calls for the development of “an enforceable state-level accountability system” to foster progress on those goals.

**Permit CCC to Offer Baccalaureate Degrees (ETV 23).** The CPR report recommends that a pilot program be developed that allows certain community colleges to offer baccalaureate degrees, with the goal of increasing opportunities for students to earn such degrees.

**Modify CCC’s Full-Time Faculty Requirement (ETV 27).** The CPR report recommends that career-technical courses be excluded from the statutory requirement that full-time faculty constitute at least 75 percent of community colleges’ faculty.

**LAO Comments.** Accountability measures and mechanisms in recent years have been developed for K-12 systems nationwide. This trend is now beginning to extend to higher education. As a first step, promoting account-

ability requires the development of outcome standards. In California, there has as yet been little progress in developing such standards. Pending legislation (SB 1331, Alpert) would create a higher education data system to track higher education performance using selected outcome measures. The CPR report recommends the Governor support the concepts contained in this bill, which might serve as a starting point for an accountability structure.

The proposal to permit community colleges to offer baccalaureate degrees runs counter to state law and the state Master Plan for Higher Education, which assigns CCC the role of offering lower-division instruction to students, who then may wish to transfer to a university to earn a baccalaureate degree. State law assigns to CCC a variety of other responsibilities as well, such as vocational education, remedial education, and local economic development. Consideration of this proposal raises broader issues of the Master Plan’s basic division of responsibility

**Figure 8**  
**Major Higher Education Recommendations**

CPR Reference	CPR Recommendation	2004-05 Fiscal Effect	CPR Five-Year Cumulative Fiscal Effect
ETV 03	<b>Consolidation</b> —Consolidate selected state higher education agencies.	None	Savings of \$5.3 million General Fund \$5.3 million special funds
ETV 08 ETV 15 ETV 19	<b>Student Enrollment</b> —Modify policies concerning student enrollment.	None	Savings of \$175 million Proposition 98 Unknown General Fund
ETV 16 ETV 18 ETV 22	<b>Fees/Financial Aid</b> —Modify policies concerning fees and financial aid.	Savings of \$5.6 million Student Loan Operating Fund \$48.8 million student fees	Savings of \$32 million Student Loan Operating Fund \$1 billion student fees Unknown General Fund
ETV 21 ETV 23 ETV 27	<b>Other Major Proposals.</b>	None	Unknown General Fund savings.

among the three public segments of higher education.

Concerning the full-time faculty requirement, our office has recommended in the past that the 75 percent requirement should be eliminated. Instead, we believe that individual colleges should be permitted to select the mix of full- and part-time faculty that they believe would result in the best education for their students given their available financial resources. (See our *Analysis of the 2001-02 Budget*, pages 215-216.)

## **HEALTH AND SOCIAL SERVICES— CROSSCUTTING ISSUES**

### ***Transform Eligibility Processing (HHS 01).***

The CPR recommends changing eligibility processing for Medi-Cal, California Work Opportunity and Responsibility to Kids (CalWORKs), and Food Stamp programs from a paper-intensive system operated by 58 individual county welfare departments into a consolidated system operated at the state level. The state would hire a contractor to develop a new system that would take advantage of information technology (IT) and accept applications via the Internet, telephone, and mail. According to CPR, this proposal would achieve additional efficiencies by eliminating the asset test for most applicants and allowing people to self-certify their assets under penalty of perjury. The state would also operate a public awareness program and pay \$50 per application to assistants to help ensure that people submit complete applications. The CPR estimates that the proposal would result in costs of \$1 million are anticipated in 2004-05 and net cumulative savings of \$4 billion (\$1.5 billion General Fund) over five years.

**LAO Comments.** This proposal is compelling given the significant amount of savings esti-

mated. However, it is highly uncertain if the proposed level of savings would be achieved. Our *Analysis of the 2003-04 Budget Bill*, similarly recommended the Legislature consider centralizing the eligibility determination process for Medi-Cal, but cautioned that the level of savings was unknown and that transferring this responsibility from the counties would be a difficult and complex task. Such a transfer would require changes in state law, the waiver of federal laws, and negotiation with state and county unions. It would also require the implementation of a significant IT project which could be risky and costly given the state's history with developing large IT systems. Implementation of a state-operated system would likely take longer than the CPR proposed and a staged implementation over several years should be considered to ensure that potentially adverse impacts could be addressed. In addition, any simplification of the eligibility determination process might increase program utilization resulting in greater costs.

Despite the complexity of such an undertaking, this proposal also has programmatic advantages, in addition to the potential to achieve savings. For example, adopting a single eligibility determination system would ensure greater uniformity in processing applications. Self-certification of assets would make eligibility requirements for these programs more consistent with the Healthy Families Program (which serves persons with greater income levels). However, the Legislature should weigh the likelihood of achieving the estimated savings versus potential increases in costs from greater caseloads.

***Realignment of State and County Responsibilities (HHS 02).*** Currently, counties are 100 percent responsible for the Medically

Indigent Adult (MIA) Program and many mental health programs. However, the state is responsible for roughly 90 percent of the Early and Periodic Screening, Diagnosis, and Treatment (EPSDT) program and 100 percent responsible for certain Medi-Cal mental health benefits. In addition, counties are responsible for about 35 percent of the costs of In-Home Supportive Services (IHSS), 40 percent of the cost of foster care, and 30 percent of the costs of child welfare. The CPR proposes that the state be 100 percent responsible for both the MIA and IHSS programs. The CPR also proposes that the counties be 100 percent responsible for child welfare services, foster care, and all mental health programs, including EPSDT. The CPR estimates that the proposed realignment is roughly budget neutral, resulting in estimated annual net state costs of \$29 million and identical county savings.

**LAO Comments.** Generally, the proposed realignment is consistent with previous recommendations we have made regarding which level of government should have financial responsibility and program control for various health and social services programs. Given the intended role of IHSS in preventing the need for

long-term care, it makes sense to have both programs operated at the same level of government. Giving counties control over the full array of children’s services makes sense in that they would control the interactive process of child welfare services and foster care. Given the generally positive results of the 1991 mental health realignment, providing the counties with financial responsibility and program control for the remaining mental health programs makes sense.

Although the report states that MIA program costs are unknown, the CPR assumes MIA costs are \$1.5 billion. To the extent that MIA costs differ from \$1.5 billion, the realignment proposal may not be cost neutral. Further, moving the MIA program into Medi-Cal requires federal approval and could lead to unanticipated caseload increases because federal approval of Medicaid expansions may require the state to expand eligibility for other low-income Californians. In addition, increased costs to any county resulting from the transfer of program and funding responsibility likely would be considered a reimbursable state mandate, particularly if voters approve Proposition 1A on the November 2 ballot.

**Figure 9**

**Major Health and Social Services Crosscutting Recommendations**

CPR Reference	CPR Recommendation	CPR 2004-05 Fiscal Effect	CPR Five-Year Cumulative Fiscal Effect
HHS 01	<b>Transform Eligibility Processing</b> —Reduce costs by centralizing eligibility determinations for Medi-Cal, CalWORKs, and Food Stamp programs at the state level.	Costs of \$625,000 General Fund \$375,000 federal funds	Savings of \$1.5 billion General Fund \$2 billion federal funds \$472 million county funds
HHS 02	<b>Realignment</b> —Shift IHSS and Medically Indigent Adult programs to the state. Shift child welfare services and mental health to the counties.	None	Costs of \$116 million General Fund Identical county savings

## HEALTH SERVICES

### Medi-Cal

***Intermediate Care Facilities for the Developmentally Disabled (HHS 24).*** The CPR recommends that the state submit a state Medicaid plan amendment from the federal Centers for Medicare and Medicaid Services to more broadly define the services provided by an Intermediate Care Facility for the Developmentally Disabled (ICF/DD). This would allow the state to increase federal funding for these services and reduce General Fund expenditures by \$152 million over five years.

***Other Health Coverage (OHC) for Medi-Cal Beneficiaries (HHS 27).*** Federal law requires that the Medi-Cal Program be the payer of last resort and ensure that the state does not pay claims for health care services when a beneficiary has another source of health coverage (for example, eligibility for Medicare). This proposal would disenroll from Medi-Cal managed care plans approximately 76,000 Medi-Cal enrollees who have another source of health coverage, employ a contractor on a contingency fee basis to identify persons with OHC, and reduce the number of state staff by nine. These combined actions result in annual net savings beginning in 2005-06 of \$53.7 million (\$26.8 million General Fund).

***Medi-Cal Antifraud Program (HHS 28, HHS 31, PS 08, PS 12).*** Two of the four changes the CPR recommended in the Medi-Cal antifraud program would shift existing positions from the Department of Health Services (DHS) to the Department of Justice and to the proposed Department of Public Safety and Homeland Security that would consolidate existing

law enforcement agencies. Shifting the positions is expected to increase federal funds, address management and training problems, and allow for greater coordination of statewide law enforcement efforts. The CPR also recommends the Medi-Cal Program pilot the use of "smart cards" that use computer chips to store a beneficiary's health and personal data in order to improve its ability to identify fraud. Finally, the CPR recommends the Medi-Cal Program ensure that its antifraud efforts are most effective by using strategies that are driven by data and target areas where the most savings can be generated and beneficiaries protected.

***LAO Comments.*** The CPR recommendation to draw down additional federal funds to offset the state cost of services provided to residents of ICF/DDs should be pursued as recommended in our *Analysis of the 2004-05 Budget Bill*. The CPR estimate of savings does not adjust for annual increases in caseload and utilization that have been rapidly growing in recent years and as a result savings may potentially be higher. The proposal to identify OHC has merit in order to ensure that the Medi-Cal Program is the payer of last resort. However, the ability to achieve the estimated level of savings is uncertain because it is unclear if the CPR estimate considers various potential cost increases such as the state paying monthly premiums for OHC. Finally, regarding the fraud recommendations, DHS is required to complete an error rate study by November 2004 that will measure the major types of Medi-Cal fraud. Any reorganization of the Medi-Cal antifraud program should await the outcome of the study so the state will have the information necessary to focus its resources on combating the most serious fraud problems.

## Public Health

**Public Health Funding Agreements (HHS 12).** The CPR recommends that DHS simplify its public health funding agreements with city and county health departments by reducing the number of contracts written and processed and by using web-based applications to facilitate the contracting process.

**California's HIV and AIDS Reporting Systems (HHS 14).** The report includes a proposal to convert the state's HIV reporting system from a code-based to a name-based format and to expand laboratory reporting requirements to include the reporting of low T-cell (or white blood cell) counts. The CPR asserts that the change in HIV reporting is warranted given the possibility of losing federal funding and the work required by laboratories and local health departments to maintain the system.

**Revenue Collections in DHS (HSS 20).** The CPR further recommends the consolidation of revenue collection activities and the redirection of staff associated with DHS's licensure, certification, and enforcement programs and the pursuit of web-based technology to streamline revenue transactions.

**LAO Comments.** Many of the CPR recommendations for streamlining administrative activities in public health programs lack an estimate of the net fiscal impact making it difficult to assess and prioritize the recommendations. Also, proposals requiring the development of IT systems have unknown costs that potentially would offset any savings achieved during the initial years.

The recommendation to consolidate the public health contracts would relieve workload pressure on DHS, but primarily local govern-

ments would benefit financially from this proposal because they would have fewer reporting requirements and applications for grants that they must submit. Previous attempts to change the HIV reporting system to a name-based one have failed partially due to concerns about confidentiality. Also, the CPR has raised the concern that the existing reporting system might not meet federal standards in the future. Lastly, maximizing revenue collections would potentially increase funds for various fee-supported programs and strengthen oversight by prioritizing and dedicating a single unit to this activity. However, the Legislature should ensure the redirection of program staff does not impair licensure, certification, and enforcement activities.

## SOCIAL SERVICES

### Department of Child Support

**Competitive Bidding Process (HHS 03).** This recommendation requires the Department of Child Support to conduct a competitive bidding process which allows public and private providers to compete to provide child support collection services at the local level. The selection of local vendors would be done at the state level, not the county level. This recommendation is intended to address the state's continued poor performance on the federal child support outcome measures.

**LAO Comments.** This recommendation significantly increases state control since the state would select the vendor. Local child support agencies, except to the extent that they successfully bid for the contract, would no longer have a role in the program. The existence of strong performance measures makes privatization a potentially viable option for this

program because such measures would enable the state to track the performance of various vendors and adjust contract terms and payment rates as necessary. Nevertheless, the same measures could be used in a county-run performance-based system. Privatization raises two additional questions: (1) can the state complete and successfully operate the federally required statewide automation system in a privatized environment and (2) are there private firms willing to bid on the *entire* array of child support services. The savings (\$29 million General Fund over five years) assumed for this recommendation appear to be reasonable.

### Licensing and Certification

The CPR proposes two significant reforms in the area of licensing and background checks for health and social services programs. The first recommendation is a policy reform that standardizes background checks within the proposed Health and Human Services Department (HHSD). The second recommendation is a structural reform which consolidates within one office of the restructured HHSD all of the licensing and certification functions which currently exist within various departments.

**Standardizing Background Checks (HHS 19).** Several departments within the Health and Human Services Agency conduct

**Figure 10**

### Major Health Recommendations

CPR Reference	CPR Recommendation	CPR 2004-05 Fiscal Effect	CPR Five-Year Cumulative Fiscal Effect
HHS 24	<b>Intermediate Care Facilities for the Developmentally Disabled</b> —Increase federal funds by broadening definition of eligible services.	None	Savings of \$152 million General Fund
HHS 27	<b>Other Health Coverage</b> —Automate identification of other sources of health coverage to ensure that Medi-Cal is the payer of last resort.	None	Savings of \$107 million General Fund \$108 million federal funds
HHS 28	<b>Smart Cards</b> —Reduce the amount of fraud and abuse in Medi-Cal through the use of smart cards.	Cost of \$75,000 General Fund	Savings of \$78 million General Fund
HHS 31	<b>Medi-Cal Fraud Targeting</b> —Redirect fraud efforts to achieve greatest savings.	CBE	CBE
PS 08	<b>Medi-Cal Fraud Investigations Branch</b> —Transfer this branch to the Department of Public Safety and Homeland Security in order to improve management, training, and coordination.	CBE	CBE
PS 12	<b>Medi-Cal Provider Fraud Investigations</b> —Transfer these activities to the Department of Justice thereby increasing federal funds and reducing General Fund costs.	Increased federal funds of \$1 million	Increased federal funds of \$8 million
HHS 12	<b>Simplify Public Health Funding Agreements</b> —Streamline contracting for local governments.	CBE	CBE
HHS 14	<b>California's HIV and AIDS Reporting Systems</b> —Convert to a name-based HIV reporting system.	CBE	CBE
HHS 20	<b>Maximize Revenue Collections in DHS</b> —Centralize and automate revenue collection.	CBE	CBE

background checks and fingerprint clearances for individuals seeking jobs assisting vulnerable children and adults. Currently, there is no uniformity in terms of (1) which individuals must have a background check, (2) whether departments have discretion to approve workers convicted of certain crimes, (3) whether individuals can begin employment before their background checks are complete, and (4) whether departments investigate individuals with subsequent arrests. This recommendation requires the standardization of the entire background checking process throughout the various departments.

***Consolidating Licensing and Certification (HHS 21).*** The CPR recommends consolidating the licensing functions within the proposed HHSD. Currently, six departments within the existing Health and Human Services Agency are responsible for conducting their own licensing and background clearances. This consolidation would create administrative efficiencies, reduce the duplication of background checks as individuals move among different types of caregiving jobs, and would allow for a consolidated database for all background clearances and investigations. In addition, the CPR consolidates all foster care background checks at the state level rather than allowing counties to conduct their own checks (HSS 06).

***LAO Comments.*** These recommendations have a great deal of merit. The proposal is consistent with the social services trailer bill, Chapter 229, Statutes of 2004 (SB 1104, Committee on Budget), that would require the Health and Human Services Agency to look at ways of streamlining and standardizing the background checking process throughout its departments. With respect to the workload

associated with conducting more background investigations (pursuant to the proposed standardization), we believe CPR has overstated the number of necessary investigators by about 75 percent. (We base this estimate on workload ratios in the Department of Social Services [DSS].)

## **Child Care**

***Simplify the Subsidized Child Care System (HHS 04).*** The CPR recommends a number of measures to streamline child care program administration, including merging the administration of child care for California Work Opportunity and Responsibility to Kids (CalWORKs) families on cash aid, eliminating CalWORKs Stage 3 child care, and reforming the State Department of Education (SDE) child care provider contract process. Under the CPR proposal, child care for families on cash assistance would be administered by county welfare offices through DSS, with all other child care programs administered by SDE. The CPR recommends establishing a set-aside to provide two years of transitional child care to families who have left cash aid.

The CPR further recommends making waiting lists “first come, first served” for those families with incomes at or below 50 percent of the State Median Income (SMI) level. Once former CalWORKs families have been off of aid for two years (after exhausting their time in the set-aside funded program) their status on the wait lists would be evaluated based on the date they started CalWORKs, not the date they left the set-aside funded program.

***LAO Comments on Simplifying Subsidized Child Care System.*** Consolidating the administration of child care for families on cash assistance creates a more logical division of child

care administrative responsibilities. However, the CPR recommendation does not resolve the fundamental problem of divided administrative responsibility (DSS and SDE would share child care program responsibility), which contributes to programmatic and administrative complexities.

The CPR recommendation to eliminate Stage 3 is consistent with the LAO position to minimize differential treatment of former CalWORKs families and other similarly situated low-income families. Under the proposed set-aside and wait-list structure, former CalWORKs families with incomes less than 50 percent of SMI would have priority access to subsidized child care after they have been off of aid for two years. However, families leaving the set-aside funded program with incomes above 50 percent of the SMI, may, like other similarly situated families, have difficulties securing subsidized child care.

***Increase Subsidized Child Care Quality (HHS 05 and HHS 07).*** The CPR recommends

taking steps to make child care provider reimbursement commensurate with quality of care provided. It proposes to do this by reducing the maximum reimbursement rates from the 85th percentile to 50 percent of the Regional Market Rate (RMR) for unlicensed providers and making other provider rate changes. During 2005-06 and 2006-07, the CPR estimates that the rate adjustments would result in savings of \$108 million General Fund, and \$108 million in federal block grant funds. In later years, the savings would be redirected to fund provider training and to pay higher average reimbursement rates because providers are likely to obtain higher levels of certification in order to receive the higher rates. Thus, the CPR estimates no long-term savings. Additionally, the CPR recommends a number of changes to prevent payments to ineligible providers who have been convicted of certain crimes.

***LAO Comments on Child Care Quality.*** The concept of differential provider reimbursement

**Figure 11**  
**Major Social Services Recommendations**

CPR Reference	CPR Recommendation	CPR 2004-05 Fiscal Effect	CPR Five-Year Cumulative Fiscal Effect
HHS 03	<b><i>Improve Child Support Performance</i></b> —Replace county-run system with state contracts with private and public entities.	None	Savings of \$29 million General Fund \$57 million federal funds
HHS 04 HHS 05 HHS 07	<b><i>Child Care</i></b> —Simplify the system by merging child care administration for cash-aided families, creating set-aside funding for families off cash aid for two years, eliminating Stage 3, and implementing contract reform. Improve quality through differential provider reimbursement rates based on levels of health, education, and safety standards.	None	Savings of \$108 million General Fund \$108 million federal funds in 2005-06 and 2006-07 No ongoing savings
HHS 06 HHS 19 HHS 21	<b><i>Criminal Background Check and Licensing Process</i></b> —Standardize background clearance process and unify these functions within one department.	Cost of \$2.1 million General Fund \$2.1 million federal funds	Savings of \$2.4 million General Fund \$31.7 million in federal and special funds

based on different levels of health and safety standards, and education and training is consistent with previous LAO positions, most recently in our *2004-05 Analysis of the Budget Bill*. However, reducing reimbursement to 50 percent of the RMR is a substantial decrease in reimbursement rates for unlicensed providers, and could reduce the supply of child care providers.

## TRANSPORTATION

### Department of Transportation

**Transportation Funding.** The CPR presents several issues related to the Department of Transportation (Caltrans) in its chapter on infrastructure. One of these issues (INF 15) contains several recommendations, including (1) a ballot measure to protect the transfer of gasoline sales tax revenue to transportation, (2) a pilot project to test the feasibility of road user fees as a funding source, and (3) a letter to be sent from the Governor to the California Congressional delegation supporting efforts to raise the federal tax on fuel containing ethanol.

A second issue (INF 16) states that federal transportation funding falls short of the state's needs and contains two recommendations to secure more federal funding. These recommendations are to write two letters to the California Congressional delegation requesting (1) earmarked funds from Congress for high-priority transportation projects and (2) more homeland security funding for "lifeline routes" that must remain open after a disaster.

Of all of the funding-related recommendations discussed above, the CPR attaches a dollar amount—\$1.96 billion over five years—only to the effort to raise the federal tax on ethanol fuel.

**Other Transportation Issues.** The CPR's other recommendations for Caltrans include several proposals to reduce expenditures or to improve Caltrans' operations or management. Among the more significant recommendations are:

- **Implement Performance Measures for Traffic Operations (INF 04).** Implement a plan developed by Caltrans that would increase funding for traffic operations activities (including such things as the Freeway Service Patrol and freeway ramp metering lights) while setting performance measures, at a total cost of \$550 million over five years.
- **Expand High-Occupancy/Toll (HOT) Lanes (INF 05).** Create more high occupancy vehicle lanes that single occupancy vehicles can use for a fee.
- **Relinquish Routes to Local Agencies (INF 13).** Transfer ownership of 6,500 lane-miles of the state highway system to local agencies, saving the state \$432 million in maintenance costs over five years.
- **Address Poor Highway Quality (INF 20).** Identify full lifecycle costs for new projects so that (1) future maintenance costs are considered when choosing new projects and (2) adequate maintenance funding can be provided. Establish performance measures for state highway system maintenance.
- **Improve Project Management (INF 32).** Give Caltrans project managers more decision-making authority and move project delivery staff from headquarters

to the districts. Stabilize state staff by tying staffing levels to more predictable workload and contracting out for less predictable workload.

**LAO Comments.** As noted above, the CPR's only transportation funding recommendation in INF 15 and INF 16 with an associated dollar amount is the effort to raise the federal tax on fuel containing ethanol. We believe that the \$1.96 billion associated with this change over five years is an accurate estimate of the additional funds available for transportation *if* the federal government made this change in tax law. However, we question the reasonableness of attributing to CPR the fiscal effect of a statutory change in federal tax policy.

One of the CPR's funding recommendations is a ballot measure to protect the transfer of gasoline sales tax revenue to transportation. While the details of such a ballot measure are not specified, if the measure were to remove the ability of the Legislature to keep gasoline sales tax money in the General Fund under certain circumstances, the proposal could have a *negative* effect on the General Fund.

Regarding the other recommendations, we agree that there is a need for Caltrans to focus more attention on traffic operations (INF 04). However, the plan referred to by CPR that would cost \$550 million in the first five years has not yet been released to the Legislature. Therefore, the Legislature cannot determine the appropriateness of the specific recommendations in the plan or the total cost of the plan's implementation. As regards relinquishing parts of the state highway system to local agencies (INF 13), it would certainly save the state money, and it may be appropriate to do so for the types of roads discussed by CPR. However,

maintenance costs for the relinquished roads would be borne by the local agencies, potentially at the expense of other local programs unless additional revenues are raised for this purpose. Finally, we agree with the general concepts of expanding the use of HOT lanes in the state (INF 05), providing adequate maintenance funding and improving performance measures (INF 20), and improving project delivery and stabilizing state staff (INF 32). We have made similar recommendations in these areas in recent years. However, the Legislature will need further details on these CPR recommendations in order to adequately assess them.

### **California Highway Patrol**

**Traffic Enforcement in Freeway Work Zones (INF 12).** Currently, Caltrans contracts with the California Highway Patrol (CHP) to provide traffic enforcement services at various construction and maintenance areas along state freeways. These additional patrols are staffed by off-duty CHP officers, who are paid at the officers' overtime rate. Caltrans reimburses CHP about \$17 million annually for all equipment and personnel costs incurred under this program using funds from the State Highway Account.

The CPR notes two problems with the current arrangement. First, CHP has been unable at times to provide Caltrans with the requested number of traffic officers for enforcement duties due to reduced staffing levels and increased workload. Second, CPR contends that paying overtime for these services is not cost-effective.

As a solution, CPR proposes that CHP hire 78 additional full-time traffic officers and purchase supporting equipment, at a total annual cost of about \$11 million, to be available for traffic enforcement duties in freeway work

zones. In so doing, approximately \$6 million would be saved annually in overtime-related costs, since officers assigned to freeway work areas would work on a regular time basis. In addition, CPR notes that these officers would be available for other duties, such as regular patrol activities, whenever there are no construction or maintenance projects scheduled in the areas to which they are assigned.

**LAO Comments.** While this proposal merits further consideration, it is uncertain how from year to year the additional staff resources will be matched to the changing location of project sites. The CPR proposes that in the first year, Caltrans would provide CHP with a list of anticipated projects requiring enforcement patrols that year, including their location in the state and anticipated start and end dates. Based on this information, CHP would deploy the appropriate number of newly hired officers to the areas of the state requiring enforcement services that year. In subsequent years, however, CHP could be faced with the need to reallocate staff to other areas of the state based on changes in Caltrans' workload requirements. Alternatively, CHP supervisors in areas requiring new construction and maintenance work would have to pull officers from their existing assignments in order to provide the necessary enforcement coverage at freeway work sites.

### **Department of Motor Vehicles**

#### ***Biennial Vehicle Registration (GG 36).***

Currently, motorists must register their vehicles with the Department of Motor Vehicles (DMV) annually. The CPR proposes to require most owners to register their vehicles every two years. In so doing, DMV's annual vehicle registration workload would be reduced by about half,

which CPR believes would allow DMV to cut costs and reduce wait times at field offices. In addition, by implementing the proposal over a two-year period, the CPR report projects that the state would receive a one-time revenue "windfall" of about \$2.1 billion, including about \$1.3 billion in Vehicle License Fee (VLF) revenues. According to CPR, this windfall results because in the first year of the plan's implementation, one-half of the motorists in the state would pay one year's worth of fees and taxes on their vehicles, while the other half would pay two years of fees and taxes. The CPR proposes to transfer the VLF windfall monies to the General Fund, rather than distributing them to cities and counties.

**LAO Comments.** Our review suggests that the one-time VLF revenue windfall is likely to be about \$1 billion rather than \$1.3 billion. Regardless, it would appear that the proposed transfer of all VLF windfall revenues to the General Fund would require a constitutional change. This is because VLF revenues are constitutionally designated for distribution to local governments. Also, the VLF windfall that would result from the proposal's implementation could be construed as a one-time tax increase, since in the first year of the plan's implementation about \$1 billion more would be collected from state motorists than would otherwise be the case.

Since the CPR was issued, the DMV has estimated that reduced workload from the proposal would allow the department to eliminate or redirect about 225 positions. In addition, the proposal would involve significant one-time costs to DMV, potentially up to \$20 million, to convert the department's vehicle registration database and fee collection programs to a biennial system.

Figure 12

**Major Transportation Recommendations**

CPR Reference	CPR Recommendation	CPR 2004-05 Fiscal Effect	CPR Five-Year Cumulative Fiscal Effect
INF 04	<b>Traffic Operations Performance Measures</b> —Fund a Caltrans operations plan and implement performance measures.	None	Cost of \$550 million special funds
INF 05	<b>HOT Lanes</b> —Expand use of high-occupancy/toll lanes.	CBE	CBE
INF 13	<b>Relinquish Routes</b> —Transfer ownership and maintenance of some highways to locals.	None	Savings of \$432 million special funds
INF 15	<b>Increase Revenues</b> —Request higher federal ethanol tax, protect sales tax revenues for transportation, test road user fees.	None	Increased revenues of \$1.96 billion federal funds
INF 16	<b>Increase Federal Funding</b> —Request earmarks for high-priority projects, request homeland security funds for “lifeline” routes.	CBE	CBE
INF 20	<b>Improve Highway Quality</b> —Identify and fund full maintenance costs for new projects, establish road quality performance measures.	CBE	CBE
INF 32	<b>Improve Project Management</b> —Transfer authority and staff from Caltrans headquarters to districts, stabilize state staffing.	CBE	CBE
INF 12	<b>Traffic Enforcement Program in Freeway Work Zones</b> —Use on-duty CHP officers, directly funded from the State Highway Account, to provide traffic enforcement services in freeway work zones.	None	Savings of \$22.4 million special funds (\$5.6 million annually for four years)
GG 36	<b>Biennial Vehicle Registration</b> —Require most owners to register their vehicles every two years, rather than annually.	None	Increased revenues of \$1.259 billion General Fund

**RESOURCES, ENVIRONMENTAL PROTECTION, AND ENERGY****Land Acquisition and Conservation**

The CPR contains a number of recommendations related to how the state acquires and conserves land for resources-related purposes. In general, these recommendations involve consolidating processes to create efficiencies, improve consistency, and make the review process more timely. The CPR also contains policy statements about preferred tools for meeting resource conservation objectives.

**Consolidating Resource Land Acquisition Processes (RES 13).** The CPR recommends

consolidating land acquisition functions for resources-related purchases into a “Resource Conservation Board” which would have the broad authority to approve and fund all resources-related acquisitions. The CPR also recommends changing the current appraisal process to allow the appraisal review function currently done by the Department of General Services to be handled by an independent appraisal expert on behalf of the new board.

**Restructuring Land Conservancies (RES 12).**

The CPR recommends devolving five state conservancies of a “regional” nature (Baldwin Hills Conservancy, Coachella Valley Mountains Conservancy, San Diego River Conservancy,

San Gabriel and Lower Los Angeles Rivers and Mountains Conservancy, and San Joaquin River Conservancy) into local joint powers authorities and eliminating current state funding for staff support of these conservancies. The CPR also recommends that the Resources Agency (or its successor) develop a statewide master plan for land acquisition and resource protection for habitat and recreational purposes.

**Increased Use of Conservation Easements (RES 35).** The CPR recommends increasing the use of conservation easements, as opposed to land acquisitions that can involve significant development costs, to protect natural resources and improve open space.

**LAO Comments.** Overall, we find these recommendations merit serious consideration. We have previously raised concern about the multiplicity of state agencies with resource-related land acquisition functions (see, for example, *California's Land Conservation Efforts: The Role of State Conservancies* [2001]). We think that a comprehensive evaluation of California's land conservation programs could present opportunities to significantly improve the effectiveness of the state's land acquisition and resource protection efforts.

However, we also find that some of the recommendations include important trade-offs for the Legislature to consider. For example, while the proposed changes to the appraisal process may produce efficiencies, the proposal may also reduce the state's oversight and accountability of this process. Similarly, although acquiring conservation easements may be less expensive than acquiring land in title, easements may provide the state with fewer benefits when compared to outright land acquisitions, such as less public access or less resource protection. In

addition, the use of easements raises monitoring and enforcement issues. While conservation easements are already used by state agencies, a significant increase in their use would represent an important policy change for the Legislature to evaluate.

### **Forestry-Related Policy Shifts**

The CPR contains some forestry-related recommendations which contain policy changes that are appropriate for legislative evaluation before implementation.

**Changes to the Timber Harvest Plan Review Process (RES 21).** The CPR recommends a number of changes to the timber harvest plan (THP) review process. These include allowing exemptions from the THP review process for certain types of projects that are considered "low consequence" and the use of privately developed forestry standards to approve THPs.

**Separating Wildland Fire Protection From Forest Resource Management (PS 03).** The CPR recommends consolidating all roles, functions, and responsibilities for statewide fire protection and emergency management into a new division of Fire Protection and Emergency Management within the proposed Department of Public Safety and Homeland Security (DPSHS). The remaining forestry-related activities and functions would be placed in a different department, the new Department of Natural Resources.

**LAO Comments.** The proposed changes to the THP review process represent significant policy changes that are similar to the Governor's THP reform proposals of this past spring. Increasing the use of exemptions to the THP review process may promote greater efficiency and reduce state costs, but it could also increase the risk that a proposed project may have

significant impact on the state's natural resources. Approving THPs pursuant to privately developed standards may have merit in concept, depending upon the quality of the standards selected.

We find that the proposal to consolidate emergency management functions into the DPSHS lacks sufficient information regarding how it would improve wildland fire protection or reduce costs associated with wildland fires. Since an important cost driver of wildland fire protection expenditures is fuel conditions in wildlands, the separation of the Department of Forestry and Fire Protection's current fire protection functions from its forest resource management functions (which would be retained) could be problematic. The proposed restructuring of functions involves important policy decisions about the mission of the state's forestry agency and how best to achieve that mission.

### **Resources-Related Fees**

The CPR includes a handful of recommendations concerning resources-related fees. In general, these recommendations do not involve new or increased fees, but rather concern the use of or improving the collection of existing fees. One notable exception to this is found in the recommendation to consolidate siting responsibilities for energy infrastructure (discussed later). Under this recommendation, CPR recommends that applicants be charged siting and compliance fees that reflect the actual costs of processing the application. Currently, some of these costs are borne by energy utility ratepayers.

***Broaden Use of Specified Environmental Fees (RES 32).*** The CPR finds that the use of

revenues for a number of environmental fees is narrowly defined in statute, thereby constraining the ability to use these fee revenues to address other unmet, high priority environmental needs. Fees falling into this category include waste tire and used oil recycling fees. The CPR's solution to this issue is to broaden the statutorily authorized uses of various fee revenues.

***Improve Collection of Fish and Game Environmental Filing Fees (RES 34).*** The CPR recommends adjusting the current fee levels for environmental filing fees in order that they better reflect the complexity and potential impact of projects subject to the fee. The CPR also recommends providing a fiscal incentive to encourage local agencies, which are responsible for collecting the fees on behalf of the Department of Fish and Game (DFG), to increase collection efforts.

***LAO Comments.*** While there may be legitimate opportunities to broaden the authorized uses of existing environmental fees as CPR suggests, there are legal constraints that may limit the ability to do this. The legal characterization of an assessment as a fee (as opposed to a tax) is dependent on there being a sufficient "nexus" between the fee payer and the activities funded from the fee.

With regard to the collection of existing fees, we have previously identified concerns with the collection of DFG's environmental filing fees. (Please see *Improving Fish and Game's CEQA Review* [2002] and the *Analysis of the 2002-03 Budget Bill*, page B-64.) While the department has taken steps to improve the collection of these fees, we think the CPR's proposal to improve collection efforts has merit.

## Cal-EPA Administrative Functions

**Cal-EPA Administrative Consolidation (RES 07).** The CPR recommends consolidating the administrative divisions of the six constituent boards and departments in the California Environmental Protection Agency (Cal-EPA) into a single office. The administrative functions to be consolidated would include such functions as personnel management, accounting, and budgeting. The CPR projects that such consolidation will result in among the largest savings from CPR's resources-related recommendations—\$53.6 million (mainly special funds) cumulatively over a five-year period.

**LAO Comments.** Budget trailer legislation—Chapter 230, Statutes of 2004 (SB 1107, Committee on Budget and Fiscal Review)—already directs the Secretary for Environmental Protection to consolidate administrative functions common among the Cal-EPA boards and departments to the extent that doing so will achieve actual budget savings. While the savings projected by CPR appear on the high side, significant budget savings from the proposed consolidation are likely.

## Energy Infrastructure

The CPR makes a number of recommendations designed to facilitate energy-related infrastructure development in the state and to provide for increased coordination in energy policymaking and program implementation.

**Consolidation of Energy Infrastructure Siting Functions (INF 22).** The CPR recommends consolidating energy-related siting functions of the California Energy Commission and the Public Utilities Commission (including power plant siting and power transmission line siting) under one department. In addition, the

new siting authority would also be responsible for permitting oil refineries, pipelines, and marine petroleum product terminals—currently functions that are a local responsibility.

**Streamline Permitting of Petroleum Infrastructure (RES 14).** The CPR proposes that “unnecessary” regulations that may prevent the expansion or new construction of oil refineries be identified and removed. The CPR also recommends streamlining the petroleum infrastructure permitting processes by adopting air district best management practices on a statewide basis and by creating a single state entity to coordinate multi-jurisdictional permitting processes.

**Consolidation of Energy Policy Development and Energy Efficiency Program Implementation (INF 23).** The CPR recommends consolidating energy planning and policy development and the implementation of energy efficiency programs—all currently involving multiple state agencies—under one agency.

**Development of Comprehensive Transportation Fuels Strategy (INF 24).** The CPR recommends that there be a comprehensive transportation fuels strategy developed under a single entity. The CPR finds that 17 different departments have fuel strategy efforts. In addition, the CPR recommends that incentives be increased to encourage the use of alternative and emerging fuels.

**LAO Comments.** We have commented previously on issues raised by the multiplicity of state energy-related agencies. (Please see *The 2002-03 Budget: Perspectives and Issues*, page 113.) While there is likely merit to consolidating some energy-related permitting authorities, we think that any restructuring of permitting functions should follow the structure of the energy market (for example, the extent to which the market is deregulated). This is because the

energy market structure will determine the roles and responsibilities of the state's energy agencies. Since the energy market structure is currently uncertain, we think that it is premature to reorganize the state's energy functions. As regards a unified state policy for energy efficiency and developing a coordinated, comprehensive transportation fuels strategy, we believe

that both of these make sense from the standpoint of program effectiveness.

## GENERAL GOVERNMENT

### Federal Funds

**Increased Federal Funds.** Currently, each state agency pursues federal grant money for its

**Figure 13**

### Major Resources, Environmental Protection, and Energy Recommendations

CPR Reference	CPR Recommendation	CPR 2004-05 Fiscal Effect	CPR Five-Year Cumulative Fiscal Effect
RES 13	<b>Resources-Related Land Acquisition Process</b> —Consolidate land acquisition functions into new board.	CBE	CBE
RES 12	<b>Land Conservancy Governance</b> —Devolve five of current eight state conservancies into local entities.	Savings of \$1 million special and bond funds	Savings of \$9.4 million special and bond funds
RES 35	<b>Resource Conservation Methods</b> —Make greater use of conservation easements, rather than land acquisitions.	None	Savings of \$184.5 million (mostly bond funds)
RES 21	<b>Timber Harvest Plan Review</b> —Streamline review process.	CBE	CBE
PS 03	<b>Fire Protection Services</b> —Consolidate fire protection functions within proposed state emergency management entity.	CBE	CBE
RES 32	<b>Uses of Environmental Fees</b> —Broaden eligible uses of environmental fees.	CBE	CBE
RES 34	<b>Fish and Game Environmental Review Fees</b> —Clarify law and regulation to improve fee collection.	None	Savings of \$18.8 million General Fund
RES 07	<b>Administrative Functions of Cal-EPA Departments</b> —Consolidate administrative functions into single office.	Savings of \$25,000 General Fund \$480,000 special funds	Savings of \$2.9 million General Fund \$53.6 million special funds
INF 22	<b>Siting of Energy-Related Infrastructure</b> —Combine siting functions into a single agency.	CBE	CBE
RES 14	<b>Permitting of Petroleum Infrastructure</b> —Streamline permitting process and create a single state permitting authority.	CBE	CBE
INF 23	<b>Energy Policy-Setting and Energy Efficiency Programs</b> —Consolidate energy policy functions and energy efficiency programs.	CBE	CBE
INF 24	<b>Transportation Fuel Strategy</b> —Develop a comprehensive fuel strategy.	CBE	CBE

own programs. The CPR recommends that efforts to secure such monies be consolidated under the Governor's Office of Planning and Research (GG 05). The report suggests that such a consolidation would allow the state to better track the receipt of federal funds, identify opportunities to collect more funds, and pursue changes to federal formulas. The report assumes new revenues of \$1.3 billion beginning in 2005-06, increasing to \$2.6 billion by 2008-09, and totaling \$8.2 billion over the next five years.

**LAO Comments.** Most of these grants are formula-driven payments for major health and social services programs, transportation, and education. California has long advocated for increases in federal funding to recognize this state's above-average poverty rates and above-average costs associated with illegal immigration. However, it is not clear how the CPR proposal would enhance California's chances of modifying federal formulas. Without significant changes to federal law, which also could have negative fiscal implications for other states, the level of assumed revenues is unlikely to materialize.

### State Budgeting

**Biennial Budget.** The report makes several recommendations concerning the administration of state government and the budget process. The CPR recommends that the Constitution be amended to require a budget every two years, rather than the annual budget required under current law (SO 40). The CPR suggests that a biennial budget would allow state officials additional time to review and evaluate state program performance.

**Performance Goals.** In addition, the CPR recommends that the funding provided in the budget should focus on performance goals

approved by policy makers, rather than incremental changes (SO 33 to SO 37). These performance goals would be developed as part of a long-range financial planning process required of all state agencies.

**LAO Comments.** The state implemented some performance-based budgeting measures as a pilot program for several departments in the mid-1990s. While the changes required a significant investment in resources, the benefits were unclear. Establishing the specific outcomes against which to measure performance was particularly difficult. With regard to biennial budgets, it is important to recognize that roughly 70 percent of General Fund spending is in caseload-driven programs in education, health, social services, and corrections. These programs would likely require action by the Legislature on a more frequent basis than every two years. Program areas that are not caseload-driven may lend themselves more readily to a change in budget cycle.

### State Employment and Retirement

**Smaller State Workforce.** The report notes an expected wave of retirements as "baby boomers" leave state service in the next few years. As a result, CPR recommends developing (1) a workforce plan to evaluate future state needs and (2) a centralized recruitment program (SO 43 to SO 46). The report assumes more than \$3 billion in savings over five years by slowing state employment growth. For new state hiring, the report recommends greater public access to non-entry-level exam opportunities rather than the current focus on promotional testing opportunities for existing state employees.

**Employment Changes.** The CPR also discusses several ways to improve the management

and efficiency of the state employment system. These include the following:

- Purchase a statewide salary survey (and regularly update it) to develop compensation policies for use in labor negotiations (SO 48).
- Replace the automatic entitlement to annual merit pay raises with a pay-for-performance approach that includes a graduated scale of raises to acknowledge work that exceeds expectations (SO 49).
- Allow business needs and employee performance to be factored into layoff order rather than just seniority (SO 57).
- Maintain the traditional public safety criteria for determining what positions qualify for enhanced safety retirement benefits. Other risky, but nonpublic safety jobs would be compensated with pay-related provisions instead of enhanced retirement (SO 51).
- Allow lump-sum retirement bonuses and other retirement plans besides the current defined benefit program (SO 50).

**LAO Comments—Savings Overstated.** The CPR assumes several billion dollars in cumulative savings from a workforce plan resulting in slower state employment growth. The CPR assumes that the workforce plan would identify inefficiencies sufficient to prompt less hiring. To the extent that such inefficiencies are identified elsewhere in the report, the savings identified with the workforce plan are double-counted and, therefore, overstated.

Some recommendations, such as adopting a new merit salary adjustment process and layoff prioritization, would have to be negotiated with employee unions (since current contracts include provisions regarding such “terms of employment”). It is unclear at this time what concessions the administration might have to make in order to reach such agreements. Such concessions, however, could offset any savings or efficiencies achieved from the recommended actions.

### **Information Technology**

**New Information Technology (IT) Governance Structure.** Since the sunset of the Department of Information Technology in 2002, the state has been without a formal IT governance structure to oversee the state’s technology practices and operations. To address this issue, CPR recommends three entities guide and direct the state’s IT operations (SO 01 and SO 02). First, CPR recommends formally establishing a State Chief Information Officer who would be responsible for developing a statewide strategic IT plan and issuing state IT policies. In addition, CPR recommends creating a Technology Services Division (TSD) within the Office of Management and Budget. The TSD would be responsible for (1) operating most state IT systems and networks, (2) conducting all IT procurements, and (3) providing project management, research and development, and telecommunication services. Finally, the Technology Council (TC)—composed of agency secretaries, the Department of Finance, and the State Controller—would oversee and direct these state IT activities.

**IT Investment Fund.** In addition to providing statewide technology guidance, the TC would also administer an IT investment fund (SO 02).

This continuously appropriated fund would consist of all monies from all fund sources appropriated for state IT activities. This would include (1) funding for new and ongoing IT projects and (2) departments' baseline funding for support and maintenance of IT equipment and telecommunications systems. On an annual basis, the TC would decide how to distribute these funds for statewide purposes.

***New IT Systems and Technology Improvements.*** The CPR proposes implementing several new IT systems, including statewide financial and asset management systems. Some of these systems' development and maintenance costs would be funded through fees charged to the users of the system. For example, a portion of the costs for the proposed online procurement system would be covered by fees charged to vendors competing for state contracts. In addition to proposing new systems, CPR also proposes implementing a number of technology improvements aimed at lowering the state's ongoing IT costs. For example, CPR recommends combining the state's voice and Internet data systems in order to produce a savings ranging up to \$6.3 million per month (SO 15).

***LAO Comments—No Independent Oversight of State IT.*** Oversight ensures that state IT operations and projects result in (1) efficient operations and (2) improved services. Oversight also monitors IT projects and expenditures, intervenes when expenditures exceed benefits, and ensures that benefits achieved from efficient IT operations are integrated into the state budget. Typically, state oversight has been independent of the day-to-day IT operations. The CPR's IT governance structure, however, combines oversight and operations. In CPR's proposal, the entity responsible for running most of

the state IT operations would also be the entity overseeing those operations. While the report also mentions some oversight would occur at the TC level, it does not define to what extent or how this oversight would occur. In addition, since the TC is composed almost entirely of administration representatives, the independence of its oversight responsibilities is questionable.

***LAO Comments—IT Investment Fund Circumvents Legislature's Appropriations.*** One of the constitutional powers given exclusively to the Legislature is the power of appropriating funds. The annual state budget is the Legislature's primary method of authorizing expenses for particular activities. The continuous appropriation of the IT investment fund, however, would provide the administration vast discretion over the use of billions of dollars in funds appropriated for specific purposes by the Legislature.

***LAO Comments—New System Costs Underestimated and Schedules Unrealistic.*** The CPR estimates savings above \$700 million over the next five years from the implementation of new IT systems. For the majority of the systems, however, CPR does not identify the development and maintenance costs which we believe could total in the hundreds of millions of dollars. For that reason, any savings from implementing and maintaining these new systems is greatly overstated. In addition, CPR estimates that most of these systems could be implemented within the next few years. Given the state's experience in developing and maintaining IT systems, we believe CPR underestimates the number of years it will take to implement these new IT systems.

***LAO Comments—Program and Service Delivery Needs Not Considered.*** Typically, the Legislature approves the use of new systems and

technologies based on the needs of the program and its service delivery strategies. For example, Chapter 270, Statutes of 1997 (AB 1542, Ducheny), authorized the use of electronic debit cards for benefit payments in order to (1) reduce the cost of delivering benefits to individuals and (2) allow recipients the opportunity to better manage their financial affairs. In some instances, CPR, however, did not appear to consider the needs of programs. For example, CPR recommends that the state implement a wireless high-speed telecommunications network aimed at improving communication services and reducing costs (SO 17). The recommendation, however, does not identify the specific program shortcomings that this new technology would address.

## Procurement

### *Changes to Purchasing Laws and Practices.*

The CPR recommends a number of changes to the state's procurement laws and practices. The significant proposals include:

- Shifting most purchasing activities from the Department of General Services (DGS) to departments (SO 60).
- Eliminating some existing exemptions from conducting competitive procurements (SO 63).
- Reforming the vendor protest process (SO 64).
- Repealing or modifying preferences for (1) specific types of companies located in certain areas, (2) disabled veterans, and (3) small businesses (SO 65, SO 68).

- Eliminating the requirement that departments purchase from the Prison Industry Authority (SO 67).

### *Methods to Purchase Goods and Services.*

The CPR recommends a number of different procurement methods that the state can use to purchase goods and services. By using these procurement methods, CPR estimates the state would save \$2 billion over the next five years. Some of these methods have already been used by the state such as performance-based procurements (SO 71) in which the contractor receives a monetary incentive to complete the project ahead of schedule. Other recommended procurement methods, however, would be new to the state. For example, to reduce prescription drug costs, CPR recommends that the state hire a Pharmacy Benefit Manager (PBM) who would be responsible for conducting most activities to support the state's prescription drug needs (SO 70). The PBM would acquire the drugs through discounted drug programs and then deliver those drugs to various departments. In addition, CPR recommends that the state examine opportunities to utilize a federal government program that provides drug discounts to entities that provide services to specific patient populations. The CPR recommends that the state enter into a cooperative agreement with an eligible entity to purchase discounted prescription drugs for the state.

***LAO Comments—Procurement Oversight May Be Reduced.*** One of the major components of the state's current procurement program is oversight of departments' purchasing activities by DGS to ensure departments follow state law and make good purchasing decisions. The CPR's changes to the procurement program

assume the state's existing governance structure of DGS, agencies, and departments—rather than CPR's mega-department structure. As such, CPR's proposed procurement organizational structure would have agencies performing purchasing reviews. Yet, CPR also recommends that the agencies conduct procurements and award contracts for departments. Since agencies would be involved in the same procurements and contracts that they will later review, the independent perspective of these reviews could be compromised.

**LAO Comments—Procurement Savings Overstated.** The CPR's proposal to consolidate the state's drug purchases identifies an important area for further study. The CPR estimates \$2 billion in savings would be achieved by using various procurement methods, including \$94 million in General Fund savings in 2004-05. This amount is likely overstated. First, the 2004-05 budget already includes General Fund savings of \$96 million from improved procurement practices. We believe the state's ability to meet this baseline level of savings in the current year is questionable. In addition, CPR estimates almost \$1 billion in savings over the next five years by using performance-based procurements. As noted earlier, this method has been in use for several years, but its effectiveness on a statewide basis is unknown.

### **State Lottery**

**Increased Revenues From State Lottery.** Current law for the lottery prohibits banked games (those in which the state has a financial stake in the outcome) and requires that 34 percent of lottery revenues be provided to education. The CPR recommends several changes to the state lottery to increase participation and

lottery sales revenues (GG 05 and GG 06). Specifically, the report recommends that the state (1) participate in a multi-state lottery game, (2) increase the amount of money paid out in prizes by reducing the percentage allocated to education, and (3) expand the types of games offered to include banked games. The report suggests that increasing the percentage allocated to prizes would increase sales revenues and total dollars to education. The report estimates that these recommendations could result in a total of \$1.2 billion in new revenues for education over the next five years.

**LAO Comments.** It is not clear that the proposed changes would generate new revenues to education. This is because the increase in gambling may not offset the reduction in education's percentage of total revenues.

### **CRIMINAL JUSTICE**

The CPR report does not contain specific recommendations in the corrections area, rather it references the recommendations made by the Corrections Independent Review Panel (CIRP). The CIRP, headed by former Governor George Deukmejian, released 239 recommendations to improve California's correctional system. Below we discuss and comment on a number of significant recommendations made by the CIRP.

**Employee Investigations and Discipline (Chapter 3).** The CIRP found that the Department of Corrections lacks a standardized procedure for internal employee investigations and discipline. For this reason, the CIRP recommends creating a centralized employee investigations and disciplinary office. This new office would centrally record public complaints, monitor serious use-of-force incidents, conduct and oversee staff misconduct investigations, and

Figure 14

## Major General Government-Related Recommendations

CPR Reference	CPR Recommendation	CPR 2004-05 Fiscal Effect	Five-Year Cumulative Fiscal Effect
GG 05 GG 06	<b>Expand Lottery Prizes and Games</b> — Change law to increase prize payouts and types of games, including allowing participation in multistate lottery.	None	\$1.2 billion special fund revenues
GG 07	<b>Increase Federal Fund Revenues</b> — Establish special unit to focus on maximizing federal funds to the state.	None	\$8.2 billion federal fund revenues
SO 01 SO 02	<b>Information Technology (IT) Governance Structure and Investment Fund</b> —Create a new governance structure and investment fund for state IT.	Savings of \$9.4 million General Fund \$9.4 million special funds	Savings of \$145.4 million General Fund \$145.4 million special funds
Various	<b>IT Systems and Technologies</b> — Implement new IT systems and technologies to reduce costs and improve services.	Savings of \$10 million General Fund \$10 million special funds	Savings of \$396 million General Fund \$316 million special funds
SO 33 to SO 37, SO 40	<b>Changes to State Administrative Practices</b> —Make various changes to state administrative practices including implementing a biennial budget, performance-based management and budgeting, and strategic planning.	CBE	CBE
SO 43 to SO 46	<b>Prepare for Upcoming Retirements</b> — Develop a workforce plan for future state needs and a centralized recruitment program.	Savings of \$115 million General Fund \$120 million special funds	Savings of \$1.6 billion General Fund \$1.6 billion special funds
SO 47 to SO 49, SO 52	<b>Position and Pay Management</b> — Develop employee performance standards and replace automatic merit pay raises with a performance-based approach.	Savings of \$0.8 million General Fund \$0.8 million special funds	Savings of \$21 million General Fund \$21 million special funds
SO 60, SO 64 to SO 68	<b>Modify Procurement Laws and Practices</b> —Modify current law and practices to increase competition and create state efficiencies.	Savings of \$3.8 million General Fund \$3.8 million special funds	Savings of \$98 million General Fund \$92 million special funds
Various	<b>Procurement Methods</b> —Adopt procurement methods to reduce costs in purchased goods and services.	Savings of \$94 million General Fund \$94 million special funds	Savings of \$1.2 billion General Fund \$1.2 billion special funds

represent the department during the appeal process. While the panel does not provide a fiscal estimate for this recommendation, it believes that these changes would result in savings by lessening the potential for employees to appeal discipline cases and pursue civil litigation.

**Inmate/Parolee Population Management (Chapter 7).** The CIRP found that about half of the prison inmates released into the community return to prison for parole violations and/or new crimes thereby driving up the cost of the prison system. As a result, the CIRP recommends a variety of measures to address these issues,

including improving and expanding in-prison and on-parole programs to reduce recidivism, early release of elderly inmates, and early discharge of low-risk parolees. Further, the panel recommends establishing “presumptive sentencing” which would set minimum and maximum release dates for inmates. Under this proposal, inmates could not be released before their maximum release date unless they exhibit good behavior and complete programs mandated by the state. The panel estimates savings of \$96 million within the next three years, including approximately \$3 million from early release of elderly inmates and \$93 million from early discharge of low-risk parolees.

***Ward/Parolee Population Management (Chapter 8).*** The panel found the California Youth Authority’s education and treatment services to be inadequate. Also, the panel identified changes to parole services that it believes would improve public safety and program effectiveness.

Some of the panel’s recommendations for improving ward education include a “school first policy” to reduce student absenteeism, an improved teacher-to-student ratio for all levels of wards, and financial incentives to recruit more dual-credentialed teachers. The panel recommends improving counseling and mental health services through a variety of changes including, ensuring treatment services conform to national standards, providing appropriate assessment, and placement and programming for wards identified as suicide risks. Finally, the panel recommends changes to parole services including, allowing counties the option to supervise nonviolent parolees, increasing the sliding fee scale to reflect actual costs of incarcerating wards, and redirecting parole resources to

increase the number of specialized parole agents who supervise sex offenders and mentally ill wards on parole. The panel estimates savings of \$4.5 million from the parole recommendations and costs of \$6.8 million from implementing the education recommendations.

***Deactivation of Inmate Beds and Youth Authority Facility Closures (Chapter 9).*** As the prison inmate population falls—due to programs currently being implemented—the IRP recommends the deactivation of certain types of beds. These include triple bunks, two inmates in a one-inmate cell, and beds in gyms and dayrooms. The panel estimates savings of \$45 million between fiscal years 2005-06 and 2008-09 from deactivating such beds. The savings result from eliminating a total of 639 correctional officer positions at prisons.

The panel found that the California Youth Authority facilities are presently a poor fit for some of the wards currently occupying some of the facilities. The Youth Authority is housing a high percentage of violent offenders and youths who need mental health care, drug treatment, and other specialized services. As a result, the panel recommends that two currently closed facilities (a youth facility in Stockton and a women’s adult correctional facility in Stockton) be reopened and that the Youth Authority relocate certain wards to these facilities. In turn, this would allow the Youth Authority to close two youth facilities.

The panel recommends providing judges with the option of imposing “blended sentences”—both juvenile and suspended adult sanctions. The panel also recommends adjusting the age jurisdiction of the Youth Authority down from age 25 to age 21. According to the panel, these changes, along with the facility closures,

would reduce the living unit size and the staff-to-ward ratio to nationally recognized standards. The panel estimates net savings from the youth facility closures of \$6 million in 2005-06 and ongoing net savings of \$12 million in each subsequent fiscal year. We would note that the CIRP, in its assessment of facility closures, does not appear to use the same criteria that the department uses in determining facility closures. As a result, the CIRP recommends closing facilities that the department has not identified in its closure plan.

**Correctional Health Care (Chapter 6).** The CIRP cites recent lawsuits and audit reports that conclude the Department of Corrections is not providing adequate inmate health care and has not adequately controlled costs. As a result, the CIRP recommends that the department transition from the current administration of health care by correction employees to a new system that would be administered largely through contracting with private health care providers. Other significant recommendations include

establishing a health care advisory group that would provide objective data and policy direction, transferring responsibility for mental health care of all seriously mentally ill inmates and wards to the Department of Mental Health, and exploring an interagency agreement with the University of California to advise and consult on a long-term solution for correctional health care. The panel does not score specific costs or savings for the above recommendations.

**LAO Comments.** Overall, the CIRP has identified significant issues facing California’s correctional system and its recommendations merit further consideration. For example, its recommendations to centralize a currently fragmented employee investigation and discipline system and to establish improved ward-to-teacher ratios have merit. However, it is difficult to fully analyze some of the significant recommendations because they lack sufficient detail. For example, the panel recommends transitioning the correctional health care system from one that is primarily administered by

**Figure 15**  
**Major Criminal Justice Recommendations**

CIRP Reference	CIRP Recommendation	CIRP 2004-05 Fiscal Effect	CIRP Five-Year Cumulative Fiscal Effect
Chapter 3	<b>Employee Investigations and Discipline Process</b> —Consolidate and centralize the employee investigations and disciplinary process.	Undetermined savings	Undetermined savings
Chapter 7	<b>Inmate/Parolee Population Management</b> —Reduce inmate and parolee population through the implementation of various new and expanded programs.	Savings of \$10 million General Fund	Savings of \$96 million General Fund
Chapter 9	<b>Inmate/Ward Closures</b> —Deactivate various types of inmate beds, close two youth facilities, and open two closed facilities.	None	Savings of \$87 million General Fund
Chapter 8	<b>Ward/Parolee Population Management</b> —Reduce student absenteeism, improve teacher ratios, conform treatment services to national standards, and redirect parole services.	None	Cost of \$2.3 million General Fund
Chapter 6	<b>Correctional Health Care</b> —Transition to administration of health care by contracted health care providers.	Savings not yet determined	Savings not yet determined

correctional employees to one that is primarily administered by private contractors. However, the report provides limited rationale as to why the state should make this wholesale change and provides no specific costs and benefits for this recommendation.

Finally, we would note that the IRP's estimated savings may be overstated for various recommendations. For example, the panel recommends several parole reforms whose savings might overlap with savings already anticipated for parole reforms implemented in 2003-04 and 2004-05. Further, the panel attributes savings to the deactivation of various types of prison beds but does not identify state policy changes that would reduce inmate population that would allow the realization of these savings.

## CAPITAL OUTLAY

***Consolidate Infrastructure Planning, Development, and Management.*** The report recommends the consolidation of state infrastructure functions in order to better coordinate infrastructure planning and programming, and achieve better utilization of its capital assets (INF 18 and INF 19). This proposal would create an Infrastructure Department that would perform the planning, programming, evaluation, and financing of infrastructure needs in six operating divisions: (1) Water; (2) Energy; (3) Transportation; (4) Housing, Buildings, and Construction; (5) Telecommunications; and (6) Boating and Waterways. According to CPR, by consolidating all capital outlay and infrastructure functions, the state could develop an integrated infrastructure policy, streamline and standardize administrative procedures, and coordinate the need for capital projects.

The proposal also calls for the creation of an

Infrastructure Authority, a public corporation chaired by the Governor's Secretary for Infrastructure which would serve as the board of directors for the Infrastructure Department. The CPR proposes that the authority be financially independent from the state budget and fee-based. The authority would be established outside of the civil service system, and would be responsible for overseeing infrastructure planning, capital budgeting, fiscal controls, asset management, acquisitions, construction, maintenance, and property sales. In addition, CPR proposes that this entity be authorized to issue tax-exempt bonds, secure private financing, and enter into contracts without approval from control agencies such as the State Personnel Board and the Department of General Services (DGS).

***LAO Comments.*** Our office has long advocated for better infrastructure planning, management, and oversight. However, as stated in Section 2 of this report, while some aspects of state government organization can be improved through reorganization, this particular proposal lacks sufficient detail to evaluate whether a proposed consolidation would improve the state's efforts in this program area.

We believe that establishing a financially independent public corporation that can issue tax-exempt financing (using the state's credit), secure private financing, and is free to enter contracts without executive or legislative branch review raises significant fiscal, policy, and oversight issues. In addition, the CPR does not elaborate on how the authority would be funded, nor does it indicate who would pay the fees.

The CPR proposal would consolidate the responsibilities of the California Transportation Commission, Energy Commission, Public Utilities Commission, and the Bay-Delta Authority in

the Infrastructure Department. Currently, these entities have established procedures for public participation in their decision-making process. It is not clear how this participation will be incorporated in the consolidation proposal.

**Surplus Property Sales.** The state currently owns property that is no longer needed for state programs. Historically, it has taken several years from when a property is identified as surplus and when it is actually sold. The CPR recommends the process of disposing of surplus real property be modified and streamlined to generate additional state revenue (INF 11). Major changes to the current process would include requiring all surplus property be sold at fair market value, eliminating the “right of first refusal” to nonstate entities, and authorizing the State and Consumer Services Agency, or its successor, to declare state properties surplus and direct their sale. The CPR estimates that surplus sales could result in revenue of \$379 million over the next five years.

**LAO Comments.** The proposal to accelerate the sale of surplus state property was proposed in Executive Order S-10-04, issued on May 11, 2004. Subsequently, Chapter 227, Statutes of 2004 (SB 1102, Committee on Budget and Fiscal Review), a budget trailer bill, accelerated the identification and sale of surplus property on a one-year basis. We note that the CPR recommendations would significantly weaken the Legislature’s involvement in the determination of which properties are declared surplus and sold. Currently, the administration must first obtain legislative concurrence and approval to dispose of surplus property. The CPR recommendation would eliminate this requirement.

The 2004-05 Budget Act assumed that by augmenting the DGS budget by \$2.8 million,

the department would generate an additional \$50 million in surplus property sales revenue. (The CPR used this assumption to generate its fiscal estimate.) Thus, CPR’s 2004-05 estimate double counts revenues currently accounted for in the state budget. With regard to the five-year estimate, we note that it is heavily dependent on the specific properties identified as surplus and how quickly they are sold. Moreover, revenues generated from properties purchased with special fund dollars would return to those special funds. This may cause the General Fund fiscal effect to be overstated.

**Delegate Property Management and Real Estate Services.** The DGS currently provides various real estate services, such as leasing, facility management, and construction, to other state agencies. According to CPR, these real estate-related processes are costly when compared to the private sector (INF 30). The CPR believes that by delegating the ability to contract for property management and construction services (from preapproved service providers) to individual agencies, the state will realize savings. The CPR estimates a five-year cumulative savings of around \$819 million from this change.

**LAO Comments.** The recommendation to delegate real estate services to individual departments conflicts with the larger CPR recommendation to consolidate and integrate all infrastructure and capital outlay functions, including real estate services, in the Department of Infrastructure.

We note that CPR’s savings estimate assumes that most departments will contract for property management and real estate services from the private sector. However, the CPR proposal does not provide sufficient detail to assess the magnitude of the estimated savings.

**Reduce the State’s Leasing Costs.** The CPR states that DGS currently leases about 20 million square feet of office and warehouse space. According to CPR, the current system of leasing from private owners is burdensome and costly. The CPR believes that by increasing the use of telecommuting, renegotiating current leases, eliminating redundant site inspection and plan check requirements, and by using state financing for state tenant improvements, the state can significantly reduce its leasing costs (INF 10). The CPR estimates that state could save approximately \$128 million over a five-year period by implementing its recommended changes.

**LAO Comments.** Control Section 5.50 of the 2003-04 Budget Act required DGS, in part, to renegotiate leases for office and warehouse space. Because of the renegotiations with various property owners, state leasing costs were reduced by approximately \$15 million annually. As such, DGS has already reduced leasing costs by \$75 million over a five-year period. Consequently, we question the likelihood of achieving an additional \$128 million in savings over the next five years.

## TAX ADMINISTRATION AND REVENUE

### Tax Policy

**Tax Relief on Manufacturing Equipment (GG 17).** The CPR proposes the institution of a substantial new sales and use tax (SUT) incentive for the purchase of manufacturing and telecommunications equipment. Although California previously had an income tax-based manufacturing incentive program that recently sunsetted, this new program would be structured as a sales tax credit as opposed to an income tax credit. Under the proposal, the incentive program would provide a tax credit equal to the General Fund portion of the SUT (currently equivalent to a 5 percent rate) paid on eligible equipment. Businesses qualifying for the program could use the credit against their sales taxes after 12 months have elapsed from the date of the equipment purchase. The proposal calls for the credit program to begin in 2006 and be in effect through 2015. Based on a study prepared for the California Manufacturers and Technology Association, the CPR states that tax revenues from added personal income tax (PIT)

**Figure 16**  
**Major Capital Outlay Recommendations**

CPR Reference	CPR Recommendation	CPR 2004-05 Fiscal Effect	CPR Five-Year Cumulative Fiscal Effect
INF 18, INF 19	<b>State Infrastructure</b> —Consolidate functions in order to better coordinate infrastructure planning, programming, and asset management.	None	Savings of \$2.3 million special and federal funds
INF 11	<b>Surplus Property</b> —Accelerate surplus property sales.	Revenue of \$47.2 million General Fund	Revenue of \$379 million General Fund
INF 30	<b>Real Estate Services</b> —Delegate property management and real estate services to individual departments.	None	Savings of \$409.5 million General Fund \$409.5 million other funds
INF 10	<b>Facility Leasing</b> —Reduce costs by increased telecommuting, renegotiating facility leases, and modifying leasing process.	Savings of \$7.1 million General Fund \$7.1 million other funds	Savings of \$64.1 million General Fund \$64.1 million other funds

and corporate tax generated by the program would more than offset SUT losses in all ten years of the program, with net revenues of approximately \$80 million in 2008-09.

**LAO Comments.** The CPR proposal is intended to act as an incentive for business investment in manufacturing and telecommunications equipment. The structure of the tax incentive would benefit these industries and specifically allow start-up firms and firms with no tax liability to benefit. However, as we indicated in our October 2003 report, *An Overview of California's Manufacturers' Investment Credit*, the broad findings of research in the area of tax incentives suggests that although state-level investment tax credits may affect decisions of individual firms "on the margin," they have little impact in the aggregate on business investment decisions relative to other factors. As a result, incentive programs of the type proposed in the CPR are likely to be expensive (in terms of foregone revenues) relative to the benefits they bestow in the form of additional investment activity in the state. For example, DOF has estimated that additional activity generated by the manufacturers' investment credit (MIC)—which was in place in California from 1994 until it sunsetted in 2003—resulted in partially offsetting revenue gains of about one-third the size of the gross revenue losses. Thus, a gross revenue loss of \$100 million would be partially offset by a revenue gain of about \$30 million, for a net revenue loss of \$70 million.

**Revise the Homeowners' and Renters' Assistance Program (GG 35).** The CPR proposes to reduce costs associated with the Homeowners' and Renters' Assistance Program (HRAP), by eliminating the tax relief portion for homeowners.

**LAO Comments.** As noted in the report, given that homeowners have received substantial property tax relief since the HRAP was started due to the passage of Proposition 13, this proposal is worth consideration by the Legislature. Program reductions in this area were presented to the Legislature as an LAO option in the 2004-05 *Budget: Perspectives and Issues* (page 235).

### Tax Administration

The CPR proposes several changes in the area of tax administration, compliance, and enforcement.

**The California Tax Commission (Volume 2, Chapter 11).** The CPR report indicates that California's tax system is duplicative, inefficient, and confusing due largely to the split of tax administration among the Franchise Tax Board (FTB), Board of Equalization (BOE), and Employment Development Department (EDD). The CPR proposes that some of the state's principal tax collections agencies, together with certain components of DMV, be consolidated into a new California Tax Commission (CTC). The report indicates that the BOE would be retained as an independent entity, and its board members would serve as ex-officio board members of the CTC.

**LAO Comments.** The notion of a consolidated tax agency for California is not a new one. Dating as far back as 1945, our office has in fact recommended the formation of just such an entity. In 1993-94, we indicated that the administration's proposal for a Department of Revenue—involving consolidating activities of FTB and BOE—represented an appropriate administrative policy that could result in improved services and long-run savings. We continue to think that a consolidated depart-

ment for all major taxes could result in improved services, coordination, and accountability. In particular, the largest benefits of such consolidation could occur in the coordination of tax enforcement and compliance. Short-term costs, however, are quite likely due to the need to maintain existing systems while establishing new ones. The CPR recommendation would address only some of these issues. It is not clear as to the authority of the CTC board with respect to the various taxes, or how the proposed CTC board relates to the existing constitutional authority of the BOE board. In addition, it does not appear that the proposal includes the BOE's administrative structure within the CTC. As a result, the state's major taxes would still be administered by separate entities.

**Raise State Revenue Through Tax Amnesty (GG 01).** The CPR includes a proposal to establish a comprehensive statewide amnesty program for the PIT, SUT, and vehicle license and registration fees.

**LAO Comments.** The Legislature has already enacted a tax amnesty program that covers the PIT and the SUT. The program will take place during February and March of 2005, and result in increased revenues in 2004-05 of \$333 million. Thus, most of the revenues that would be generated by the CPR proposal have already been incorporated in the budget. It is important to note that tax amnesties generate most of their benefits through the acceleration of revenues rather than generating additional new revenues.

**More Tax Collection and Audit Staff Will Generate Additional Tax Revenue (GG 02).** The CPR proposes to increase audit and collections staff at FTB, BOE, and EDD. According to the report, lowering the existing benefit/cost ratio used by the tax agencies would generate addi-

tional General Fund revenues of over \$150 million over five years.

**LAO Comments.** Before considering an augmentation in the areas of tax auditing and collections, the Legislature should be convinced of the likelihood that such additional revenues will actually be received. For example, the report proposes that FTB receive additional resources to fund collection activity down to the 3:1 benefit-cost level, for additional annual net revenues of \$12 million. However, it is our understanding that FTB is already working at the 3:1 level using existing resources. Likewise, with respect to the BOE and EDD proposals, the Legislature should determine that estimated revenues are based on "cash in the door," and do not merely reflect proposed tax assessments that may or may not result in additional revenues. Finally, to the extent these revenue generating activities increase auditing and collection activities, the Legislature should systematically weigh the potential adverse impact on compliant taxpayers of this additional administrative presence.

**Consolidate and Upgrade Cashiering for State Taxing Agencies (GG 03).** The report indicates that savings of about \$35 million over a five-year period could be achieved in mail and cashiering activities of the tax agencies through upgrades and consolidation.

**LAO Comments.** The CPR recommendations appear reasonable and are in keeping with similar recommendations over the recent past. However, it is not apparent how this partial consolidation relates to the CPR recommendation regarding the formation of a new tax commission that would result in the full consolidation of certain tax agencies (see above). Pursuant to Chapter 569, Statutes of 2003 (AB 986, Horton), our office will be reporting to the Legislature later this year regarding the possible

consolidation of the remittance, cashiering, and mail processing functions of FTB, BOE, and EDD.

**Centralize for Efficiency the Assessment of Commercial Aircraft (GG 19).** The CPR indicates that the property tax assessment of commercial aircraft fleets by county assessors results in inconsistent tax treatment and the duplication of administrative functions. It proposes that the assessment of such fleets be centralized and carried out by the BOE at a five-year cost of about \$2 million with unknown revenue impact.

**LAO Comment.** While the proposal could result in elimination of duplication and inconsis-

tencies in assessment activities, the same could be said regarding the assessment of certain other types of personal property. Given this, the Legislature may want to consider the proposal in a broader policy context that takes into account all of the types of industries or personal property that may be suited for a centralized assessment approach. It also may wish to assess the potential adverse impact of the proposal in terms of the resulting reduction of local expertise and input in the assessment process.

**Figure 17**

**Tax Administration and Revenue**

CPR Reference	CPR Recommendation	CPR 2004-05 Fiscal Effect	CPR Five-Year Cumulative Fiscal Effect
Volume 2, Chapter 11	<b>California Tax Commission</b> —Consolidate tax agencies' activities within a new commission.	CBE	CBE
GG01	<b>Tax Amnesty</b> —Implement broad tax amnesty for major revenue sources.	Revenues of \$229 million General Fund \$15 million special and local funds	Revenues of \$383 million General Fund \$16 million special and local funds
GG02	<b>Audit and Collections</b> —Increase auditing and collection resources for FTB, BOE, and EDD.	None	Revenues of \$155 million General Fund \$36 million special and local funds
GG03	<b>Cashiering Functions</b> —Consolidate and upgrade mail, cashiering, and remittance processing functions of tax agencies.	None	Savings of \$21 million General Fund \$14 million special and local funds
GG17	<b>Manufacturing Tax Credit</b> —Provide sales tax credit for the purchase of manufacturing and telecommunications equipment.	None	Revenues of \$343 million General Fund
GG19	<b>Property Tax Assessment</b> —Centralize assessment of commercial aircraft.	CBE	Costs of \$2.2 million General Fund
GG35	<b>Homeowners' and Renters' Assistance Programs</b> —Institute various program revisions and reductions.	None	Savings of \$91 million General Fund

## CONCLUSION

The CPR offers the state an opportunity to reexamine the functions and operations of state government. As discussed in the preceding pages, careful consideration requires an exami-

nation of the problem being addressed and whether the proposed solution effectively addresses it and results in improved service.

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