

2001-02 Analysis

MAJOR ISSUES

General Government



Legislature Needs Information on the Gambling Commission and the Status of Indian Gambling

- A primary role of the commission is to ensure that the terms of tribal-state compacts for gambling are followed. The commission needs to clarify its role and responsibilities as well as the division of responsibilities between the commission and the Department of Justice.
- Currently, there are 61 tribal-state compacts. The commission needs to report on the current status and potential growth of gambling activity on Indian land and the commission's procedures for oversight of Indian gambling (see page F-43).



Serious Management and Operations Problems at Barstow Veterans' Home

- Ongoing management and operations problems at the Barstow Veterans' Home resulted in the loss of the home's Medi-Cal and Medicare certification along with its federal per-diem payments. In an attempt to regain certification, the Department of Veterans Affairs has contracted with a private firm to run the 180-bed skilled nursing facility at the home and prepare it for recertification by June 30, 2001.
- We recommend the Legislature not approve funding for the home until such time as the department reports to the Legislature on the progress and timetable for obtaining recertification of the facility (see page F-182).



Energy-Related Proposals

- The Governor's budget proposes a number of augmentations totaling \$1.2 billion (\$1.1 billion General Fund) related

to the state's energy crisis. In addition, the Legislature in special session has approved several bills related to the state's electricity crisis.

- We have withheld recommendation on most of the Governor's proposals pending receipt and review of information justifying the proposed expenditures (see page F-13).



Data Center Consolidation Study Out-of-Date

- The Department of Information Technology's 1997 Data Center Consolidation Study is out-of-date for a number of reasons. We recommend that the Legislature direct the Department of Information Technology to report on resources needed to conduct a study which examines the data center rates, considers opportunities to specialize data centers, and identifies functions that could be performed more efficiently by private industry (see page F-130).



Touch Screen Voting Pilot Program Lacks Justification

- The budget proposes a \$40 million pilot program to test touch screen voting equipment in three counties. The proposal fails to justify the need for additional pilot testing since touch screen voting has already been pilot tested and certified in California (see page F-40).



Evaluations of Completed Information Technology Projects Are Deficient

- The state's post-implementation evaluation reporting (PIER) process has a number of deficiencies. The PIER results are not being shared with the Legislature, control agencies do not keep records on completed projects, and departmental reviews lack independence.
- We recommend that the Legislature require departments to report at budget hearings on completed projects, adopt budget control language requiring timely reporting on PIER results, and enact legislation requiring the administration to provide PIER information (see page F-34).

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OVERVIEW

General Government

T*otal funding for general government is proposed to increase by 3 percent in the budget year. The budget does not include funds for increases in employee compensations that may result from collective bargaining for new memoranda of understanding or for increases in the state's contributions to employee retirement programs.*

The "General Government" section of the budget contains a variety of programs and departments with a wide range of responsibilities and functions. These programs and departments provide financial assistance to local governments, protect consumers, promote business development, provide services to state agencies, ensure fair employment practices, and collect revenue to fund state operations. The 2001-02 Governor's Budget proposes \$13.5 billion to fund these functions not including federal funds. The proposed budget-year funding is \$418 million more than estimated 2000-01 expenditures.

SPENDING BY MAJOR PROGRAM

There are six major program areas within general government:

- Local government subventions, which includes shared revenues and local government financing.
- Tax relief.
- Regulatory programs.
- Tax collection programs.
- State administrative functions.
- State retirement and employment.

We describe these program areas below and Figure 1 shows the estimated 2000-01 and proposed 2001-02 budget expenditures by program area. The large increase in local government subventions and the large decrease in tax relief are related to the implementation of additional vehicle license fee (VLF) relief enacted last year.

Figure 1

General Government Spending By Program Area

2000-01 Through 2001-02
(In Millions)

Agency/Program	Estimated 2000-01	Proposed 2001-02	Difference
Local government subventions	\$3,134	\$5,500	\$2,366
Tax relief	4,694	3,108	-1,586
Regulatory	1,497	1,388	-109
Tax collection	614	618	4
State administration	1,643	1,467	-176
Retirement	1,531	1,450	-81
Totals	\$13,113	\$13,531	\$418

Local Government Subventions

The largest general government program is the local government subvention program, proposed to total \$5.5 billion in 2001-02. This program: (1) distributes state-collected revenue (primarily from VLFs and gas taxes) to local government agencies and (2) provides local governments additional funding for specified programs.

The Governor's budget proposes to subvene \$4.8 billion in shared revenues (virtually all from special funds). This compares to the current-year total of \$2.4 billion, which was significantly reduced in 2000-01 due to the way additional VLF relief was enacted last year. Another \$673 million in local assistance (all General Fund) is proposed for local government general purpose relief (\$250 million), the Citizen's Option for Public Safety program (\$242 million), and other local government programs.

Tax Relief

The state provides local tax relief—both as subventions to local governments and as direct payments to eligible taxpayers—through a num-

ber of different programs. The Governor's budget proposes more than \$3.1 billion for tax relief appropriations in 2001-02. The two largest are the VLF reduction and the Homeowners' Property Tax Relief (homeowners' exemption) programs. The Governor's budget shows a reduction of \$1.6 billion from 2000-01 due to (1) the way additional VLF relief was enacted last year and (2) a one-time increase in senior citizen property tax relief in the current year.

Regulatory Activities

A total of 22 departments are responsible for providing regulatory oversight of various consumer and business issues. These regulatory agencies protect the consumer and promote business development while regulating various aspects of licensee, business, and employment practices. The groups regulated range from individual licensees to large corporations. Most of these departments are funded from special funds that receive revenue from those subject to regulation. Included in this total are the Departments of Consumer Affairs, Industrial Relations, Food and Agriculture, Financial Institutions, and Corporations, as well as the Public Utilities Commission.

The total proposed expenditures for all regulatory activities in the budget year are \$1.4 billion. This includes approximately \$1.1 billion from special funds and \$328 million from the General Fund. Total expenditures in this category are \$109 million, or over 7 percent, below estimated current-year expenditures. The four largest agencies in terms of overall proposed expenditures are the Department of Consumer Affairs, \$343 million (\$2.8 million General Fund); the Department of Industrial Relations, \$227 million (\$175 million General Fund); the Energy Commission, \$195 million (\$17 million General Fund); and the Department of Food and Agriculture, \$179 million (\$98 million General Fund).

Tax Collection Programs

Expenditures. The Franchise Tax Board and the Board of Equalization are the largest revenue collection agencies in the state. Between them, the boards collect the state's personal and business income taxes, sales tax, and special use taxes. The budget proposes \$618 million for these tax programs in 2001-02, an increase of \$4 million, or 0.7 percent, over estimated current-year expenditures.

Revenues. The Governor's budget estimates that combined General Fund collections by both boards will be \$77 billion in 2001-02. More than half of all General Fund revenues (\$44.8 billion) come from personal income taxes.

State Administrative Functions

There are more than 30 departments and agencies that provide a wide range of administrative services. These services range from oversight and support of other departments (Department of General Services, Department of Information Technology, and Office of Administrative Law), to economic development (Technology, Trade and Commerce Agency), to various specialized services provided to individuals and communities (Office of Emergency Services, the Military Department, and the Department of Veterans Affairs).

The budget proposes a total of \$1.5 billion to support these functions in 2001-02. This is a decrease of \$175 million, or 11 percent, from current-year expenditures. The decrease is primarily due to a reduction in one-time appropriations for local assistance under the Department of Housing and Community Development.

State Retirement Programs

Retirement-related expenditures account for a significant part of state spending for the budget year. In 2001-02, state expenditures for various costs associated with public employee retirement (excluding University of California costs) will total \$2.3 billion, including \$1.9 billion from the General Fund. As summarized in Figure 2, the General Fund provides for employer contributions and/or various other payments to four retirement systems. In addition, the state (1) contributes to the payment of premiums for health and dental benefit plans for retired state employees and (2) makes Social Security and Medicare contributions for most state employees.

Public Employees' Retirement System. The Public Employees' Retirement System (PERS) is the retirement system for most state employees. The budget projects General Fund expenditures of \$78 million for PERS in 2001-02. However, we believe this amount is understated because the state's costs will more than likely increase in 2001-02 because of enhanced retirement benefits for all state employees that became effective January 1, 2000. Under the legislation that enhanced the benefits—Chapter 555, Statutes of 1999 (SB 400, Ortiz)—PERS was required to modify certain actuarial valuation methods in order to recognize excess assets more quickly. As a result, the state's costs for the new benefits were partially offset, and the budget year is the first year that PERS fully recognizes the increased liability in setting the state employer contribution rates. Based on the estimated state employee salary level, we estimate that each percentage point increase in the state's overall contribution rate increases General Fund retirement costs approximately \$55 million.

State Teachers' Retirement System. The State Teachers' Retirement System (STRS) is the retirement system for teachers in public K-12 schools

and community colleges. The STRS receives contributions from teachers and their employers. However, these contributions have historically been insufficient to provide for the cost of basic retirement benefits (which were enhanced by 1998 and 2000 legislation), the protection of retirees' purchasing power, and past unfunded liabilities (the system no longer has an unfunded liability). These shortfalls have been covered by annual transfers from the General Fund. In the budget year, the shortfalls are expected to total \$874 million—about \$29 million less than the current year. This decrease results from a reduction in the state's annual percentage contribution to STRS, as changed by 2000 legislation, offset by increased contributions due to statewide teacher salary increases and purchasing power protection.

Figure 2	
General Fund Costs For Retirement Programs^a	
2001-02 (In Millions)	
State Retirement Plans	
State Teachers' Retirement	\$874
Public Employees' Retirement	78
Judges' Retirement	77
Defined Contribution Plans ^b	47
Legislators' Retirement	—
Subtotal	(\$1,077)
Other Retirement Benefits	
Health and Dental Benefits for Annuitants	\$431
Social Security and Medicare ^c	353
Subtotal	(\$784)
Total	\$1,861
^a Excludes costs for University of California employees. ^b Programs for Bargaining Unit 6 and excluded employees. ^c Legislative Analyst's Office estimate based on 1999-00 costs.	

Health and Dental Premiums. The budget also includes \$431 million from the General Fund to pay the state share of health and dental insurance premiums for retired state employees and their qualifying beneficiaries. This is \$21 million more than estimated current-year expenditures, reflecting an increase in the number of retirees. The PERS is currently negotiating the health premiums rates for the second half of the budget

year. These negotiations may result in a change in the estimated General Fund cost for the budget year.

Employee Compensation

There are nearly 176,000 rank-and-file state employees (not including those in higher education) covered under state collective bargaining law. The pay, benefits, and working conditions for these employees are typically spelled out in memoranda of understanding (MOUs). In September 1999, the Legislature approved MOUs for all of the state's 21 collective bargaining units that are effective through June 30, 2001. Major compensation provisions in these MOUs included 4 percent salary increases effective on July 1, 1999 and September 1, 2000, and increased retirement benefits (provided in Chapter 555).

The Governor's budget does not include any budget-year funding for employee compensation. However, the Department of Personnel Administration will begin collective bargaining negotiations to replace the expiring MOUs this spring. Consequently, we anticipate the state will face some increases in employee compensation costs in 2001-02. Based on the estimated state employee salary level, we estimate that each 1 percent salary increase for state employees increases General Fund costs approximately \$55 million.

CROSSCUTTING ISSUES

General Government

ENERGY-RELATED PROPOSALS

The Governor's budget proposes a number of augmentations totaling \$1.2 billion (\$1.1 billion General Fund) related to the state's energy crisis (see Figure 1, next page). These proposals would add nearly 100 positions across six departments. These proposals are summarized below.

Set-Aside \$1 Billion for Energy Initiatives. The largest share of proposed expenditures is for a \$1 billion General Fund set-aside for energy initiatives to address the energy crisis. Proposed budget bill language specifies that (1) the funds are for "projects awarded by the Governor's Clean Energy Green Team" and (2) allocation of the amount appropriated will be subject to legislation. No further information is available on this set-aside at this time.

Rising Department Energy Costs. The budget also proposes \$50 million (\$25 million General Fund) for the increased costs departments will face due to higher natural gas and electricity costs.

Indirect Emission Offsets for New Power Plants. Both the Air Resources Board (ARB) and Department of Transportation (Caltrans) propose emission offset programs that are at least partly designed to support efforts to build new power plants. The \$100 million General Fund ARB proposal would establish a grant program to replace or retrofit older diesel engines to provide emission offset credits for proposed "peaker" power plants that would operate during times when electricity demand is high, such as the summer months. The \$20.3 million Caltrans proposal would upgrade its car fleet by retrofitting diesel engines and replacing

Figure 1**Energy-Related Budget Proposals
2001-02 Governor's Budget***(Dollars in Thousands)*

Proposal	Amount		
	General Fund	Special Funds	Positions
Energy Initiatives (Item 3365)			
Set-aside for energy projects	\$1,000,000	—	—
Air Resources Board (Item 3900)			
Diesel engine grant program to offset new power plant emissions	100,000	—	4
Utilities Costs (Item 9911)			
For increased state department costs for natural gas and electricity	25,000	\$25,000	—
Department of Transportation (Item 2660)			
Diesel retrofit and green fleet program to offset emissions from new power plants	—	20,332	—
Energy Commission (Item 3360)			
Long Term Energy Baseload Reduction Initiative: electricity market analysis, Renewable Energy Program administration, and energy efficiency standards update	3,230	2,626	8
Power plant siting program	3,129	—	19
Alternative energy grant programs	—	1,000	—
Subtotals (Item 3360)	(\$6,359)	(\$3,626)	(27)
Department of Justice (Item 0820)			
Investigate electricity generators and natural gas suppliers	\$3,975	—	15.5
Public Utilities Commission (Item 8660)			
Green Team activities	2,738	—	34
Track San Diego Gas and Electric costs to purchase electricity	—	\$682	4
Subtotals (Item 0820)	(\$2,738)	(\$682)	(38)
Electricity Oversight Board (Item 8770)			
Augment and reorganize staff by function to improve market oversight	—	\$983	7
Green Team activities	\$512	—	4
Contract funds for the University of California Energy Institute for market research	—	500	—
Reauthorize expired positions	—	249	3
Contract funds for legal services	—	75	—
Subtotals (Item 8770)	(\$512)	(\$1,807)	(14)
Totals	\$1,138,584	\$51,447	98.5

cars with “greener” alternatives, partly to provide emission offset credits that could be used for new power plants.

Administrative Activities. The remaining proposals, totaling \$19.7 million (\$13.6 million General Fund), would fund departments’ administrative efforts to oversee and investigate the electricity market.

- **Energy Commission—\$10 Million (\$6.4 Million General Fund).** Long-Term Energy Baseload Reduction Initiative, which includes electricity analysis, renewable energy, and energy efficiency components. Continuation of current-year funding for (1) expected workload in the power plant siting program and (2) solar and distributed generation grant programs.
- **Department of Justice—\$4 Million General Fund.** Investigation of electricity generators and natural gas suppliers for evidence of collusion, market manipulation, or other unfair business practices.
- **Public Utilities Commission—\$3.4 Million (\$2.7 Million General Fund).** Continuation of current-year funding for Green Team responsibilities, promoting self-generation, identifying transmission system congestion problems, and improving energy efficiency programs currently administered by the utilities (pursuant to Chapter 329, Statutes of 2000 [AB 970, Ducheny]). Implementation of Chapter 328, Statutes of 2000 (AB 265, Davis), which requires the Public Utilities Commission (PUC) to track San Diego Gas and Electric costs to purchase electricity above the consumer rate cap and determine the reasonableness of those costs.
- **Electricity Oversight Board—\$2.3 Million (\$0.5 Million General Fund).** Expand oversight of the electricity market with additional staff, continuation of Green Team funding provided by Chapter 329, and contract funds for research purposes and legal activities related to proceedings before the Federal Energy Regulatory Commission.

LAO Recommendations. We do not raise concerns with the Caltrans, Department of Justice, or PUC proposals. For the remaining departments, our recommendations appear in our analyses of those budget bill items. Briefly:

- We withhold recommendation on the proposals for (1) the \$1 billion energy initiatives set-aside, (2) \$50 million for departments’ utilities costs, (3) \$3.1 million for the Energy Commission’s power plant siting activities, and (4) \$0.5 million in consultant funds for the Electricity Oversight Board, pending receipt and review of information justifying the proposed expenditures (this chapter).

- We recommend that the Legislature delete the \$100 million ARB diesel engine grant proposal from the budget bill and adopt the proposal in separate legislation if the Legislature wishes, given the policy implications of trading off emission reductions for additional power plant capacity (see “Resources” chapter).
- For the Energy Commission, we recommend that the Legislature (1) approve for one year only the \$2.8 million request for General Fund support to continue survey activities regarding electricity use and (2) change the fund source for specified energy efficiency and grant proposals (this chapter).

Recent Legislation

In addition to these proposals in the Governor’s budget, the Legislature convened in a special session on electricity beginning in January. At the time this analysis was written, the special session was continuing and the Legislature had approved several bills related to the state’s electricity crisis.

State Purchases of Electricity. On January 17, 2001, the Governor declared a state of emergency in response to the financial condition of Pacific Gas and Electric (PG&E) and Southern California Edison (SCE). The Governor ordered the Department of Water Resources (DWR) to buy electricity for these two utilities to meet customer demand. Under this emergency authority, DWR spent \$150 million buying electricity.

Subsequently, two special session bills were enacted authorizing the state to purchase and sell electricity. These bills are:

- ***Chapter 3x, Statutes of 2001 (SB 7x, Burton).*** Appropriated \$400 million from the General Fund for DWR to purchase electricity for 12 days beginning January 19 (the day the statute became effective), and sell it at cost to the Independent System Operator (ISO), municipal utilities, or directly to utility customers.
- ***Chapter 4x, Statutes of 2001 (AB 1x, Keeley).*** Authorized DWR to enter into long-term contracts to purchase electricity, authorized the sale of revenue bonds (discussed further below), appropriated \$500 million from the General Fund for the state to continue purchasing electricity, and authorized a ten-day notification process to the Legislature for deficiency requests from the Department of Finance (DOF) for additional funds.

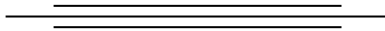
As the state began negotiating cheaper long-term contracts, pursuant to AB 1x, DOF submitted a deficiency request to the Legislature for an

additional \$500 million. Thus, the state had committed to \$1.6 billion from the General Fund to buy electricity at the time this analysis was written.

Assembly Bill 1x also authorized DWR to issue revenue bonds to help finance the cost of the state's electricity purchases. These bonds would be used in part to reimburse the General Fund for the funds already committed for this purpose, presumably before the end of the current year. In addition, the bonds would prospectively finance the difference between the actual cost DWR pays for electricity and the rate consumers pay. A portion of ratepayers' payments will be designated to pay off these bonds.

Other Legislation. In addition to these two bills, the Legislature has also revised some provisions of the original restructuring legislation. Chapter 1x, Statutes of 2001 (AB 5x, Keeley), replaced the 26-member stakeholder board of ISO with a five-member board of gubernatorial appointees. Board members cannot be affiliated with any participants in the electricity market and do not require Senate confirmation.

Chapter 2x, Statutes of 2001 (AB 6x, Dutra), prohibits the utilities from selling any more power plants until January 1, 2006. Remaining utility-owned power plants are to be dedicated to providing electricity to utility customers.



PETROLEUM VIOLATION ESCROW ACCOUNT

Background

In the early 1970s, the Organization of Petroleum Exporting Countries embargoed crude oil exports to the United States. In response to this severe restriction in oil supply, the federal government regulated oil prices from 1973 to 1981 to prevent price gouging by domestic crude oil producers and to ensure fair allocation of oil resources. The federal Department of Energy was responsible for identifying violations, recovering overcharges, and obtaining restitution for wronged parties.

Settlements. Through the 1980s, several overcharge cases against domestic oil producers were settled or decided in court.

- The first case was settled in 1981. Standard Oil of California (Chevron) paid a \$50 million fine for oil overcharges, of which California received \$6.6 million.
- In 1983, California received \$19 million in settlement funds pursuant to the Warner amendment of the federal budget act.
- In 1986, Exxon Corporation paid \$2.1 billion in restitution for overcharges, of which California received \$207 million based on historical usage patterns of petroleum products.
- Also in 1986, the Stripper Well settlement resulted from charges that producers miscertified oil to avoid government price restrictions. California received \$169 million of the \$993 million that went to states, again based on historical usage patterns.
- California also received \$25 million from subsequent smaller settlements.

In total, California has received \$426 million from these settlements.

Allowable Uses of Funds. The allowable uses of overcharge funds varied by case or settlement and included programs such as the following:

- Public transportation, computerized school bus routing, and ridesharing.
- Building energy audits, energy assistance, and home weatherization.
- Highway, bridge, and airport maintenance and reduction in airport user fees.
- Specified federal programs.

In general, the penalties levied against oil producers were intended to provide restitution to victims of the oil overcharges. Expenditure of the funds was required to benefit energy consumers and could not supplant state funds already allocated for energy-related programs. (The Energy Commission is the state agency responsible for certifying that proposed projects meet these standards for allowable uses of the Petroleum Violation Escrow Account [PVEA] funds.) The courts also specified that interest earned on these funds must be used for the same purposes.

Expenditure of PVEA Funds. From 1985-86 through the current year, the state has spent \$624 million in PVEA funds for program and administrative costs (see Figure 1, next page). This includes the \$426 million in settlement funds the state received over the years plus interest earned on these funds. Projects and programs have addressed many issues, including the following:

- **Transportation.** Traffic flow improvements, transit capital improvements, traffic signal management, and ridesharing vanpool loans.
- **Fuel.** Fishing fleet fuel efficiency, school buses that use cleaner burning fuels, and alternative fuels demonstration projects.
- **Low-Income Persons.** Low-income energy assistance and weatherization.
- **School Assistance.** Air conditioning for year-round schools.

Funding for these projects and programs has been allocated to several departments. The Energy Commission and the Department of Transportation have been the principal recipients of PVEA funds. The California Conservation Corps, the Department of Community Services and Development (formerly the Department of Economic Opportunity), the Air Resources Board, and the Office of Planning and Research also received funding.

Administrative Costs. In addition to these program expenditures, the Energy Commission compiled data from available information for PVEA funds allocated to administrative costs. The Energy Commission incurred

the large majority of administrative costs—\$23 million of \$30 million. These administrative costs are approximately 5 percent of total PVEA expenditures.

Figure 1

Petroleum Violation Escrow Account Expenditures

(In Thousands)

Year	Expenditures		Totals ^b
	Program	Administration ^a	
1985-86	\$3,900	—	\$3,900
1986-87	172,500	—	172,500
1987-88	16,452	\$848	17,300
1988-89	173,266	579	173,845
1989-90	4,392	779	5,171
1990-91	24,922	978	25,900
1991-92	16,619	1,532	18,151
1992-93	40,278	3,313	43,591
1993-94	32,105	2,345	34,450
1994-95	6,666	2,718	9,384
1995-96	11,294	2,235	13,529
1996-97	3,712	2,577	6,289
1997-98	17,776	2,923	20,699
1998-99	23,087	2,730	25,817
1999-00	4,562	2,814	7,376
2000-01 ^c	43,493	2,393	45,886
2001-02 ^d	4,857	967	5,824
Totals	\$599,881	\$29,731	\$629,612

^a Information provided by the Energy Commission.

^b Information from Governor's budgets.

^c Estimated.

^d Proposed.

Interest Repaid to PVEA. As mentioned above, the court settlements and decisions required that states use interest earned on PVEA funds for the same energy-related purposes as the settlement funds allocated to them. In 1996, however, the Department of Finance (DOF) audited PVEA and found that the account had not been credited with interest for settlement monies that had been transferred or appropriated to other funds. This "loss" of interest to PVEA was related to transactions involving loans to

the General Fund and the deposit of interest earned on PVEA funds into the General Fund and the Public Transportation Account rather than PVEA.

The DOF audit identified a total of \$43 million that should have been credited to PVEA. The full amount identified by DOF, *plus* interest accrued since the 1996 DOF audit, has been repaid to PVEA. As shown in Figure 2, the total amount repaid was \$56 million—\$33 million from the General Fund and \$23 million from the Public Transportation Account.

Figure 2

Interest Owed to PVEA

(In Thousands)

Year	General Fund	Public Transportation Account	Totals
1996-97	—	\$17,485	\$17,485
1997-98	—	5,366	5,366
1998-99	—	497	497
1999-00	\$4,000	—	4,000
2000-01	28,633	—	28,633
Totals	\$32,633	\$23,348	\$55,981

Current Status of PVEA

The 2001-02 Governor’s Budget indicates that PVEA has a \$3.1 million balance at the beginning of the fiscal year. In the 1990s, settlement revenues allocated to the states from the federal government declined to just a few million dollars as more and more overcharge cases concluded. The Governor’s budget shows that in 2001-02, for the first time, California will receive no new settlement funds. Thus, the only budget-year revenues will be interest earned on the \$3.1 million fund balance and on PVEA monies transferred to other funds for projects approved in prior years. The budget projects this interest income will total \$3.7 million, providing \$6.8 million in total resources for the budget year (see Figure 3, next page).

The Governor proposes expenditures totaling \$5.8 million—\$967,000 for Energy Commission administrative costs and \$4.9 million for the Department of Community Services and Development to fund low-income energy assistance and weatherization programs. This leaves \$1 million in uncommitted resources at the end of the budget year.

Figure 3	
PVEA Fund Condition 2001-02	
<i>(In Thousands)</i>	
Beginning balance	\$3,089
Interest income ^a	3,740
Total resources	\$6,829
Expenditures	\$5,824
Remaining resources	\$1,005
^a Includes interest earned on monies in PVEA and PVEA monies previously transferred to other funds.	

The Future of PVEA

We recommend that the Energy Commission report to the Legislature, prior to budget hearings, on a multiyear projection of expected (1) administrative costs, based on schedules for current and proposed projects, and (2) interest earnings, so that the Legislature can determine how many years PVEA can be expected to provide some funding for energy-related projects.

With no further settlement revenues expected, the state cannot continue to fund many projects from PVEA. Two other factors influence the amount of PVEA funds that will be available for projects: Energy Commission administrative costs and interest earnings. The Energy Commission currently oversees approximately 300 active PVEA-funded projects. As these projects are completed, the commission's administrative expenses should decline, but there will still be administrative costs over the next several years. Also, funds in PVEA will continue to earn interest until the funds are actually spent. The commission should be able to provide the Legislature a multiyear projection of expected (1) administrative costs, based on schedules for current and proposed projects, and (2) interest earnings. Consequently, we recommend that the commission report prior to budget hearings on these two factors. With this information, the Legislature can determine how many years PVEA can reasonably be expected to provide some funding for energy-related projects.

STATE DATA CENTERS

Data Center Study Needed

In 1997, the Department of Information Technology (DOIT) completed a study which recommended ways to reduce the number of state-operated data centers. In 1998, DOIT suspended its data center consolidation activities to focus on completing Year 2000 (Y2K) remediation activities. At the time that this analysis was prepared, DOIT had not resumed its data center consolidation efforts.

A number of factors, including technological changes and staff recruitment and retention issues, have rendered DOIT's 1997 Data Center Consolidation Report out-of-date. We therefore recommend that the Legislature direct DOIT to report at budget hearings on the resources and time frames needed to conduct a study which (1) examines data centers' rates for nonmainframe activities, (2) identifies potential opportunities for specialization between the state's primary data centers, and (3) identifies data center functions that can be provided more efficiently by private industry.

The Stephen P. Teale Data Center (TDC) and the Health and Human Services Agency Data Center (HHSDC) are the state's two primary data centers which provide computer and network services to various departments and local jurisdictions. The two data centers are funded entirely through reimbursements from client departments, and their combined expenditure authority is \$234.8 million in the budget year.

Data Center Establishment. Chapter 787, Statutes of 1972 (SB 1503, Teale) established the state's current data centers to serve specific program areas, as summarized in Figure 1 (see next page).

The HHSDC, TDC, and Hawkins Data Center provide the majority of the state's centralized computing services. Neither the Franchise Tax Board (FTB) nor Board of Equalization (BOE) data centers ever developed the larger computing capacity that characterized the other three data centers.

Legislature Directs Administration to Evaluate Consolidation Benefits. Chapter 508, Statutes of 1995 (SB 1, Alquist) made significant changes in the

planning, implementation, and oversight of the state's information technology (IT) activities. Specifically, this legislation directed the DOIT to conduct a study evaluating the benefits of consolidating the existing data centers.

Figure 1

State Data Centers Established by Chapter 787, Statutes of 1972 (SB 1503, Teale)

Primary Program Area	Data Center Providing Computing Services
Law enforcement	Department of Justice, Hawkins Data Center
Business and service	Stephen P. Teale Data Center
Revenue	Franchise Tax Board and Board of Equalization
Human services	Health and Human Services Agency Data Center

Findings From DOIT's 1997 Data Center Consolidation Study. Figure 2 summarizes the major recommendations from DOIT's 1997 Data Center Consolidation Study.

Figure 2

Major Recommendations From DOIT's 1997 Data Center Consolidation Study

Recommendation	Implementation Status
Consolidate all state IBM-compatible mainframe functions into either the Health and Human Services Agency Data Center (HHSDC) or Stephen P. Teale Data Center (TDC) but do not consolidate Hawkins Data Center with any other data center	Implemented
Contract for selected data center functions but do not contract for HHSDC or TDC operations	Considered, not implemented
Place either HHSDC or TDC under private ownership and control	Considered, not implemented
Begin administrative initiatives such as establishing centers of expertise in either HHSDC or TDC	Partially implemented
Place midrange computers at either HHSDC or TDC	Implemented

The study concluded that little savings could be achieved (\$7.7 million annually after an initial one-time investment of \$12.9 million) by consolidating HHSDC and TDC.

Administration Suspends Implementation of Data Center Consolidation Due to Y2K Efforts. In 1998 the administration notified the Legislature that it would suspend all data center consolidation efforts until completion of Y2K activities with the exception of placing midrange computers at either HHSDC or TDC. At the time this analysis was prepared, DOIT had not resumed data center consolidation efforts. As Figure 2 shows, to date, two of the recommendations have been implemented, several were considered but not implemented, and one recommendation was partially implemented.

New Factors to Consider on Data Center Consolidation

The 1997 study identified several anticipated events, such as staff retirements and changes in contracting costs that might require the state to reevaluate its recommendations at some time in the future. In fact, the state has experienced a number of changes in its IT operations which render the DOIT's earlier report, with its findings and conclusions, out-of-date. These factors are summarized in Figure 3 and discussed in more detail below.

Figure 3

New Factors to Consider in Data Center Study

- Technology has shifted from mainframe to mid-range systems; much mainframe consolidation has already been accomplished
- Network technology has become more complex
- Data center rates for nonmainframe activities are difficult to calculate
- State has a staff recruitment and retention problem for information technology classifications
- Stephen P. Teale Data Center (TDC) may lose specialized skills as older workforce retires
- Health and Human Services Agency Data Center and TDC perform identical functions
- More options may be available to contract with private business for specific functions

Technology Has Shifted From Mainframe to Midrange Systems. Technology has dramatically changed since the establishment of the data centers in 1972. At that time, mainframes were the only computers available for processing large volumes of data. Now, midrange systems provide computing power on par with earlier mainframes. The DOIT's 1997 report focused almost exclusively on mainframe systems.

In 1997, DOIT reported to the Legislature that it intended to consolidate the existing IBM-compatible mainframe operations at FTB, BOE, State Controller's Office (SCO), Public Employees' Retirement System (PERS), California State Lottery, and State Treasurer's Office (STO) into TDC. During our review, we found that BOE, STO, and SCO have consolidated all of their mainframe operations into TDC. The administration does not have statutory authority to implement consolidation at PERS and the California State Lottery. At this point it is unlikely that the state would achieve much additional benefit from mainframe consolidation because mainframes are no longer as prevalent as they were in 1997.

The DOIT's 1997 report gave little attention to nonmainframe systems. Since that time, both HHSDC and TDC have experienced tremendous growth (over 400 percent) in midrange systems. As a result of these changes, earlier consolidation recommendations may not address current circumstances and therefore are of limited value.

Network Technology Has Become More Complex. As the state has shifted from mainframe to midrange systems, the data communications networks have also changed. Mainframe communications networks used to allow only one type of data communications signal to transmit through the networks. Now, data networks allow multiple communication signals to transmit through the networks, thereby permitting multiple systems such as personal computers (PC), midrange and mainframes systems to connect to the same network. This makes it more costly and complicated to design, implement, and maintain these networks. Both HHSDC and TDC operate these more complex data networks and have requested budget increases over the past few years to support them. The DOIT's 1997 study did not analyze these functions.

Data Center Charges for Nonmainframe Activities Are Difficult to Calculate. The mainframe and early networks systems were designed for use by multiple organizations. For this reason, they contained mechanisms which allowed data centers to charge based on actual usage rates. The newer midrange and network systems do not have those same mechanisms thereby making it difficult for data centers to base charges on actual usage.

In our review, we found that HHSDC and TDC use different methods to calculate charges for supporting similar systems. In addition, we

found that the administration has not examined these rate setting differences to determine which would be most appropriate.

State Has Problems With IT Staff Recruitment and Retention. For the past several years, the state has experienced some problems in recruiting and retaining IT staff. Generally, the state provides lower salaries and incentives than private industry and experiences additional recruitment difficulties due to civil service requirements. The state's current vacancy rate for IT classifications, which ranges between 15 percent to 19 percent, is slightly higher than the overall state vacancy rate of 15 percent. Further examination is needed to assess the state's ability to fill IT positions, particularly at the state's primary data centers which support critical IT systems.

The TDC Has Older Workforce. The DOIT's report found that HHSDC and TDC had an older workforce with highly specialized skills. The report indicated that data centers run the risk of losing these skills due to higher retirement rates among this segment of the workforce.

Our review indicates that TDC has a slightly older workforce than the state's IT workforce as a whole. For example, 17 percent of the state IT workforce is between the ages of 51 and 55 compared to 23 percent of TDC's workforce. This means that TDC can anticipate losing some of its highly skilled workforce in the near future and may be unable to adequately replace these employees because of the state's overall problem of IT staff recruitment.

The HHSDC and TDC Perform Identical Functions. Both HHSDC and TDC perform the same functions including supporting mainframe and midrange systems and communications networks. The exceptions are HHSDC's oversight of large automation projects and TDC's support of Geographical Information Systems. The DOIT's 1997 report did not examine the benefits of specializing existing functions between the two data centers, but instead focused primarily on reducing the number of mainframe data centers. We believe it may be possible to achieve efficiencies—either in cost savings or improved operations—by each data center specializing in particular functions. For example, one data center could provide support to mainframes while the other could support midrange systems.

More Outsourcing Options May Be Available. The DOIT's 1997 report also recommended that the state have private industry perform selected data center functions (a process known as "outsourcing") such as printing, help desk, and network support. Since the report was issued, both HHSDC and TDC have contracted out their printing functions, but not others.

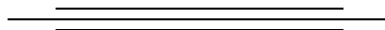
Since technology has shifted from the mainframe to midrange systems, private industry now provides services that were not available in 1997. For example, private data centers provide “web hosting” services which allow customers to be responsible for maintaining web pages while the private data center supports and operates the computer. With anticipated retirements and the state’s difficulty in recruiting and retaining IT staff, outsourcing may offer a solution to providing adequate support for some of the state’s IT operations.

Data Center Study

The primary purpose of the 1997 study was to (1) reduce the number of mainframe data centers operated by the state, (2) identify areas for contracting with private vendors to provide state data center operations, and (3) identify state functions that could be performed efficiently by private industry. In view of the issues discussed above, DOIT’s 1997 report is out-of-date. A new data center study is needed to focus on those activities that were *not* reviewed in the 1997 study. Those would include (1) examining the rate setting methods for nonmainframe activities, (2) identifying opportunities to specialize existing functions between the state’s two primary data centers, and (3) examining potential new outsourcing opportunities that have developed since the 1997 study.

The DOIT Should Report on Resources Needed to Conduct Study. We recommend that the Legislature direct DOIT to report at budget hearings on the resources and time frames it would need to conduct a new data center consolidation study. The DOIT should identify the resources needed to:

- Identify existing data center functions that can be specialized between HHSDC and TDC and which will result in reduced costs or improved efficiencies.
- Examine HHSDC’s and TDC’s methods for rate-setting for nonmainframe activities and develop a single consistent and appropriate methodology.
- Identify those data center functions private industry can provide at a reduced cost and/or with improved efficiency.



DEPARTMENTAL ISSUES

General Government

DEPARTMENT OF INFORMATION TECHNOLOGY (0505)

The Department of Information Technology (DOIT) is responsible for ensuring that appropriate plans, policies, and procedures are in place to guarantee successful implementation of state information technology (IT) projects. Chapter 508, Statutes of 1995 (SB 1, Alquist) created DOIT to address state problems in successfully implementing IT projects. This legislation included a sunset date of July 1, 2000. The Legislature enacted Chapter 873, Statutes of 1999 (AB 1686, Dutra) to extend DOIT's sunset to July 1, 2002.

The budget proposes \$11.8 million (\$11.1 million from the General Fund and \$750,000 from reimbursements) for support of the department's operations in 2001-02, an increase of \$483,000, or 4 percent, above estimated current-year expenditures. The budget proposes 76 personnel-years for the department in the budget year.

Key Program Information Not Currently Available to the Legislature

We recommend that the Legislature not take action on the Department of Information Technology's (DOIT) budget until (1) DOIT submits required supplemental reports and (2) the Legislature has an opportunity to receive and review the outcomes of an audit of DOIT operations performed by the Bureau of State Audits at the request of the Joint Legislative Audit Committee.

The DOIT Has Failed to Meet Legislative Directives in the Past. Over the past four years, the Legislature has directed DOIT, either through budget or supplemental report language, to issue policies in a broad array of areas. These policy directives were to include project management training, procurement alternatives, project sizing, project delegations, maintenance and operations, system and information security, operational recovery, project oversight, feasibility study reviews (FSR), and procurement. With the exception of FSR and operational recovery, DOIT has not issued any new policies as directed by the Legislature.

Figure 1 summarizes the Legislature's requests to DOIT for seven supplemental reports in 2000-01. At the time this analysis was prepared, DOIT had submitted two reports on oversight policy. As regards the report on the oversight of county-based IT projects, we believe that the department has failed to adequately respond to this requirement as discussed below. As regards the remaining five reports, the department indicates that it is in the process of developing three reports that would address (1) policies for a streamlined FSR process and revised state acquisition practices and (2) DMV automation difficulties. The status of two reports (Veterans' Home and "Capability Assessment") is unknown.

The DOIT Has Not Responded to Request for Information on County-Based Projects. One important area where DOIT has failed to respond to the supplemental report requests is in the area of county-based projects. The state has several large county-based automation projects underway. (These are described in detail in our analysis of budget Item 4130—the Health and Human Services Agency Data Center [(HHSDC).] Both DOIT and HHSDC provide some level of oversight for these various projects. Last year the Legislature adopted supplemental report language asking the two departments to explain how their oversight roles differ and at what point in a project's development they provide that oversight.

In response to this request, HHSDC developed an oversight plan, with input from the key stakeholders, and provided a report to the Legislature in January 2001. The Legislature also directed DOIT to submit a report which would describe DOIT's oversight role and activities for county-based projects and describe how these activities would be conducted between HHSDC and the counties. The DOIT stated that it met the intent of the supplemental report by providing input into HHSDC's oversight plan.

In our view, the HHSDC oversight plan was not intended, nor does it meet, the intent of the supplemental report for DOIT. It does not describe the role of DOIT, nor does it define the activities that DOIT will conduct. Finally, it does not describe how DOIT's activities will

be coordinated between the counties and HHSDC. We recommend that DOIT submit a separate report on county projects prior to budget hearings which addresses the issues identified in last year's supplemental report language.

Figure 1

DOIT Reporting Requirements Supplemental Report of 2000 Budget Act

Report Title	Purpose of Report	Date Report Due	Status
Information Technology Oversight Policy	Issue state IT oversight policy.	9/1/00	Complete
DOIT's Oversight Role on County-Based IT Projects	Provide report on DOIT's oversight role on the Health and Human Services Agency Data Center's county-based IT projects.	9/1/00	Incomplete
Feasibility Study Review Policy	Issue state policy on DOIT's streamlined feasibility study report review process and procedures.	11/1/00	Underway
Veterans Home Information System	Analyze current automation system operating at the Department of Veterans Affairs' Veterans' Homes and recommend improvements.	12/1/00	Unknown
Department of Motor Vehicles (DMV) Study	Analyze problems DMV encounters when implementing IT projects, estimate cost for replacing current DMV systems, and recommend action for ensuring DMV success in replacing the current systems.	1/1/01	Underway
Capability Assessment Report	Assess DOIT's capability to meet mandates with current resources.	1/15/01	Unknown
Information Technology Procurement Policy	Issue state policy on revised state acquisition process.	3/1/01	Underway

Bureau of State Audits (BSA) Report Would Assist Legislature's Review of DOIT Budget. In June 2000, the Joint Legislative Audit Commit-

tee authorized BSA to undertake a comprehensive review of the state's IT program and projects. The scope of the audit directs BSA to:

- Create a statewide inventory of major IT projects that are in the planning and implementation stages.
- Determine if DOIT has adopted an overall IT strategic plan that guides departmental IT efforts and whether or not departmental strategic plans are aligned with DOIT's plan.
- Select and examine a sample of projects to determine if those projects have been approved by DOIT and designed, managed, and evaluated in accordance with generally accepted project management principles.
- Determine if DOIT has a mechanism for ensuring cooperation among departments on mutually beneficial projects such as E-mail systems.
- Evaluate the sufficiency of DOIT resources.
- Determine if and how DOIT ensures that project risk is shared with vendors.

The BSA advises that the audit will be completed in spring 2001 and that the results will be provided to the Legislature at that time. Because the audit findings may have significant budgetary implications, the Legislature may wish to consider BSA's findings prior to taking any action on DOIT's budget. We, therefore, recommend that the BSA report to the Legislature during budget hearings on the results of this audit and that the Legislature not take action on DOIT's budget until it has had an opportunity to receive and review these audit findings as well as the reports requested by the Legislature.

Information Technology Hardware and Software Replacement Policy Is Needed

The budget contains a number of proposals totaling \$15.1 million (\$12.7 million General Fund, \$2.1 million special fund, and \$300,000 in reimbursements) for the replacement or upgrade of departmental personal computer-based office automation systems. We concur with the merits of these various proposals. We recommend, however, that the Department of Information Technology and the Department of Finance update their current policies to ensure that departments adequately plan and budget for the replacement or upgrades of these departmental systems.

Background. Every department has some kind of office automation system which provides word processing, spreadsheets, and file sharing capabilities. These office automation systems are composed of personal computers (PC), printers, file servers, and networks. Departments are able to acquire these systems through two types of budget mechanisms. Specifically, a department can prepare a FSR with an associated budget request or the department can use the state's Workgroup Computing Policy (WCP).

The state developed the WCP in the 1980s in an effort to allow departments to redirect savings in departmental operating equipment and expense funds to purchase office automation systems. The state's WCP requires that each department develop its own policy that ensures PC compatibility, describes planning and management strategies, and ensures proper oversight and risk mitigation.

Current Policy Seems to Work Well for Acquiring Systems. Since the initiation of the state's WCP, office automation systems have become common place in the state and have probably improved departments' overall internal operations in such areas as reducing the need for typing pools and allowing staff to share documents.

Current Policy Does Not Address Periodic Replacement and Upgrades. The current policy, however, does not address the need to plan and budget for periodic replacement or upgrades to these systems. We have seen evidence of this planning and budget deficiency during the reviews of the state's Year 2000 (Y2K) funding requests. Several departments had to request funds to replace outdated PCs so they could use the Y2K compliant software. In this year's budget proposal, there are a number of similar "replacement" requests summarized in Figure 2 (see next page) to upgrade office automation systems.

Policy Needed Requiring Departments to Budget for Equipment Replacements. We have no concerns with the merits of these particular proposals. We do, however, see a need for the state to update its current policies to require departmental planning and budget adjustments for the periodic replacement and upgrades of their PC-based office automation systems. For this reason, we recommend the adoption of the following supplemental report language for DOIT and Department of Finance (DOF):

The Department of Information Technology and Department of Finance shall by September 1, 2001 issue policies requiring departments to plan and budget for the periodic replacement and upgrades of personal computer-based office automation systems. The policies should include recommended replacement and upgrade schedules and budgeting guidelines for the funding of these replacement and upgrade activities.

Figure 2**2001-02 Proposals to Replace or Upgrade Departmental Office Automation Systems***(In Thousands)*

Department/Proposal	One-Time				Ongoing	
	General Fund	Special Funds	Reimburse-ments	Total	General Fund	Special Funds
Board of Equalization/ Purchase network management software	\$356	\$35	\$79	\$470	—	—
Board of Equalization/ Purchase network management software	1,178	120	263	1,561	—	—
Conservation/ Upgrade department network	1,301	1,302	—	2,603	\$85	\$85
Fish and Game/ Replace software on departmental PCs	4,951	—	—	4,951	1,129	—
Fish and Game/ Upgrade department network	4,544	—	—	4,544	1,199	—
Health Services/ Replace software on departmental PCs	391	392	—	783	—	—
Teachers' Retirement System/ Upgrade department E-mail system	—	209	—	209	—	—
Teachers' Retirement System/ Upgrade department network	—	—	—	—	—	123
Totals	\$12,721	\$2,058	\$342	\$15,121	\$2,413	\$208

Post-Implementation Evaluation Reporting Process Deficient

Our review has found a number of deficiencies and problems with the administration's current process for conducting post-implementation evaluation reports (PIER). We, therefore, recommend that the Legislature (1) fund only those projects with identified measurable benefits; and (2) direct the Department of Information Technology (DOIT) and Department of Finance, through supplemental report language, to issue policies on criteria and funding for independent evaluations. We further recommend the Legislature adopt a three-pronged approach to improve PIER practices during the current year, budget year, and beyond which includes: (1) requiring departments to report at budget hearings on completed Information Technology projects (current year), (2) adopting

budget control language requiring DOIT to report on the results of its PIER reviews (budget year), and (3) enacting legislation requiring the administration to provide PIER information (ongoing years).

Background. When the Legislature receives a budget proposal or a FSR for a state IT project, the proposal generally identifies proposed cost savings or improved efficiencies the project is expected to achieve. Figure 3 provides examples of expected benefits from some state IT projects currently under development.

Figure 3

Examples of Expected Benefits From State IT Projects Under Development

Department	Project Name	Examples of Expected Benefits
State Treasurer's Office	State Treasurer's Registration Issuance and Payment System	<ul style="list-style-type: none"> • Manage state debt in the most efficient, cost effective, and error-free manner.
State Personnel Board	Automated Case Tracking System	<ul style="list-style-type: none"> • Increase by 10 percent the timely processing and closure of appeal cases. • Reduce by 25 percent the hiring of additional administrative law judges to assist in the hearing process.
Forestry and Fire Protection	Infrared Imaging Project	<ul style="list-style-type: none"> • Provide real-time fire perimeter mapping. • Provide detection of low-intensity lightning-caused fires.
Franchise Tax Board	California Child Support Automation System	<ul style="list-style-type: none"> • Increase caseworker efficiency and effectiveness. • Improve relationships with employers and financial institutions.
Justice	Consolidated Firearms Information Systems Enhancements	<ul style="list-style-type: none"> • Prevent the sale or transfer of uncertified handguns. • Process all assault weapon registrations within ten days of receipt.

According to the State Administrative Manual (SAM), departments are required to prepare a post-implementation evaluation report (PIER) for each completed state IT project. The assessment must measure the benefits and costs of the implemented IT system and document projected maintenance and operation costs over the life of the system.

The PIER is intended to document what was *expected* to be achieved and what was *actually* achieved. Without PIERs, the Legislature is unable

to know if an implemented project ever achieved any savings, efficiencies, or other benefits as the administration originally proposed. In addition, without PIERs, the Legislature cannot determine how much an IT system ultimately cost to develop or will cost to operate and maintain on an annual basis.

How the PIER Process Currently Is Administered. According to SAM, most assessments are to be conducted within six months of implementation of the IT project but could occur up to two years after implementation, depending on the nature of the project.

Departments generally conduct their own assessments. In some cases, however, the DOF's Office of State Audits and Evaluation may conduct the assessment and prepare the PIER. After a department has completed the PIER, the PIER is provided to DOIT and the Legislature. The DOF also requires that all PIERs be submitted to it for review. The DOIT evaluates the PIER to determine if the project achieved the anticipated benefits and savings and approves the PIER to finalize the project.

Deficiencies and Problems Exist With Current PIER Process. In our review of the state's PIER process, we found a number of deficiencies and problems which are summarized in Figure 4.

Figure 4

LAO Findings on State's Current PIER Process



No tracking system exists to monitor when PIERs are due or submitted to the Legislature. As a result, the Legislature typically does not receive information about benefit and cost savings resulting from completed IT projects.



The DOIT does not keep records of which IT projects have been completed.



DOIT's PIER review process has lower priority than the review of feasibility study reports and special project reports.



Measurable benefits have not been identified for many IT projects.



Departmental reviews lack independence.

No Tracking System Exists to Monitor PIER Due Dates or Submission to the Legislature. In our review, we found that neither DOIT nor DOF track when PIERs are due on state IT projects. In addition, neither department provides any follow-up when PIERs are overdue. Since there is no tracking mechanism to ensure accountability, it is unclear if departments are completing their PIERs as required by current state policy.

In addition, even though departments are required to provide PIERs to the Legislature, we could find no tracking system within the administration that ensures departmental compliance. It is our understanding that neither DOIT nor DOF is responsible for monitoring whether departments provide PIERs to the Legislature. Therefore, to the extent that the Legislature does not receive PIERs, it is unable to identify the benefits or savings that accrue to the state as a result of IT projects.

The DOIT Does Not Keep Records of Completed IT Projects. The SAM states that DOIT's approval of a PIER "completes" a project. Our review indicates that DOIT does not keep records of PIER reviews. In addition, we found that DOIT does not consistently notify the administration or the Legislature concerning the results of its PIER reviews. According to our records, there currently could be over 400 "open" IT projects (that is, projects for which a PIER has not been submitted to DOIT).

The DOIT Gives PIER Review Process Low Priority. Of the 87 PIERs that DOIT has received from other agencies, DOIT is unable to identify the number it has actually reviewed and approved. According to DOIT, the review of PIERs has lower priority than its other activities such as reviewing FSRs and special project reports. In addition, DOIT states that it did not have enough resources to process this workload until the Legislature increased its budget in the *2000-01 Budget Act*.

Measurable Benefits Have Not Been Identified for Many State IT Projects. State policy requires that each state IT project result in measurable program benefits. The PIER is the mechanism used to determine how well the IT system was able to achieve those benefits.

In our review, we found that measurable benefits have not been identified in the FSR for many IT projects, even though such benefits may very well result from the projects. Therefore, it is difficult for departments to evaluate how well the IT project was able to provide measurable benefits.

Departmental Self-Evaluations May Lack Objectivity. Current state practice directs departments to perform their *own* evaluation of implemented projects. This practice has a potentially significant limitation, particularly for large scale projects: the department that *implemented* the project is also the same department that *evaluates* whether or not the project was successful in providing the intended benefits. This practice of using

the implementor of a project to also evaluate the results of the project may call into question the validity and objectivity of the final evaluation.

Improvements in PIER Process Needed. We believe that there are a number of steps the Legislature can take to improve the state's PIER process which are summarized below. We recommend that the Legislature use a three-pronged approach with actions to be taken in the current year, the budget year, and future years.

Budget Funds Only for Projects With Identified Measurable Benefits and Require DOIT and DOF to Issue Policies on Project Evaluations. We recommend the Legislature fund only those state IT projects that have specifically identified measurable goals of either reducing government costs, improving service, or increasing state efficiencies. In addition, the Legislature should direct DOIT and DOF, through supplemental report language, to develop and issue policies for use in determining when a post-implementation evaluation review warrants preparation by an independent evaluator. The policies should specify (1) the size and types of projects requiring an independent evaluation and (2) procedures for selecting and funding independent evaluators. The following supplemental report language is consistent with this recommendation.

The Departments of Information Technology and Finance shall issue by January 1, 2002 policies for use by departments in determining when a post-implementation evaluation review warrants preparation by an independent evaluator. The policies shall specify (1) the types of projects requiring an independent evaluation and (2) procedures for selecting and funding independent evaluators.

Require Administration to Report on PIER Reviews. During this year's budget hearings, the Legislature should require that the departments report on all IT projects completed in the last year. (The Legislature has used this approach in past budget hearings for other statewide issues of legislative concern such as implementation of the Dymally-Alatorre Bilingual Services Act of 1973 and departmental compliance with statutory recycling requirements.) Departments should be able to identify what projects have been completed, the benefits or cost savings that were achieved, any cost or schedule deviations that may have occurred, and the annual costs associated with the maintenance and operation of the implemented system.

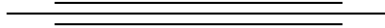
For the budget year, we recommend that the administration report to the Legislature on the results of PIER evaluations and reviews. Accordingly, we recommend that the Legislature adopt the following budget bill language:

Within 30 days of receiving a Post-Implementation Evaluation Report (PIER), the Department of Information Technology shall provide a copy

of the PIER and the results of its PIER evaluation to the chairs of the budget committees in each house and the Chair of the Joint Legislative Budget Committee. The results of the PIER evaluation shall describe the benefits that were achieved as a result of the implemented project, any cost or schedule deviations that may have occurred during the development of the project, and the annual costs associated with the maintenance and operation of the implemented system.

Enact Legislation Requiring the Administration to Provide PIER Information. When the Legislature considers legislation to extend DOIT's sunset date, we recommend adding several provisions to improve the process for conducting post-implementation evaluation reviews in future years. We suggest that language be included to:

- Require the administration to provide copies of the PIER and DOIT's PIER approval letter to the fiscal committees of both houses and the Joint Legislative Budget Committee.
- Require DOIT to report annually on all completed IT projects, overall benefits and savings that were achieved, any cost or schedule deviations that may have occurred, and the annual costs associated with maintenance and operation of the implemented systems.



OFFICE OF PLANNING AND RESEARCH (0650)

The Office of Planning and Research (OPR) assists the Governor and the administration in planning, research, and liaison with local governments. The office has responsibilities pertaining to state planning, California Environmental Quality Act assistance, environmental and federal project review procedures, and oversees the Commission on Improving Life Through Service, which administers the California Americorps program.

The Governor's budget proposes expenditures of \$100 million (\$50 million from the General Fund, \$48.7 million from special funds, and \$1.3 million in reimbursements). This includes an increase of \$41 million from the General Fund for a touch screen voting system pilot program, which is discussed below.

Touch Screen Voting Pilot Program Not Justified

We recommend the Legislature reject the request for \$40 million from the General Fund to support a three-county touch screen voting pilot program because the Secretary of State already has certified these systems for use in California elections, and counties already have initiated pilot programs to test this equipment. The proposal fails to justify the need for an additional pilot program, nor does it provide information on how the program would be administered or evaluated. (Reduce Item 0650-101-0001 by \$40 million.)

The budget proposes a one-time augmentation of \$40 million from the General Fund for a pilot program which would provide local assistance grants to test touch screen voting systems. Specifically, the proposal would provide funds, on a dollar-for-dollar matching basis, to three counties of varying size.

Background. Touch screen voting systems allow voters to push on-screen "buttons" to record their choice. The system is designed to prevent

voters from accidentally voting for multiple candidates for an office for which there can be only one winner. The machines, generally located in regular polling places, automatically count and recount vote totals, but can print out facsimiles of paper ballots for a hand recount if desired.

The Secretary of State (SOS) is responsible for testing and certifying all voting systems used in California elections, including touch screen systems. To date, SOS has certified three different types of touch screen systems for counties to use. In addition, six counties have used touch screen systems to varying degrees in actual elections, and one county has used touch screen voting for an entire general election.

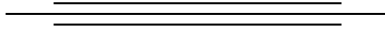
We have the following concerns with this budget proposal.

Touch Screen Voting Has Already Been Tested in California. The budget proposal states that a pilot program is necessary to test the feasibility of using touch screen voting systems. The SOS, however, has already certified three touch screen systems and has completed three pilot projects to test the capacity of the touch screen voting system to handle ballot measures, recall elections, and one general election. Most recently, during the 2000 general election, Riverside County residents voted using touch screen voting equipment. Although the county encountered some problems, it has resolved these issues. The budget proposal does not explain what additional information OPR hopes to obtain through further pilot testing.

Proposal Lacks Important Details. Key program components necessary to evaluate the budget proposal, currently are unavailable. These include:

- Details on how a grant program would be administered, how counties would be selected, and what expenditures would be permitted.
- A determination of whether the state or local governments would be responsible for providing ongoing system support, storage, maintenance, and equipment replacement costs.
- Development of criteria for evaluating touch screen voting systems once they are implemented.
- An explanation of how the program would be coordinated with SOS, which generally has provided oversight for all election-related programs.
- Information on how OPR expects to acquire the knowledge and experience to implement a pilot program that would build on, rather than duplicate, past county touch screen voting pilot programs.

Analyst's Recommendation. For these reasons, we recommend the Legislature deny this proposal, for a General Fund savings of \$40 million.



CALIFORNIA GAMBLING CONTROL COMMISSION (0855)

The California Gambling Control Commission was established by Chapter 867, Statutes of 1997 (SB 8, Lockyer). The five-member commission is appointed by the Governor subject to Senate confirmation. The commission (1) monitors and enforces the terms of tribal-state gaming compacts (including the administration and distribution of funds received by the state as a result of Indian gaming activities); (2) is responsible for the licensing and regulation of card rooms, card room owners, and certain card room employees; and (3) provides oversight for specified aspects of horse track betting.

The 2001-02 Governor's Budget proposes \$4.7 million (\$2.8 million from the Indian Gaming Special Distribution Fund and \$1.9 million from the Gambling Control Fund) and 42.8 personnel-years (PYs) for support of the commission and its activities. This compares to the half-year funding the Legislature provided in the 2000-01 Budget Act of \$576,000 (Gambling Control Fund) and 11 positions (including the commissioners). The Governor's budget indicates that the administration will seek legislation to augment the current-year funding by \$2.4 million (\$1.7 million from the Indian Gaming Special Distribution Fund and \$0.7 million from the Gambling Control Fund) and increase staff by 15 PYs. According to the Governor's budget, the proposed funding from the Indian Gaming Special Distribution Fund in the current year and budget year is dependent on a General Fund loan because there are no expected revenues to this fund in either year.

Background

The Commission's Role in the Tribal-State Gaming Compacts. As a result of the passage of Proposition 1A in March 2000, Class III gambling (such as slot machines and banked or percentage card games) became

legal on California Indian land for those Indian tribes that enter into a tribal-state compact approved by the Legislature, the Governor, and the federal government. The primary role of the commission is to interact with the tribal gaming agencies to ensure the terms of the compacts are followed. The following is a list of some of the commission's major responsibilities under the compacts:

- Develop and propose regulations to the Tribal Gaming Association to ensure public health, safety, and welfare.
- Administer as trustee the collections, deposits, and distribution of funds in the Sharing Trust Fund (described further below) pursuant to the terms of the tribal-state compacts.
- Administer the collections and deposits of revenue for the Special Distribution Fund (described further below) pursuant to terms of the tribal-state compacts.
- Review licenses and permits to assure no unqualified or disqualified person is issued or allowed to hold a license.
- Monitor licensed gambling operation ownership to assure no unqualified or disqualified person has material involvement.

Commission Responsibilities and Staffing Need Clarification

We withhold recommendation on the proposed \$4.7 million for support of the California Gambling Control Commission because the commission's roles, responsibilities, and planned activities, and the division of responsibilities between the commission and the Department of Justice, need clarification.

The budget year is the first full year of operation for the commission. In the current year, the commission is authorized five commissioners and six staff. On August 29, 2000, the Governor announced the appointments of four members to the commission. As of January 2001, the fifth commissioner had not been appointed. Prior to the appointments of the commissioners, the Department of Justice's (DOJ's) Division of Gambling carried out the investigation and review of licenses and employment applications as called for under the compacts. The commission, now that it is in operation, needs to determine the extent to which the commissioners will assume the responsibilities for these activities. This would include, but not be limited to, the development of a work plan that specifically identifies the duties and responsibilities of both the commission and the division.

Roles and Responsibilities Need to Be Clearly Defined. Although the commission has provided a descriptive narrative for the organization, the roles, responsibilities, and expected workload of each unit as it relates

to oversight of Indian gaming has not been delineated. Although no historical workload data exists, the commission should develop a work plan that reflects these roles and responsibilities and anticipated workload activities. For example, for the licensing oversight division the commission should address the role of the unit, its specific responsibilities, and the expected activities of the staff (such as the number of licenses and employment applications to be reviewed and licensed machines to be verified). This information would give the Legislature a benchmark for assessing the commission's budget-year request. In addition, the commission needs to identify the specific responsibilities of the DOJ under the compacts and explain how the commission's activities will be coordinated with the department's. This information should be available to the Legislature for review before it approves the commission's budget. Pending receipt and review of this information, we withhold recommendation on the commission's budget-year request.

Legislature Needs to Be Informed of the Status of Indian Gambling Activities

We recommend the California Gambling Control Commission report to the Legislature during the budget hearings on the status of funds received for deposit into the Revenue Sharing Trust Fund and the Special Distribution Fund and various other information required to conduct appropriate oversight of Indian gambling.

Currently, there are 61 approved tribal-state compacts. These compacts lay out the legal relationship between the tribes and the state with respect to Indian gambling.

Gaming Machines Authorized Under Compacts. A significant provision of the compacts is the number of gaming machines (such as slot machines) that each tribe is allowed to operate and the total number of machines allowed throughout the state. Pursuant to the compacts, each tribe that signed a compact was required to report the number of gaming machines operated by the tribe as of September 1, 1999. Based on the 61 compacts, there was a total of 19,005 gaming machines in operation at that time. Figure 1 (see next page) summarizes the distribution of these machines.

Under the compacts, the maximum number of machines a tribe can operate is 2,000. The total number of machines that can be operated throughout the state is less certain. This is because the compact language concerning calculation of the total number of authorized machines is unclear and subject to different interpretations. It is essential to clarify this uncertainty for several reasons. First, the total number of machines will determine the overall magnitude of Nevada-style gambling that can occur on Indian land within the state. It is also needed in order for the com-

mission to carry out its state oversight role to determine if the tribes are complying with the level of gambling authorized in the compacts. Finally, the number of statewide machines determines the amount of money that will be distributed to certain tribes.

Figure 1	
Indian Gaming Machines In Operation September 1, 1999	
Number of Gaming Machines Per Tribe	Number of Tribes
0	23
1 to 350	16
351 to 750	13
751 to 1,250	7
1,251 to 2,000	2
Total	61

Revenue Sharing Trust Fund. This fund is to be distributed annually to each noncompact tribe in the amount of either \$1.1 million or an equal share of the fund should there be insufficient funds to provide the full \$1.1 million each. A noncompact tribe is defined by the compacts as a federally recognized tribe that either does not operate machines or is operating fewer than 350 machines. Payments to the Revenue Sharing Trust Fund are dependent on the number of *licensed* machines. The compacts state that a tribe may acquire and maintain a license to operate a gaming machine by paying into the Revenue Sharing Trust Fund, on a quarterly basis, as shown in Figure 2. In addition, a tribe must pay a one-time nonrefundable fee of \$1,250 per machine to obtain a license for the machine. These license fees also are deposited into the fund.

The commission is the trustee of the fund and is responsible for collection, deposit, and distribution of the fund. The compacts provide the commission no discretion with respect to use or disbursement of the fund.

Special Distribution Fund. This fund is subject to legislative appropriation for the following statewide purposes:

- Reimbursement for state regulatory costs associated with implementation of the compacts.
- Grants for gambling addiction programs.

- Grants to state and local agencies affected by tribal government gaming.
- Payment of shortfalls that may occur in the Revenue Sharing Trust Fund.
- Any other purpose specified by the Legislature.

Figure 2	
Revenue Sharing Trust Fund Annual Payment per Machine	
Number of Licensed Gaming Machines	Fee Per Machine Per Year^a
1 to 350	—
351 to 750	\$900
751 to 1,250	1,950
1,251 to 2,000	4,350

^a Fee is paid on the number of machines in each increment. For example, a tribe with 800 machines pays no fee on the first 350, then \$900 per machine on the next 400, and \$1,950 per machine on the last 50 machines.

Revenues to the fund are dependent on the number of machines in operation as of September 1, 1999. Beginning the last half of 2001-02, tribes must contribute from 0 percent to 13 percent of the average quarterly net win from these machines. Figure 3 (see next page) summarizes how these contributions are made based on the number of machines. The commission is responsible for collecting the appropriate amount of payments into this fund.

Commission Needs to Provide Status Report to the Legislature. In view of the issues outlined above—uncertainty surrounding the number of machines currently operating in the state, the maximum number of machines authorized under the compacts, and the status of the two funds established under the compacts—the commission, prior to budget hearings, needs to provide the Legislature a status report addressing the following:

Gaming Machines

- The maximum number of machines that can be operated throughout the state and the basis for determining that number.
- Current number of licensed machines and machines in operation for each tribe in the state.

- Description of procedure the commission will use to monitor both the number of licensed machines and the machines in operation.

Figure 3	
Special Distribution Fund Payments By Tribes Into Fund	
Machines Operating as Of September 1, 1999	Percent of Average Quarterly Net Win^a
1 to 200	—
201 to 500	7%
501 to 1,000	10
over 1,000	13
^a Fee is based on number of machines in each increment.	

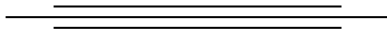
Revenue Sharing Trust Fund

- Commission procedures to collect revenues to the fund.
- Payment received to date from each tribe.
- Projected revenues to the fund.
- Amount of funds distributed (or expected to be distributed) to each tribe in 2000 and 2001.
- Basis for determining the amount distributed to each tribe.

Status of Special Distribution Fund

- Number of machines in operation on September 1, 1999, by tribe.
- Procedure the commission will use to determine the average quarterly net win on these machines.
- Projected revenues to the fund beginning in 2000-01.

Finally, we recommend that the commission report the above information to the Legislature on September 1, 2001 and March 1, 2002. This will keep the Legislature abreast of Indian gaming activities and allow a degree of legislative oversight.



SECRETARY OF STATE (0890)

The Secretary of State (SOS), a constitutionally established office, has statutory responsibility for examining and filing financial statements and corporate-related documents for the public record. The Secretary, as the chief elections officer, also administers and enforces election law and campaign disclosure requirements. In addition, the SOS appoints notaries public, registers auctioneers, and manages the state's archival function.

The budget proposes total expenditures of about \$78 million for the SOS in 2001-02. This is \$7 million, or 8 percent, less than estimated current-year expenditures. Expenditures from the General Fund total about \$39 million, a decrease of \$7 million, or 15 percent, compared to estimated current-year expenditures.

The lower General Fund expenditures reflect the fact that less money is needed than in 2000-01 to pay for state mandated local programs, particularly those establishing rules regarding elections. In addition to the General Fund reduction, the budget proposal also reflects a decrease in spending from the Business Reinvestment Fund.

On the other hand, legislatively enacted changes in the schedule of business fees are expected to generate additional fee revenue. These additional resources would be combined with previously accumulated fee revenues to finance a proposed information technology project to improve the office's business-related filing operations.

Business Program Computer Project Unauthorized

We withhold recommendation on a request by the Secretary of State for \$7.3 million to upgrade the office's computerized systems for managing corporate and other public records because the project has not yet been approved by the appropriate state agencies.

The budget proposes \$7.3 million from the Business Fees Fund for Phase II of the Business Programs Automation (BPA) project. This would include the development of electronic systems for various business filing programs administered by the SOS.

Business Programs Automation. Significant problems exist in the processing of corporate and other business registration programs for which the SOS is responsible. Those problems include inefficient processing of corporate filings and backlogs of tens of thousands of documents, difficulty in responding to requests for public records and information, and potentially serious mistakes in record keeping. To address these problems in 2000-01, the SOS proposed a two-phase BPA project to allow the department to provide accurate data, standardize and simplify the processing of business and security filings, reduce turnaround time, and file documents electronically. Phase I of the BPA project consists of developing a system which would accomplish these objectives with respect to Uniform Commercial Code filings only, due to the need to comply with recently-enacted legislation. Phase II of the BPA project would extend the system to other filing programs and acquire an integrated information system to support these programs.

The 2000-01 Budget Act provided \$8.5 million from the Business Fees and Business Reinvestment Funds for Phase I of the BPA project. This funding was provided under the condition that the Department of Information Technology (DOIT) and the Department of Finance (DOF) approve the appropriate project initiation documents. State administrative rules require these state agencies to review and approve new information technology projects before funds can be budgeted.

Department Does Not Have Approval to Implement Proposal. The DOF has approved Phase I of the BPA project but has not approved Phase II. This is due to the fact that SOS has not demonstrated that substantial business benefits would result from the implementation of Phase II. The SOS intends to submit a Feasibility Study Report for review by DOIT and DOF which will include plans for Phases I and II of the BPA project. Nonetheless, DOF included funding for this project in the proposed budget without reviewing the Feasibility Study Report. Budget bill language, however, indicates that these funds may not be encumbered until a Feasibility Study Report is approved.

Analyst's Recommendation. Without prejudice to the possible merits of this project, we withhold recommendation on the \$7.3 million funding request. We believe it is premature to appropriate funds for this project until the appropriate state agencies have agreed upon the scope and timetable for the project and determined the exact funding needed to proceed in the budget year. If those steps are accomplished before the SOS's bud-

get is heard in subcommittee, the Legislature would have the information it needs to decide the merits of the project. If those steps have not been completed by budget hearings, we would recommend that the Legislature not approve Phase II of the project at that time or adopt the following modified language (reflected in italics) with respect to the proposal, in budget bill Item 0890-001-0001:

Of the amount appropriated in this item, \$7,275,000 in Program 05, for costs to develop and implement the Business Programs Automation Project, may not be encumbered or expended until the Department of Information Technology and the Department of Finance approve a Feasibility Study Report *for Phase II of the Business Programs Automation Project, prepared in accordance with the State Administrative Manual and Statewide Information Management Manual. The funds shall be made available consistent with the amount approved by the Department of Finance, based upon the approved Feasibility Study Report.*

STATE TREASURER (0950)

The State Treasurer has a number of responsibilities related to the management of the state's financial assets. These responsibilities include:

- Providing custody for all money and securities belonging to or held by the state.
- Investing temporarily idle funds.
- Paying warrants and checks drawn by the State Controller.
- Preparing, selling, and redeeming the state's general obligation and revenue bonds.
- Preventing the issuance of unsound securities by irrigation, water storage, and certain other districts.

The Governors's budget proposes expenditures totaling \$23 million for the Treasurer's office in 2001-02, which represents a decrease of 3 percent from the current-year's expenditures. The request includes \$10.3 million from the General Fund, a 4 percent decrease from 2000-01. This decrease is primarily a result of elimination of excess vacant positions and a decrease in operating expenses.

Additional Funds Not Needed to Fill Vacant Positions

We recommend the Legislature delete \$244,000 under Item 0950-001-0001 because the budget already includes funding for the positions which are proposed to be filled. (Delete \$244,000 in Item 0950-001-0001.)

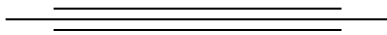
The Governor's budget includes a request for \$244,000 from the General Fund to fill two currently vacant positions to administer an expansion of the Time Deposit Program. However, the office already has authorization for the positions and its budget already includes the necessary funds to fill the positions. It is not clear if the office has redirected the funds previously approved by the Legislature. If this is the case, the

office should explain what was done and why resources are needed in that area. At this time, however, we recommend the Legislature delete \$244,000 in Item 0950-001-0001.

Modified Workload Does Not Justify More Staff

We recommend the Legislature delete \$351,000 in Item 0950-001-0001 because the office has not justified an increase in workload. (Delete \$351,000 in Item 0950-001-0001.)

The Governor’s budget includes a request for \$351,000 from the General Fund and four new positions to manage a variable interest rate general obligation bond program as authorized by Chapter 522, Statutes of 1999 (SB 997, Brulte). The program is an alternative financing option instead of the traditional fixed interest rate program. The Treasurer indicates a need for additional staff in order to administer the program. However, it is not clear that additional workload will be generated or that additional resources are necessary. The Treasurer will not be issuing a significantly larger amount of bonds. As variable rate bonds are issued, fixed rate bond issuance will decrease, resulting in minimal, if any, increase in workload. Consequently, some of the resources currently directed to the fixed rate program can be used for the variable rate program. Therefore, we recommend the Legislature delete \$351,000 in Item 0950-001-0001.



DEPARTMENT OF CONSUMER AFFAIRS (1110-1600)

The Department of Consumer Affairs is responsible for promoting consumer protection while supporting a fair and competitive marketplace. The department includes 28 semi-autonomous regulatory boards, commissions, and committees that regulate various professions. These boards are comprised of appointed consumer and industry representatives. In addition, the department has ten bureaus and programs that regulate additional professions which are statutorily under its direct control.

Expenditures for the support of the department and its constituent boards are proposed to total \$375 million in 2001-02, an \$18 million increase from the current year. Several incremental increases across the boards contribute to this increase, the largest being the \$2 million imaging and workflow automation systems project at the Contractors State Licensing Board. Included in the budget-year total are \$2 million in expenditures from the General Fund for support of the Athletic Commission and various public outreach programs.

Smog Check Update

We withhold recommendation on the Bureau of Automotive Repair's budget (Items 1111-002-1421 \$91.6 million and 1111-002-0582 \$47.5 million) pending receipt and review of information concerning (1) progress toward meeting requirements in the State Implementation Plan's proposed changes in the smog check program and (2) the expenditure of current-year funds and the results from spending these funds.

Background. The original framework for a statewide biennial Smog Check program was implemented in 1984 by the Bureau of Automotive Repair (BAR). Under this program, both smog (emission) testing and needed vehicle repairs were permitted at any privately owned smog test-and-repair station. The 1990 federal Clean Air Act amendments required a somewhat different smog program in states with the worst air

quality, including California. Federal regulations define a region's air quality in one of two ways:

- A geographic area that meets or exceeds a national ambient air quality standard is referred to as an *attainment area*.
- An area that does not meet this standard is a *nonattainment area*. These nonattainment areas are the focus of the federal Environmental Protection Agency (EPA).

The Smog Check program components as agreed to by California and the federal government are laid out in the State Implementation Plan (SIP).

Basics on the SIP. The SIP was adopted by the Legislature in 1994 and approved by the federal EPA in 1996. The SIP divides California into three types of program areas based on air quality—enhanced, basic, and change of ownership. The smog test required varies by area. In the enhanced areas vehicles are tested on a dynamometer. This device acts like a treadmill and allows the car to be tested under road-like (load tested) conditions. In the basic areas, a simple tail-pipe emission test at two idle speeds is used (no load) without simulating road conditions. Enhanced and basic smog checks are required every two years. The change of ownership areas only require a tail-pipe emission test when a vehicle is sold.

To monitor California's performance, the SIP includes performance standards and deadlines for implementation of key SIP components. Essentially, the SIP calls for the entire state to meet federal air quality standards by 2010.

In addition to the requirement in the SIP, the bureau administers several smog-related programs that have been adopted by the Legislature. These other nonmandated programs are the Low-Income Repair Assistance Program and the Voluntary Retirement Program. The state's Smog Check program is funded from two funds—the Vehicle Inspection Repair Fund (VIRF) and the High Polluter Repair and Removal Account (HPPRA). The VIRF funds the SIP-mandated program and the HPPRA funds the other programs.

Evaluation for Federal EPA. The SIP required the state (the bureau, in conjunction with the Air Resources Board [ARB]), to submit an evaluation of the Smog Check program to the federal EPA in February 2000. In July 2000, the ARB released a report evaluating the program. The evaluation indicates that the current enhanced inspection and maintenance improvements under the Smog Check program have fallen far short of the target requirements called for in the SIP. For example, the program had only achieved 60 percent of the hydrocarbon (HC) reductions and 59 percent of the nitrogen oxide (NOx) targets called for under the SIP by summer 1999. In the evaluation sent to federal EPA, the state indicated that

several changes would be made to the program in an attempt to close this gap between the targets and actual performance. These changes and the schedule for BAR to implement them are shown in Figure 1.

Figure 1	
Changes in Smog Check Program	
	Implementation Schedule
Lower nitrogen oxides (NOx) cut points^a (enhanced only)	September to December 2000
Loaded mode testing, heavy-duty trucks (enhanced only)	
Develop test protocol and select cut points	March 2001
Adopt regulations and update test equipment	August 2001
Implement heavy-duty testing	December 2001
Improved evaporative emission testing (enhanced and basic)	
Liquid leak test:	
Develop liquid leak test protocol	September 2000
Adopt regulations and notify stations	February 2000
Implement program	September 2000
Low pressure test:	
Develop and evaluate test protocol	September 2000
Adopt regulations and update test equipment	December 2001
Implement test	June 2002
Direct more vehicles to Test-Only or other high-performance stations (enhanced only)	
Direct 20 percent	September 2000
Direct 30 percent	December 2001
Direct 36 percent	December 2002
Use remote sensing to help identify high-emitting cars	
Complete pilot program design	March 2001
Start pilot program	September 2001

^a A cut point is the emission level above which the vehicle fails. A lower cut point results in more vehicles failing.

In addition to program changes identified in Figure 1, the state report indicated that further changes in certain regions of the state would

be necessary in order to meet the 2005, 2008, and 2010 targets required in the SIP. The report also indicated that these changes could involve legislative action to increase the number of vehicles subject to the Smog Check program. These changes would involve: (1) removing the rolling 30-year model year exemption (currently, pre-1974 vehicles are exempt and beginning January 2003 all vehicles 30 or more years old are exempt); and (2) extending the program to all eligible vehicles registered in a nonattainment region that is already subject to enhanced smog check requirements (currently, only urbanized areas of 50,000 or more in these regions are subject to these requirements).

Given the problems the state has encountered meeting the SIP requirements and the proposed changes, the bureau should report to the Legislature on the following:

- The status of each of the proposed changes.
- The anticipated cost associated with each change.
- The anticipated contribution towards SIP goals for each change and how BAR determined these values.
- The status and results of all existing SIP elements of the Smog Check program.
- Program and administrative costs in the current year and budget year for each element of the element.

Consumer Assistance Program. As mentioned above, the Legislature enacted several smog-related programs that are not mandated in SIP. These consumer assistance programs include:

Income-Eligible Repair Assistance

- Vehicle owners income must be less than or equal to 185 percent of federal poverty guidelines.
- Owners must provide a \$20 copay on emissions-related repairs.
- The state pays up to \$500 towards emission-related repairs.

Repair Assistance for Vehicles Directed to Test-Only Stations

- No income test for vehicle owner to receive assistance.
- Vehicle must be directed to a Test-Only inspection station.
- Vehicle owner must provide a \$100 copay on emissions-related repairs.
- State pays up to \$500 toward emission-related repairs.

Vehicle Retirement

- Generally open to all vehicle owners.
- Eligible vehicles include passenger cars, light-duty or medium-duty trucks with a gross vehicle weight of less than 8,500 pounds.
- Vehicle must have failed the smog check.
- Vehicle must have been continuously registered as an operable vehicle with DMV for past 24 months prior to current registration expiration.
- Vehicle must be operable at the time it is retired. State will pay vehicle owner \$1,000 to retire the vehicle.

The *Supplemental Report of the 2000-01 Budget Act* requires BAR to submit a quarterly report on the performance of these programs. Figure 2 summarizes the results from the first-quarter report for 2000-01 (second-quarter results were not available when this analysis was written).

Figure 2			
Consumer Assistance Program			
<i>2000-01 First Quarter Activities</i>			
	Income Eligible Assistance	Test-Only Assistance	Vehicle Retirement
Individuals participating	918	137	942
Payments to vehicle owners	\$298,000	\$46,000	\$942,000
Emission Reductions (tons per year)^a			
HC ^b		8	37
NOx ^b		4	10
CO ^b		119	298

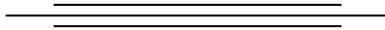
^a The BAR could not provide separate reduction data for income eligible and test-only.
^b HC—hydrocarbons; NOx—nitrogen oxides; CO—carbon monoxide.

We recommend BAR report to the Legislature during budget hearings on the following:

- The BAR’s administrative costs for each program in the current year.
- The BAR’s most recent information for each program detailing (1) participation, (2) payments to vehicle owners, and (3) emission reductions.

- An assessment—from a cost per ton of emission reduction perspective—of the cost-effectiveness of each program’s contribution toward SIP targets for HC, NO_x, and CO.

The Legislature needs, at a minimum, the information discussed above in order to assess the effectiveness of each element of the Smog Check program and to determine the appropriate level of funding for each. Consequently, we withhold recommendation on BAR’s budget pending receipt and review of this information.



DEPARTMENT OF FAIR EMPLOYMENT AND HOUSING (1700)

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

The budget proposes expenditures of \$22.4 million (\$18.3 million from the General Fund and \$4.1 million federal funds) for support of the department in 2001-02. This represents an increase of \$363,000 (1.6 percent) over estimated current-year expenditures.

Insufficient Justification of Increased Funding

We recommend the Legislature delete a total of \$151,000 and two positions because the department has not provided workload information for the requested positions. (Delete \$151,000 in Item 1700-001-0001.)

No Workload Data for Restrictive Covenant Program. The budget includes \$151,000 from the General Fund for two positions to administer a new restrictive covenant identification service, as authorized by Chapter 291, Statutes of 1999 (AB 1493, Nakano). Restrictive covenants under this program are those that limit property ownership based on race, color, religion, sex, familial status, marital status, disability, national origin, and ancestry, and violate the state's fair housing laws. Under this program, the department, upon request by property owners, reviews property deeds to determine if they contain racially restrictive covenants. According to the department, caseload tracking and processing will need to be developed for this activity. However, the department has provided no workload data indicating the number of requests expected under the pro-

gram or the amount of time it will take to process the requests. Until the department begins administering the program, it is not clear that additional staff or resources are required. We recommend the department implement the program using existing resources during the budget year and evaluate the workload during that time. If sufficient workload develops, a future request for staff and resources may be justified. Consequently, we recommend the Legislature delete \$151,000 and two positions in Item 1700-001-0001.

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FRANCHISE TAX BOARD (1730)

The Franchise Tax Board (FTB) is one of the state's major tax collecting agencies. The board's primary responsibility is to administer California's Personal Income Tax and Bank and Corporation Tax laws. The board also administers the Homeowners' and Renters' Assistance program, the Political Reform Act audit program, and the Household and Dependent Care Expense Credit (HDCEC) program. In addition, the board administers several nontax programs, including collection of child support and court-ordered payments. A three-member board—the Director of Finance, the Chair of the State Board of Equalization, and the State Controller—oversees the department. A board-appointed executive officer is charged with administering the day-to-day operations.

The 2001-02 *Governor's Budget* proposes \$427 million (\$385 million General Fund) and 5,755 positions in support of the FTB's operations. The total amount is \$11 million and 118 positions less than the current year. The main changes are (1) position reductions from implementing e-filing and from the termination of the Student Loan Collection pilot program, (2) an increase in resources for processing and fraud investigation activities associated with the HDCEC program, and (3) the elimination of some vacant positions.

California Child Support Automation System Project

We withhold recommendation on funding for the Franchise Tax Board's California Child Support Automation System. We further recommend that the board, in conjunction with the Department of Child Support Services, submit an updated budget proposal to the Legislature that is consistent with its latest report to the federal Administration of Children and Families.

Chapter 479, Statutes of 1999 (AB 150, Aroner), required FTB to act as the Department of Child Support Services' (DCSS) agent for the procure-

ment, development, implementation, and maintenance of the California Child Support Automation System (CCSAS). (For a comprehensive discussion of these developments, see our report entitled, *Child Support Enforcement: Implementing the Legislative Reforms of 1999*, issued January 27, 2000.)

The 2001-02 Governor's Budget proposes no increase in the current \$19.5 million support level for the project (\$4.8 million from the General Fund and \$14.7 million in federal reimbursements).

Proposal Inconsistent With Report to the Federal Government. In November 2000, the board provided a Planning Advance Planning Document Update (PAPDU) regarding this project to the Administration of Children and Families (ACF). The ACF requires a state to submit this document when requesting additional funds or a schedule change to a federally funded automation project.

According to the PAPDU, the board currently estimates budget-year funding needs for the project of \$29.7 million (\$7 million from the General Fund and \$22.7 million in federal reimbursements). In addition, the PAPDU reports a schedule extension of five months to account for the additional time needed to develop the project charter and define the requirements for the procurement proposal. Once that is done, the procurement for the new statewide system is expected to be completed by August 2002.

Board Should Explain Budget Inconsistencies. Based on our review of the PAPDU, the Governor's budget proposal for this project (\$19.5 million), when compared to information in the PAPDU (\$29.7 million), is underfunded by \$10.2 million (\$2.2 million General Fund and \$8 million federal reimbursements). In addition, the PAPDU's project schedule is inconsistent with the last information provided to the Legislature. For these reasons, we recommend that the board, in cooperation with DCSS, provide to the Legislature prior to budget hearings a project and schedule update, an explanation of budget inconsistencies, and a revised budget proposal reflecting the funding required in the budget year.

Child Support Collection Program

Our review of the board's California Arrearage Management Project indicates that the project (1) has exceeded its original costs and time frame for implementation, (2) did not receive federal funding as originally anticipated, (3) may adversely affect implementation of the statewide California Child Support Automation System thereby continuing federal penalties related to administrative costs, (4) may ultimately require development of another statewide arrearage system, and (5) resulted in funding redirections and revised contracting strategies of which the Legislature was not notified. For this reason, we recommend that the

board explain at budget hearings the reasons it did not advise the Legislature of the denial of federal funds and the resultant General Fund redirection and contracting revisions.

In addition, we recommend the Legislature consider amending existing law to delay a portion of the board's arrearage collection time frame. We further recommend that the board examine and report to the Legislature, prior to budget hearings, on the costs associated with deferring the arrearage collection time lines.

The Governor's budget proposes \$11.2 million to continue project development efforts for its child support arrearage collection system, the California Arrearage Management Project (CAMP). This is the same amount as in the current year. The purpose of this system is to collect unpaid and overdue child support known as "arrearage."

Program History. In 1993, the board began a child support delinquency collection pilot project in six counties and expanded the collection program to all counties two years later. The board was responsible for collecting child support payments that were delinquent by 90 days or more. County district attorneys could also choose to have the board collect payments that were delinquent by 30 days or more as well as current support payments.

Single Statewide Automation System. The ACF required the state to develop a single statewide system by 1997 for all of its child support enforcement activities that met specific information technology and program requirements. One of these requirements was that the statewide system be able to perform arrearage collections as part of its overall collection functions. For reasons unrelated to arrearage collection activities, the state was unsuccessful in implementing the single system known as the Statewide Automated Child Support System. As a result, the federal government began imposing annual penalties by reducing federal funds for administration of the state's child support enforcement program. This year's reduction is expected to be \$114 million and is expected to increase until such time as the state is able to implement the new CCSAS system.

Restructured Arrearage Collection Program. Chapter 478, Statutes of 1999 (AB 196, Kuehl) and Chapter 480, Statutes of 1999 (SB 542, Burton), assigned a number of additional child support collection responsibilities to the board, as summarized in Figure 1, and required the board to phase these in by December 31, 2002. At the time the legislation was enacted, the board had not determined the nature of the relationship between arrearage collection and the CCSAS system. The board, therefore, decided to develop CAMP as a separate system to meet the requirements and time frames of the new state legislation. Ultimately, however, the state's

collection function will need to be included in the CCSAS in order to meet federal certification requirements for a statewide automation system.

Figure 1

**Franchise Tax Board
Responsibilities Under
New Child Support Collection System**

- Handle all cases over \$100 which are more than 60 days in arrears. This is expected to double the department's caseload to approximately one million cases.
- Design and implement a computerized database to centralize information regarding each case.
- Establish a customer information center or network to respond to debtor inquires and disputes.
- Contract with third parties, where necessary, to locate debtors and debtor assets.
- Give priority to collection of child support debt. For example, if a debtor has both a child support delinquency and a personal income tax delinquency, the board is to collect the child support delinquency first.

Board Seeks Federal Funding for CAMP Development. In July 2000, the board submitted a request to ACF for an additional \$3.7 million in federal funds for CAMP. This request also indicated a need for an additional \$1.8 million of state funds in the budget year. The board reported to ACF that the total cost for CAMP was estimated to be \$59 million.

In October 2000, ACF denied all federal funds requested by the board for CAMP. The ACF's letter stated "we continue to urge California to concentrate its system development efforts on implementation of a statewide CSE [child support enforcement system] and we find that CAMP, as proposed is not an interim enhancement to an existing system, but in fact a new system development . . . We urge the State to focus its full efforts on accelerated planning, development, and implementation of a statewide system. Federal Funding Participation will only be provided for new system development in the context of a statewide system."

In response to the federal funding denial, we understand that the board has redirected General Fund monies during the current year to continue the CAMP development effort. At the time this analysis was prepared, the board had not informed the Legislature of the federal funding denial or of this redirection.

According to the Governor's budget, the board is now pursuing a "performance-based contract" to meet the arrearage collection requirement. This contracting approach, which the board has used in its tax collection operations, allows the board to defer vendor payments until the automation system is operational and is achieving an agreed upon level of benefits—generally increased revenues. When the state achieves that benefit level, it begins to pay the vendor.

Concerns With State's Pursuit of CAMP. Our review of the implementation history of CAMP raises a number of concerns.

- ***The CAMP Is More Costly Than Originally Expected.*** Prior to the final passage of Chapter 478 and Chapter 480, the board estimated the cost for a collection arrearage system to be \$12 million. Since then, that estimate has been revised upward. According to Department of Finance's (DOF) approval letter for CAMP, the total project costs were estimated to be \$35 million in February 2000. Now, according to the information reported to ACF, the board believes the total project costs to be \$59.7 million. While some cost increases are understandable, this is almost double the cost reported to the Legislature during last year's budget hearings.
- ***The CAMP Is Taking Longer to Implement Than Originally Expected.*** In addition to increased costs, the amount of time required to implement the system also is increasing. According to DOF's approval letter for CAMP, the system was to be operational by August 2002. The information reported to ACF, however, states the board will *begin* county transitions in April 2002 with full county operation occurring in December 2003. This means the state will be unable to meet the legislative mandate of full county transition by December 2002.
- ***Federal Government Appears Unwilling to Fund CAMP.*** The response the board got from ACF when it denied funds for CAMP indicates the federal government views CAMP as a separate system that is not a part of the state's efforts to achieve a statewide child support collection system.
- ***The CCSAS Must Include Arrearage Collection Functions to Satisfy Federal Requirements.*** It is important for the state ultimately

to meet the federal certification requirements for CCSAS in order to eliminate federal administrative penalties. To meet these requirements, the automated arrearage collection capability will need to reside within CCSAS. Implementation of CAMP, which is designed to be a stand-alone system, will prevent the state from receiving federal certification and, thus, have no impact on reducing federal penalties. This in turn would make it necessary for the state to discontinue CAMP and develop a second arrearage collection system to be incorporated in CCSAS.

- ***Board Has Made Significant Funding Redirections and Developed a New Contracting Strategy Without Notifying the Legislature.*** As noted earlier, the board has failed to notify the Legislature of its failure to receive federal funds as anticipated, and its subsequent redirection of state General Fund monies to replace the federal funds. The board also has not provided information to the Legislature regarding its new contract strategy, nor has it received approval from Department of Information Technology, DOE, and the Department of General Services to pursue this strategy.
- ***The CAMP Could Limit Technology Direction of Single Statewide System.*** Since CAMP is expected to be operational (in 2003) two years before full implementation of CCSAS (in 2005), it could set the technology direction for the new statewide automation system. This is due to the fact that CAMP would need to be incorporated into the CCSAS to meet federal certification requirements. To do this, however, the board would need to include technical specifications in its procurement for the single statewide system to ensure compatibility with CAMP. This strategy would be inconsistent with those provisions of Chapter 479 which require that the statewide system:
 - Be capable of implementation by multiple vendors.
 - Offer the greatest chance of achieving program and project success.
 - Meet program specifications as opposed to technology-specific specifications.

LAO Recommendations. Given the issues noted above, we recommend that the Legislature take two sets of action. First, we recommend that the Legislature require the board to report at budget hearing on the reasons why it did not advise the Legislature of the denial of federal funds, its redirection of General Fund monies, and its revised contracting strategy. Second, we recommend that the Legislature consider:

- ***Deferring Legislative Time Frame for Implementing Arrearage Collections Activities.*** Specifically, we believe it would be better to defer the deadline for transitioning counties to the board's arrearage collection program and instead have the counties begin using the board's program once they transition to the single statewide system. We believe this offers the best solution to the automation and funding issues noted above. In addition, it allows the state to focus solely on developing the single statewide system which is the only child support automation effort that will eliminate the federal penalties.

According to the board, counties are to begin transitions to the new CCSAS system in 2003 with full implementation occurring in 2005. The CCSAS time frame corresponds relatively closely to the latest CAMP schedule. Implementing the board's arrearage collection program to correspond with CCSAS implementation would mean an overall delay of at most two years.

- ***Requesting Information on Costs Associated With Deferring Child Support Collection Activities.*** Before the Legislature acts on deferring the arrearage collection time frames contained in existing law, we recommend that the board report to the Legislature prior to budget hearings on the costs associated with that deferral. This report should include what arrearage collection activities could be implemented now without the CCSAS system, the impact of redirecting existing resources to other child support activities, and other costs associated with deferring existing arrearage collection requirements.

The Household and Dependent Care Expense Credit

We withhold recommendation on the board's request for \$3.8 million (General Fund) and 64.4 personnel-years for processing and fraud detection associated with implementation of the Household and Dependent Care Expense Credit program pending receipt of additional information on actual filing for tax year 2000.

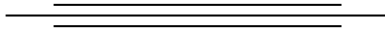
The Governor's budget proposes \$3.8 million and 64.4 personnel-years (PYs) for the FTB to cover increased processing and fraud prevention activities associated with the implementation of Chapter 114, Statutes of 2000 (AB 480, Ducheny).

Program. Chapter 114 established the HDCEC. This tax credit, which became effective beginning tax year 2000, allows for a refundable credit to be taken as a percent (depending on income level) of household and dependent care expenses incurred as necessary costs to sustain employ-

ment. The credit is tied to the federal nonrefundable credit known as the Child and Dependent Expense credit. The credit is primarily limited by the taxpayer's California adjusted gross income, ranging from 63 percent of the allowable federal credit for adjusted incomes of \$40,000 or less to 42 percent for incomes up to \$100,000. The credit is not available for incomes over \$100,000 and the maximum allowable credit is \$907.

The FTB's Concerns Over Fraud. Based on the board's experience with the Renter's Credit and federal experience with the Earned Income Credit, the board is concerned that there could be substantial fraud related to income tax filings under the HDCEC program. Based on these programs, the board estimates the possible losses from fraudulent filings could range from \$7.2 million to \$104.6 million. Since the HDCEC is tied to the federal Dependent and Child Expense credit, and the federal forms must accompany the state tax filing, it would seem reasonable for the board also to assess the fraud experience in this federal program when estimating the potential fraud under HDCEC. In any case, tax filings for 2000 will be the first year of claims under HDCEC. Consequently, the board should be in a better position to assess the impact of this program as the 2000 tax filings are received and reviewed.

The board should undertake this review, as well as assess fraud activity in the federal nonrefundable program, and report its findings to the Legislature during the budget process. These data should provide a reasonable measure of the workload requirements for the HDCEC. Thus, we withhold recommendation on the \$3.8 million and 64.4 PY request pending receipt and review of this information.



DEPARTMENT OF GENERAL SERVICES (1760)

The Department of General Services (DGS) is responsible for providing a broad range of support services to state departments and performing management and oversight activities related to these services. It provides these services through three programs: statewide support, building regulation, and real estate services.

The Governor's budget proposes total expenditures of \$845 million from various funds (including \$62.4 million from the General Fund) to support the activities of DGS in 2001-02. This is a General Fund decrease of \$7.3 million, or 10 percent, below estimated current-year expenditures.

Building Regulation Services. Proposed budget-year expenditures for these services are \$36.1 million, or \$0.3 million more than the current-year level. The major change in this program budget is the addition of 11.4 personnel-years (PYs) and \$0.9 million to meet workload requirements of Chapter 407, Statutes of 1998 (SB 50, Greene) in the Office of Public School Construction.

Real Estate Services. Proposed budget-year expenditures for these services are \$397.4 million, or \$12.1 million more than the estimated current-year level. Major increases in the budget include:

- \$1.9 million in the Asset Planning and Enhancement Branch to fund studies for the sale or disposition of various properties.
- 22.3 limited-term PYs and \$3.2 million in the Professional Services Branch to fund construction supervision and inspection on the Delano II prison construction project.
- 104.9 PYs and \$3.7 million in the Building and Property Management Branch to provide janitorial services.

- \$2.4 million in the Building and Property Management Branch to fund deferred maintenance projects at the Public Utilities Commission building in San Francisco.
- \$2.7 million in the Building and Property Management Branch to perform deferred maintenance projects at various DGS-owned facilities.

These increases were offset in part by a reduction of \$5.7 million and 57 PYs in the Building and Property Management Branch as a result of not providing property management services at the new CalEPA leased facility in Sacramento.

Statewide Support Services. Expenditures for statewide support services are \$386.5 million in the budget year which represents an increase of \$20.7 million, or almost 6 percent, over estimated current-year expenditures. The amount includes several small program increases and reductions. The largest requested increase is \$31.7 million for local assistance to enhance 911 wireless services.

BUILDING REGULATION SERVICES

Positions in Division of State Architect (DSA) Should Be Reported in Budget

We recommend the Legislature adopt supplemental report language directing the Department of Finance to report all positions in the Division of the State Architect in the Governor's budget.

The 2000-01 *Salaries and Wages Supplement* (the latest one available) indicates that 17.5 positions were proposed in DSA. The DSA has informed us, however, that it currently has 163 authorized positions. The division explains that the reason it does not report approximately 140 positions is because they are funded out of the Public School Planning, Design, and Construction Review Revolving Fund from fees paid by school districts for review of plans for school building construction, and that these funds are continuously appropriated under Government Code Section 17301. It is not clear to us that the fact positions are funded from continuously appropriated funds is justification for not reporting them in the Governor's budget. The Legislature needs this information so it can understand the number of employees in each state organization and make informed decisions on budget proposals. We therefore recommend the Legislature approve supplemental report language directing the Department of Finance (DOF) to report all au-

thorized positions each year in the *Salaries and Wages Supplement* to the Governor's budget.

Provision for Loan to Support DSA Is Not Needed

We recommend deletion of budget language authorizing a loan of up to \$4 million from the Service Revolving Fund to the Public School Planning, Design, and Construction Review Revolving Fund for support of the Division of the State Architect because it is not needed. (Delete Item 1760-001-0066, Provision 3.)

The budget proposes authorization for the Director of DGS to loan up to \$4 million from the Service Revolving Fund to the Public School Planning, Design, and Construction Review Revolving Fund ("plan review fund") to meet the cash flow needs of DSA. Revenue to the plan review fund normally comes from fees charged by DSA for checking school building plans as required by the Field Act (Education Code Sections 17281 et seq.). The fund supports the engineering and construction inspection positions in DSA that perform this oversight work. A provision similar to this proposal was approved by the *1995-96 Budget Act* and has been approved by each subsequent budget act.

We question the need for this provision for two reasons. First, it has not been needed in the past. The provision was first approved when the amount of school construction was less than it is today and it was questionable whether the condition of the plan review fund was adequate for the cash flow needs of DSA. The authorization, however, has never been used. As there is now more school building construction taking place and more revenue flowing to the plan review fund, its condition is sufficient for the needs of DSA.

Second, we question the potential use of the Service Revolving Fund to support DSA's school building plan review and inspection staff. If the amount of school construction should decline in the future, staffing levels in the division should be reduced accordingly. For these reasons, we recommend that the loan provision be deleted.

REAL ESTATE SERVICES

Cost—and Cost of Living—Should Be Considered When Locating State Offices

The cost for the state to lease office space in the Bay Area is considerably higher than elsewhere in California, as is the cost of housing for state employees. We recommend the Legislature direct the Department

of General Services to relocate state offices in high-cost areas that are not needed to serve the local community to less expensive areas when the current leases can be canceled.

The state owns over 1 million gross square feet (gsf) of office space in San Francisco and leases over 300,000 gsf in privately owned buildings. Agencies occupying state-owned buildings are not affected by the local rental market but those in leased space are. Recent leases executed by DGS for office space in the Bay Area—especially San Francisco—have been at rates that are high compared to those for similar office space elsewhere in the state. When offices are needed in San Francisco to serve the public in that community or are required by law to be located there, these high costs are basically unavoidable. But if it is not necessary to have state employees working in leased space in San Francisco, the state can realize savings by locating those state offices elsewhere, or relocating them to state-owned buildings in San Francisco.

Figure 1 summarizes some recent leases in San Francisco. At the time these leases were proposed (during the first six months of 2000), the DGS estimated that comparable office space was available in San Diego, Los Angeles, and Sacramento for between \$1.80 and \$2.60 per net usable square foot (nurf). Thus, the state paid between 50 percent and 150 percent more to lease office space for these agencies than may have been necessary if their offices had been located in other cities.

Figure 1

**Recent Office Leases in San Francisco
Executed by Department of General Services**

Tenant Agency	Size of Office ^a	Initial Lease Rate ^b	Firm Term of Lease (Years)	Lease Rate at End of Term ^b
Department of Insurance	63,002	\$3.98	9.5	\$4.75
Coastal Commission	28,036	4.08	9.5	4.87
San Francisco Bay Conservation and Development Commission	19,032	4.56	10.0	4.97

^a Net usable square feet (nurf).
^b Dollars per nurf per month.

The department reported in December 2000 the range of market rates for office leases in different cities shown in Figure 2 (see next page). The

figure shows that office lease costs in San Francisco are now 50 percent to over 400 percent more than in these other cities.

Figure 2	
Current Market Range for Office Leases	
City	Market Range (per net usable square foot)
San Diego	\$2.20 to \$2.75
Los Angeles	1.75 to 2.50
Sacramento	1.50 to 3.00
San Francisco	4.50 to 8.00

It may not have been necessary for the agencies shown in Figure 1 to be located in San Francisco. Specifically:

- The law requires that the Insurance Commissioner maintain offices in San Diego, Los Angeles, Sacramento, and San Francisco, but beyond this requirement the law does not mandate that any specific employees or activities be located in these cities. Information provided by DGS at the time indicated that of the 212 Department of Insurance (DOI) employees in the San Francisco office, ten were employed in the Commissioner's office. Some, if not many, of the remaining 202 employees may have been able to perform their functions in another less costly city. This would reduce the amount of space needed in San Francisco, which would have reduced office lease costs for the state.
- The law requires that the headquarters of the Coastal Commission be located in a coastal county, but otherwise does not specify any particular county. Thus, headquarters of the commission could be relocated to another, lower-cost coastal county, which would make it unnecessary to rent office space for the commission in San Francisco.
- The San Francisco Bay Conservation and Development Commission offices clearly need to be located in the Bay Area, but the law requires they be located in San Francisco. Thus, under current law there is little flexibility for the state to reduce lease costs for the commission. But if the law were amended to give the state

the flexibility to locate commission offices in any Bay Area county, savings on lease costs might be realized.

Cost of Housing for State Employees. When locating state offices, there is also the issue of living costs for state employees. Among the most important of these is the cost of housing. Figure 3 shows for major metropolitan areas the median sale prices of single family detached homes and the percentage of California families that could afford a median priced home. With San Francisco home prices two to three times higher than other urban areas, it is not surprising that many state employees find it difficult to live and work in San Francisco.

Figure 3

Housing Prices and Affordability

Metropolitan Area	Median Sale Price, Single Family Detached Home (November 2000)	Percentage of California Families That Could Afford Median-Priced Home (October 2000)
San Diego	\$280,490	23%
Los Angeles	228,800	35
Sacramento	154,890	52
San Francisco	477,360	11

State Agencies Currently Leasing Office Space in San Francisco. Figure 4 (see next page) shows state agencies currently leasing 10,000 nusu or more of office space in San Francisco and the date the state’s firm commitments under the lease expire.

As previously discussed, DGS has recently signed long-term leases for the California Coastal Commission, DOI, and San Francisco Bay Conservation and Development Commission offices shown in Figure 4 and the state cannot relocate these agencies in the near term. In the other cases, however, the department should endeavor to relocate the state functions unless the function (1) is necessary to serve the local community or (2) is required by law to be in San Francisco.

Because of the high cost of leasing office space and the high cost of living for state employees in San Francisco, we recommend the Legislature direct DGS to:

- Relocate state functions currently occupying leased office space in San Francisco to state-owned buildings in San Francisco or to

less expensive locations when the current leases allow the state to cancel the lease unless locating the function in San Francisco is necessary to serve that local community or is required by law.

- Notify the Joint Legislative Budget Committee 30 days prior to entering into any lease for office space in San Francisco.

Figure 4

State Agencies Leasing 10,000 Net Usable Square Feet Or More of Office Space in San Francisco

Department or Agency	Space Leased (nurf)	Lease Expiration Date ^a
California Coastal Commission	28,036	April 2010
Corrections	10,469	May 2002
Employment Development		
185 Berry Street	21,952	November 1998
3120 Mission Street	35,833	April 2001
1625 Van Ness Avenue	20,000	May 2006
1700 California Street	7,025	August 2001
Financial Institutions	23,954	April 1996
Habeas Resource Center	15,323	July 2003
Health Services	28,135	June 1997
Insurance	63,002	April 2010
Justice	25,525	March 2003
State Public Defender	19,343	September 1999
Rehabilitation	18,570	November 1997
San Francisco Bay Conservation and Development Commission	19,032	March 2010
Transportation	14,823	July 1997

^a Date firm term expires, after which lease is extended but can be canceled upon giving notice as required by lease agreement.

Reagan Building Costs Should Be Deleted From Statewide Building Rental Rate

We recommend the Legislature approve budget bill language directing the Department of General Services to treat the Ronald Reagan Building in Los Angeles the same as other bond-funded buildings by excluding it from the statewide standard building rental rate and adjust all affected building rates accordingly.

The DGS charges state agencies that are tenants in most DGS-owned buildings a statewide “standard building rental rate” to cover the cost of operating and maintaining those buildings. In calculating the standard rate, with certain exceptions, the department totals all operation and maintenance expenses for DGS-owned buildings statewide and divides that total by the total nusef of space occupied statewide by agencies in DGS-owned buildings to arrive at a single dollars-per-nusef-per-month rate.

Excluded from this calculation are the buildings shown in Figure 5. These buildings have *individual* building rental rates calculated and charged to tenant agencies because, in addition to operation and maintenance costs, these buildings were constructed with funds from lease-payment bonds whose repayment must be amortized by rent payments.

Figure 5	
Building Rental Rates for DGS-Owned Buildings Financed With Lease Payment Bonds	
Building	2000-01 Office Space Building Rental Rate^a
Elihu Harris, Oakland	\$2.81
Junipero Serra, Los Angeles	1.80
Cal Tower, Riverside	2.14
Mission Valley, San Diego	— ^b
Attorney General, Sacramento	1.83
Civic Center, San Francisco	3.46

^a Dollars per net usable square foot per month.
^b Rates not available because construction has just recently been completed.

One building financed by lease payment bonds, however, *is* included in calculation of the standard building rental rate. This is the Ronald Reagan Building in Los Angeles. Bond debt and insurance on the Reagan building adds almost \$18 million per year to the expenses used to calculate the standard building rental rate, which increases the rent charged all state agencies in most DGS-owned buildings from about \$1.52 to \$1.83 per nusef per month.

We recommend that the state treat the Reagan building in the same manner as the other seven lease payment bond-financed buildings shown in Figure 5. This would result in a reduction of about 30 cents per nusef

per month in the standard building rental rate charged tenant agencies in most other DGS-owned buildings.

In order to have building rental rates more accurately reflect the true cost of owning and operating state buildings we recommend the Legislature adopt budget bill language under Item 1760-001-0666 directing DGS to make the changes described above and modify Section 4.60 of the budget bill to allow the DOF to make the appropriate changes in the affected departments' budgets.

Asset Enhancement Consultant Services and General Fund Loan

We recommend deletion of a proposed \$1.1 million loan from the General Fund to the Property Acquisition Law Money Account (PAL) and a one-time augmentation of \$1.9 million from PAL to the Asset Planning and Enhancement Branch for property disposition studies because it is not clear there would be an economic benefit to the state that would result from the studies. (Reduce Item 1760-012-0001 by \$1.1 million and Item 1760-015-0002 by \$1.9 million.)

The budget proposes a \$1.9 million augmentation from the PAL to the Asset Planning and Enhancement Branch and a \$1.1 million loan from the General Fund (to be repaid by June 30, 2005) to the PAL to fund market, feasibility, and due diligence studies intended to result in the state receiving higher prices when it disposes of surplus state property. It is proposed that the money be spent for studies for Agnews Developmental Center, Department of Developmental Services properties, the California Institution for Men at Chino, and properties in Santa Clara and San Jose. Because of the PAL fund condition, the General Fund loan is needed to support this proposed augmentation.

We have several concerns with this proposal. First, no information is provided to indicate what *benefit* can reasonably be expected in return for the state's investment in these studies. The Legislature needs to have some basis for concluding these studies would be a cost-effective investment.

Second, it is not clear that these studies are appropriately undertaken by the seller (the state), rather than the buyer of the property. It would seem reasonable to expect that any serious potential buyer of property with development potential would conduct market, feasibility, and due diligence studies before making an offer to purchase.

Third, much of the information the proposal suggests is needed may be available without cost to the state from commercial real estate brokers who are in the business of providing this information as a way to generate successful property transactions from which they benefit.

Finally, it is not clear why the department is seeking additional funding for studies at two properties for which studies were previously funded. The budget proposes a total of \$1.2 million for studies at Agnews Developmental Center and the California Institution for Men, Chino. The department, however, was appropriated \$600,000 by the 1996-97 Budget Act for property disposition studies at the same two facilities. The budget proposals do not explain why the information developed earlier is now inadequate and why more studies of the same facilities are needed. Also, several of the proposed studies are on sites the Legislature has not declared surplus to the state's needs.

Based on the above issues, we recommend the Legislature deny the proposed \$1.9 million augmentation to the Asset Planning and Enhancement Branch and the accompanying \$1.1 million General Fund loan to the PAL.

Need to Eliminate Deferred Maintenance

We withhold recommend on a \$2.7 million augmentation proposed for special repair projects pending receipt of information from the Department of General Services detailing (1) the total deferred maintenance backlog, (2) a plan to eliminate the backlog, (3) annual funding need for proper maintenance of state buildings, and (4) necessary adjustment to state building rental rates.

As discussed above, DGS establishes a statewide "standard building rental rate" that it charges departments occupying state office space. Included in the determination of this rental rate is an amount to cover the cost of "special repairs and deferred maintenance." Special repairs are costs to periodically repair and replace major building features and equipment, such as reroofing or replacing air conditioning equipment. Deferred maintenance, in part, includes these special repairs that DGS did not accomplish when the work was needed. When this deferral occurs, the cost ultimately to undertake the repairs may be substantially more costly.

The amount included in the standard rental rate for special repairs and deferred maintenance totals \$5.6 million (\$2.9 million for special repairs and \$2.7 million for deferred maintenance). The department indicates this is insufficient to take care of all needed special repairs, and the budget proposes a one-time augmentation of \$2.7 million. It is not clear whether this action addresses their complete special repairs needs or how it affects their deferred maintenance problem. (The DGS has advised us that the deferred maintenance problem in state office buildings totals \$20 million.)

We concur with DGS's attempt to modify rental rates in order to fund maintenance and special repairs in a timely manner. Proper maintenance of buildings should ensure that these items are properly accomplished

and not deferred. As a result, DGS needs to obtain sufficient rental income to maintain buildings in a timely manner and eliminate deferred maintenance.

Consequently, we withhold recommendation on this proposal pending receipt of information from the department identifying (1) total deferred maintenance backlog, (2) a plan to eliminate the backlog, (3) the annual amount necessary to properly maintain buildings and undertake special repairs, and (4) the necessary adjustment to the building rental rates to accomplish these goals.

STATEWIDE SUPPORT SERVICES

Report on State's Telecommunications Contract Not Received

We recommend that the Legislature not take action on the proposal to decrease the Department of General Services' telecommunications expenditure authority by \$12.1 million until the department provides a report to the Legislature, due January 1, 2001, which describes the actions of the state and the contractor to address problems in the state's telecommunications network.

The budget proposes a \$12.1 million reduction in DGS expenditure authority due to the replacement of the state's telecommunications operations with the California Integrated Information Network (CIIN) contract.

The CALNET System. In 1996, DGS began the divestiture of the state's telecommunications operations, known as CALNET, and the procurement of telecommunications services from another firm. The CALNET, which was developed in the early 1990s, was never fully accepted by state departments as DGS had planned. As a result, it did not generate the anticipated revenues and, in fact, experienced losses over several years. Because CALNET was losing money, the state decided to sell off its hardware and purchase these services from a private vendor. In January 1997, DGS released its strategic plan for providing statewide telecommunications services, known as the CIIN Strategic Plan. The plan proposed moving to a privately owned and operated network, via a contract with a vendor which could cost up to \$500 million over five years.

The CIIN Contract. In December, 1998 the administration signed a contract with Pacific Bell (PacBell)/MCI to provide voice and data communication services to state and local entities. This annual amount of the CIIN contract is estimated to be about \$100 million.

State agencies began to utilize the new telecommunications service in January 1999. Conversion of voice communications has been completed and very few problems experienced.

Frame-Relay Network Experienced Major Problems in 1999. The second component to be converted to the CIIN contract was the state's "frame-relay" network which provides data communications for the state's information technology systems. The DGS started this conversion in January 1999 but halted it in April 1999 due to the severity of outage problems reported by several departments throughout the state.

The DGS took a number of actions to remedy these problems including working directly with the contractor. The frame-relay conversions have been restarted and DGS expects to complete them in 2002.

The DGS Needs to Submit Required Report to Legislature. The Legislature requested that DGS provide an update of its CIIN contract activities and steps taken by the state and the contractor to reduce future frame-relay problems. This report was to be submitted by January 1, 2001. At the time this analysis was prepared, the Legislature had not received this report.

Legislature Should Review Information Before Taking Action on Request. It is important for the Legislature to be able to review this report to ensure DGS actions are adequate to reduce or eliminate future telecommunications problems and minimize disruption of critical state services. For this reason, we recommend that the Legislature not take action on the proposed reduction in expenditure authority until it has received the report and had an opportunity to review it.

State's 911 Surcharge May Be Too High

We recommend that the Legislature direct the Department of General Services to (1) identify an appropriate reserve for the State Emergency Telephone Number Account (911) and (2) identify appropriate adjustments to the 911 surcharge to bring that reserve to the identified level.

The budget proposes an increase in expenditure authority of \$31.7 million to the State Emergency Telephone Number Account (911) to begin local government implementation of enhanced 911 service for wireless or "cellular phone" subscribers. The request is the first of a three-year enhancement effort with a projected total start-up cost of \$114 million and an ongoing cost of \$20 million.

Background. The DGS is responsible for administering the State Emergency Telephone Number Account. This account is funded through a 911 surcharge that is placed on monthly phone bills, including cellular phone service. Local agencies are responsible for providing 911 services and then requesting funds from this account as necessary to maintain 911 operations.

Current Cellular 911 Service Does Not Include Full Services. Current 911 service does not include the same capabilities for cellular phones as for land-based phones. For example, local 911 agencies are not able to

pinpoint the exact location of a cellular call as they can with a land-based call. The department's proposal would allow implementation of technical changes to upgrade the response capabilities for cellular subscribers.

The 911 Local Assistance Account Has High Reserve. According to DGS, the 911 local assistance account has been growing at a higher than expected rate due to an increase in the number of cellular phone accounts. Over a period of years, the reserve has ranged from \$60 million to \$80 million a year. According to the proposal, even with the costs of implementing enhanced 911 wireless service, the account is expected to have a reserve of between \$30 million to \$50 million depending on the cost of the enhanced 911 service and the number of cellular phone accounts.

The DGS Should Examine Surcharge Amount. Based on information provided by the department concerning the future funding requirements for 911 service, we see no reason to maintain such a high reserve and, therefore, recommend that the Legislature direct DGS to reexamine the surcharge amount. In preparing its report, DGS should take into account any possible revisions in the cost of implementing 911 wireless services. We recommend adoption of the following supplemental report language:

The Department of General Services shall, by March 1, 2002, provide a report to the chairs of the budget committees in each house and the Chair of the Joint Legislative Budget Committee which analyzes the appropriateness of 911 surcharges to California phone subscribers. This analysis shall take into consideration the growing number of cellular phone subscribers, the need to maintain current 911 operations and enhance 911 wireless services, and the need to maintain an adequate reserve in the State Emergency Telephone Number Account. The report shall identify an appropriate reserve for the State Emergency Telephone Number Account and recommend rate adjustments to the surcharge to achieve the recommended reserve level.

Special Funds Should Help Support eBusiness Center

We recommend that the Department of General Services submit to the Legislature, prior to budget hearings, a revised funding proposal for the "eBusiness Center" which reflects reimbursements for on-line activities of those departments which are supported by special funds.

The budget proposes a \$3 million General Fund augmentation (\$2.7 million one-time and \$300,000 ongoing) for the California eBusiness Center which conducts studies of e-government services to California businesses. Last year the 2000-01 Budget Act provided five personnel-years and \$4.4 million from the General Fund (\$2.4 million one-time and \$2 million ongoing) to start the eBusiness Center. In addition, the Supplemental Report of the 2000-01 Budget Act directed DGS to report to the Legislature, by

April 1, 2001, on the expected benefits of the eBusiness Center. Figure 6 summarizes the key components to be included in this report.

Figure 6**Key Components of eBusiness Center
Supplemental Report Due to Legislature April 1, 2001**

- Describe eBusiness Center project's accomplishments
- Assess statewide needs of business community's top priorities for e-government
- Conduct business process reviews for those top priorities
- Examine alternative and/or private sector financing for the eBusiness Center portal
- Provide information in the areas of professional licensing, competitive bid processing, procurement expansion, environmental regulation, and job posting and recruitment which:
 - Analyzes the impact of processing e-government transactions on current automation system.
 - Identifies potential project risk areas.
 - Reports results from customer surveys.
 - Identifies areas for potential business processes reengineering.

General Fund Being Used to Support Special Fund Programs. Our review of current- and budget-year activities indicates that a number of the eBusiness Center activities support special funds programs. For example, General Fund support is being used for an on-line bidding project which allows the California Department of Transportation (Caltrans) to post construction project proposals and conduct bidding on-line, even though most of Caltrans' activities are funded through special funds.

Administration Should Revise Proposal to Include Special Funds. We believe that services provided by the eBusiness Center to departments that are funded by special funds should be supported by special funds. Therefore, we recommend that DGS submit a revised funding proposal to the Legislature prior to budget hearings which reflects the use of not only the General Fund, but also special funds to support the eBusiness Center.

Method for Funding California Enterprise Project Is Inequitable

We recommend that the Department of General Services submit a revised funding proposal for the ongoing support and operation of the state's home page and the Governor's Office computer network which (1) distributes costs of these projects among special funds in addition to the General Fund and (2) provides adequate funding for ongoing modifications to California's home page.

The budget proposes an ongoing augmentation of \$1.7 million from the General Fund for the state's home page and a one-time augmentation of \$1.5 million from the General Fund to upgrade the Governor's Office computer network and E-mail system.

Background. The 2000-01 Budget Act appropriated \$5.1 million to DGS to redesign the California home page, enhance the citizen E-mail system, and upgrade the Governor's Office network. The department completed these activities in January 2001.

Current Funding Method Inequitable. It is our understanding that these various automation efforts provide support for all state programs even though they have been entirely funded from the General Fund. For example, all departments will use the enhanced E-mail system and will have access for their Web sites through the redesigned home page. We believe the ongoing costs for these systems should be shared by the General Fund as well as special funds through the use of a pro rata model or direct billing for usage.

Home Page Maintenance and Support Costs Seem Low. It is our understanding that the \$1.7 million home page proposal contains \$1.4 million for staff and hardware/software costs which leaves \$300,000 available for ongoing modifications. Our review of similarly sized projects indicates that between \$400,000 to \$800,000 is needed annually for ongoing modifications. Therefore, the proposal's amount for ongoing modifications seems low considering the magnitude of usage and complexity of the redesigned home page.

Administration Should Examine Cost Sharing Models and Sufficiency of Request. Given the inequities of the current funding method as well as the potential shortfall of funding to provide ongoing support of the home page, we recommend that DGS submit a revised funding proposal which (1) distributes the costs of these projects among special funds as well as the General Fund and (2) provides adequate funding for support of ongoing modifications to California's home page.

PUBLIC EMPLOYEES' RETIREMENT SYSTEM (1900)

The Public Employees' Retirement System (PERS) administers the retirement benefit program for state employees (excluding the University of California) and the health benefits program for employees and annuitants. The current value of the Public Employees' Retirement Fund (PERF) is about \$170 billion. As a result of Proposition 162, which was approved by voters in November 1992, PERS has authority to spend funds to administer the retirement program for state employees without appropriation by the Legislature. However, because the health benefits program is separate from the retirement program, the Legislature does approve the budget for the health program. The entire PERS budget, however, is included in the budget bill as an informational item, with budget bill language that requires PERS to report specified budget information to the Legislature.

The Governor's budget shows 2001-02 expenditures for PERS of \$286 million, an increase of \$1.4 million, or less than 1 percent, over estimated current-year expenditures. However, the PERS Board will approve the 2001-02 PERS budget in the spring. Thus, the budget amount reflects a continuation of existing activities and does not include any new spending proposals for 2001-02.

Cost Allocation Plan Reveals High Overhead Costs

We recommend that prior to budget hearings the Public Employees' Retirement System advise the Legislature on (1) what actions it will take to ensure that Public Employees' Contingency Reserve Fund expenditures to administer the state's health benefits program do not continue to exceed annual revenues and (2) the effect of reducing the 0.5 percent charge the state pays into the fund in order to reduce fund reserves.

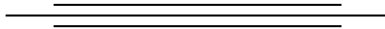
The PERS requests \$2.9 million from the Public Employees' Contingency Reserve Fund (CRF) for administration of the state's health ben-

efits program. As adopted in Control Section 4.20 of the annual budget act, the state pays an amount equal to 0.5 percent of health insurance premiums into CRF to support PERS' costs. According to the Governor's budget, this amounts to \$11.8 million in 2001-02.

Our review of PERS' budget-year spending request indicates that its overhead expenditures are 39 percent of total health administration costs. By comparison, overhead costs of 15 percent to 20 percent are more the norm for other state agencies.

While we support the concept of proportionately allocating overhead costs to department funds to accurately account for all their costs, PERS' overhead costs are very high. Moreover, this proposal would cause CRF expenditures to slightly exceed revenue from the 0.5 percent charge. As a result, we recommend that prior to budget hearings PERS advise the Legislature on what actions it will take to (1) control overhead costs and (2) ensure that CRF expenditures to administer the state's health benefits program do not continue to exceed annual revenues.

We also note that the CRF fund balance is relatively high. The proposal would leave a fund balance of \$10.8 million (89 percent of budget-year expenditures) at the end of the budget year. Consequently, we also recommend that prior to budget hearings PERS advise the Legislature on the effect of reducing the 0.5 percent charge the state pays into CRF to reduce the reserves.



DEPARTMENT OF ALCOHOLIC BEVERAGE CONTROL (2100)

The Department of Alcoholic Beverage Control (ABC), established by constitutional amendment in 1954, administers the Alcoholic Beverage Control Act. Under the act, the ABC has the exclusive authority, in accordance with laws enacted by the Legislature, to license and regulate the manufacture, sale, purchase, possession, and transportation of alcoholic beverages in California, and to collect licensing fees. The ABC also has the authority to deny, suspend, and revoke licenses.

The Governor's budget proposes \$35.4 million for support of the ABC in 2001-02 from the ABC Fund (\$34.6 million) and reimbursements (\$869,000). Included in this amount is \$1.5 million for local assistance—the same as the current year. In total, the proposed budget is less than a 1 percent increase.

The ABC Fund Condition

We recommend the Legislature enact legislation allowing the Department of Alcoholic Beverage Control to increase license fees to sustain current enforcement levels and avoid budgetary shortfalls.

The ABC Fund receives revenues from 61 different types of manufacturer, importer, retail, and wholesale liquor licenses. The ABC currently monitors over 72,000 licensees. Estimated net revenues to the fund in 2001-02 are \$32.2 million.

In the *Analysis of the 1999-00 Budget Bill* we noted that—based on projected expenditures—the fund would not cover ABC's budget by 2001-02. Since that time, however, unexpected reductions in the state employer retirement costs resulted in substantial savings in ABC's operating budget. Had the reduction in retirement expenditures not occurred, the fund

would not have been sufficient to support ABC's current level of activities in the budget year.

Based on current-year and proposed budget-year expenditures and revenues, the ABC fund will end the budget year with approximately \$2.6 million in reserve. This represents approximately one month's operating expenses for ABC. This is substantially less than the \$8 million that would be needed to maintain what is usually considered to be a prudent special fund reserve of three months' operating costs. Moreover, if retirement expenses increase in the budget year, the fund will be depleted during the 2002-03 budget year. In the event retirement costs remain stable, there will be insufficient funds to support the current level of activity in 2003-04. Consequently, in order to sustain the current level of enforcement by the department license fees will have to be increased.

History of ABC License Fees. The license fee revenue deposited in the ABC Fund is the total of a base license fee established in 1955 and four subsequent increases:

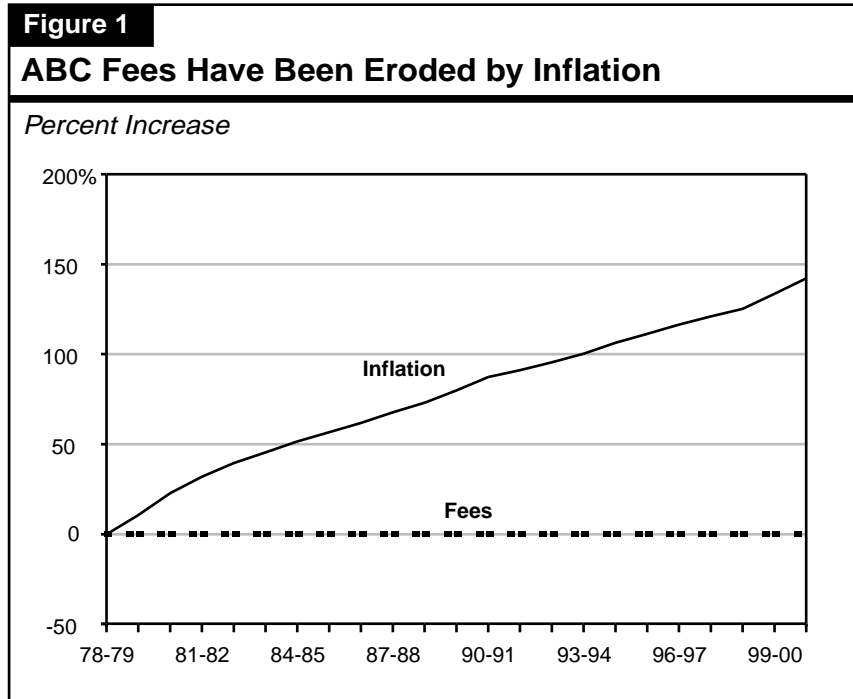
- In 1978—a 10 percent surcharge to account for inflation.
- In 1983—a 6 percent surcharge to pay for administrative hearings.
- Also in 1983—a 3 percent surcharge to fund the Alcoholic Appeals Board. These funds go directly to the board and are not available to the ABC.
- In 1991—a \$5 assessment against most licensees was added to fund designated driver education programs under the California Highway Patrol. These funds are used exclusively by the highway patrol.

Of the four license increases above, only the 1978 surcharge funded department enforcement activities. Periodically, however, regulatory agencies must evaluate their fee schedule and adjust fees upward (for example, to account for inflationary pressures) or downward (for example, when workload declines). In ABC's case, operating costs have increased because of inflation and increased enforcement activities, yet the license fees have not kept pace with these costs. Figure 1 illustrates the extent to which inflation since 1978 has reduced the purchasing power of the fees.

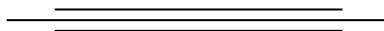
As discussed above, these fees have not been adjusted for inflation since 1978. To illustrate the impact of that on the department, we estimate that if license fees were adjusted solely to reflect inflation since 1978, the fund would have about \$55 million in additional revenue for the proposed budget year.

Ideally, the ABC fee structure should generate sufficient operating revenue to fund needed ABC operations and establish a reasonable re-

serve. In addition, because ABC fees are set in statute, the fees should be structured with sufficient flexibility to periodically allow adjustments to match the enforcement activities and associated budget changes approved by the Legislature.



Given the department’s tight budgetary situation, we recommend that the Legislature amend the Alcoholic Beverage Control Act to permit ABC to increase fees. We would suggest giving ABC the ability to raise fees up to 20 percent over several years. We further recommend that any fee increase be conditioned on the need to increase fees only to meet the budget expenditure level approved by the Legislature and necessary to maintain a prudent operating reserve.



DEPARTMENT OF FINANCIAL INSTITUTIONS (2150)

The Department of Financial Institutions (DFI) licenses and regulates several different types of entities to protect the funds entrusted by the public to these institutions. These entities include domestic banks, California branches of foreign banks, credit unions, issuers of money orders and travelers checks, and transmitters of money abroad. The DFI is supported by revenues from fees and assessments charged to regulated entities. Most of these fees are deposited in the Financial Institutions Fund and the Credit Union Fund.

The budget proposes \$19 million in expenditures and 204 personnel-years (PYs) for 2001-02. This equals estimated current-year expenditures, but represents a reduction of 10 PYs. The budget proposal reflects a variety of increases and decreases in spending resulting in the same level of expenditures in both years. The reduction in PYs is due to an increase in assumed salary savings based on past experience for this department.

Request to Relocate Sacramento Office Is Premature

We recommend that the Legislature delete \$412,000 for increased rent expenses associated with the proposed relocation of the Department of Financial Institutions' Sacramento office because the department's request is premature. (Reduce Item 2150-001-0240 by \$24,000, Item 2150-001-0298 by \$315,000, and Item 2150-001-0299 by \$73,000.)

The budget proposes \$412,000 for increased rent expenses to relocate the department's Sacramento office. According to DFI, the department needs additional office space to accommodate positions the department proposes to move from its San Francisco office. In addition, pursuant to the 2000-01 Budget Act, DFI took over a small program from the State Treasurer effective January 1, 2001, thus adding five positions to the Sacramento office.

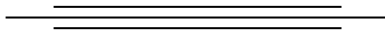
Currently, the department has 6,165 square feet of office space in Sacramento for 39 positions. The department proposes to acquire 14,673 square feet and transfer 26 positions from San Francisco, for a total of 65 positions. The department asserts that moving these positions will alleviate problems hiring and retaining staff due to the high cost of living in the Bay Area. However, DFI proposes moving these positions only as they become vacant or existing staff express a desire to relocate. Even after the 26 positions are relocated, 54 positions would remain in San Francisco—the commissioner; some executive, policy, and legal staff; and the majority of Northern California examiner staff.

We do not want to discourage DFI's attempt to consolidate staff in Sacramento. In fact, we believe moving the entire department to Sacramento merits consideration given (1) the department's difficulty filling positions in its San Francisco office due to the high cost of living in the Bay Area and (2) the high cost of office space in the Bay Area (notwithstanding DFI's current lease, at a very favorable rate, that does not expire until 2008).

We believe, however, that the proposal at hand is premature. It is not cost-effective to lease space in Sacramento that will remain vacant for some time. As noted above, DFI proposes to increase the number of Sacramento-based staff from 39 to 65, acquiring sufficient space to accommodate all 65 positions. However, positions are proposed to be moved to Sacramento only when they become vacant or when existing staff desire to relocate. Thus, DFI does not know how soon additional office space would be occupied.

In addition, while the department has not yet located new office space in Sacramento, it is looking in the downtown area. Office space in areas outside of downtown, such as Natomas or the Highway 50 corridor, would likely be less expensive.

Given these concerns, we recommend that the Legislature not approve this augmentation for increased rent expenses to acquire additional office space. Time is not at issue right now since DFI's current lease in Sacramento does not expire until December 31, 2002. A proposal for a new Sacramento office that includes a more definite time frame for relocating positions and alternative locations outside the downtown area would merit the Legislature's consideration.



DEPARTMENT OF CORPORATIONS (2180)

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

The budget proposes total expenditures of \$23.5 million and 275.4 personnel-years (PYs) in 2001-02. This is \$0.9 million, or 3.7 percent, less than estimated current-year expenditures and 4.4 fewer PYs.

State Corporations Fund Balance Very High

We recommend that the Department of Corporations report prior to budget hearings on (1) its fees and assessments, (2) proposed options for reducing or eliminating some of them, and (3) State Corporations Fund condition projections based on each option. We further recommend that upon evaluating this information, the Legislature enact legislation to change the fees and/or assessments.

As noted above, DOC is supported by license fees and assessments charged to regulated companies. Pursuant to Chapter 328, Statutes of 1998 (SB 1589, Committee on Budget and Fiscal Review), DOC suspended certain filing fees, effective July 1, 1998 through June 30, 2000, to reduce the surplus in the State Corporations Fund. These fees were reinstated for 2000-01. However, as shown in Figure 1, the fund balance remains very high. In the budget year, proposed revenues are \$32.1 million, while proposed expenditures are \$23.5 million. This would leave an end-of-year fund balance of \$38 million, or 162 percent of proposed expenditures. Typically, we recommend a prudent fund balance of around three months, or 25 percent, of annual expenditures. For DOC, this level of reserves

would total \$5.9 million, or \$32.1 million less than the indicated fund balance at the end of 2001-02.

Figure 1		
State Corporations Fund Balance 2001-02 Governor's Budget		
<i>(In Thousands)</i>		
	2000-01	2001-02
Beginning balance	\$20,889	\$29,275
Revenues	32,141	32,135
Total Resources	\$53,030	\$61,410
Expenditures	\$23,755	\$23,451
Ending Balance	\$29,275	\$37,959

According to the department, DOC is considering options for permanently reducing or eliminating some investment filing fees to reduce fund reserves. Given the size of the fund balance, we recommend that DOC report on the following prior to budget hearings:

- The level or rate of fees and assessments charged, including how much revenue is derived from each.
- Proposed options for reducing or eliminating some fees and/or assessments, the benefits and drawbacks of each option, and a recommendation.
- Five-year projections of the fund condition for each proposed option.

We further recommend that upon evaluating this information, the Legislature enact legislation to change the fees and/or assessments.

HOUSING AND COMMUNITY DEVELOPMENT (2240)

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

The budget proposes expenditures of \$531 million for 2001-02. This is a 6 percent increase from estimated current-year expenditures. The proposed General Fund expenditures of \$317 million account for 60 percent of the department's proposed funding. Included within this total is \$220 million for one-time spending on new proposals for expanding incentive payments to local governments and a new Central Valley infrastructure program. Federal funds account for \$107 million of the proposed budget-year expenditures, primarily for the Community Development Block Grant (CDBG) and Home Investment Partnership Act programs. A number of state special funds provide the remainder of HCD's funding. The department has a proposed staffing level of 497 personnel-years.

The department also received a large one-time appropriation for nearly \$500 million in the current year for a variety of programs. The budget proposes to expend these funds over 2000-01 and 2001-02. Below, we review the implementation of the current-year's housing funding package and analyze the Governor's new proposals.

IMPLEMENTATION OF THE 2000-01 HOUSING PACKAGE

The *2000-01 Budget Act* included a substantial increase in the department's General Fund support, largely on a one-time basis. In addition to augmenting funding for existing programs, the budget and ac-

companying legislation also created a number of new department programs. Figure 1 (see next page) summarizes the allocation of the more than \$500 million housing package, as well as the proposed spending in these programs in 2001-02. We discuss the status of the various programs below. Funding notices and applications should be available to eligible applicants for all of the programs by February 2001.

Local Government Incentives

Chapter 80, Statutes of 2000 (AB 2864, Torlakson), created the Jobs-Housing Balance Improvement Program in an effort to increase local housing and economic development activity. The 2000-01 budget appropriated \$110 million for three components of the program.

Incentive Grants. The 2000-01 budget provided \$100 million to make “incentive payments” to local governments intended to increase housing production. The program is scheduled to make payments based on the level and type of housing permits issued in a jurisdiction during calendar year 2001. As discussed in more detail below, the Governor has proposed augmenting the program by \$200 million and making payments based on housing production in both 2001 and 2002.

Economic Development Grants. Another component of the Jobs-Housing Balance Program will make \$5 million available to local governments to develop or implement economic development strategic plans in order to attract businesses to their communities.

Predevelopment Loans. The department will also make \$5 million in low-interest loans available to local governments and nonprofit organizations for the predevelopment costs associated with developing housing near transit stations. After these funds are allocated, the Governor proposes to merge this program with the department’s other predevelopment loan programs—making repaid loan funds available to urban, rural, and housing preservation projects as well.

Homeownership Programs

CalHome Program. Chapter 84, Statutes of 2000 (SB 1656, Alarcon), created the CalHome program as the department’s primary funding mechanism for promoting homeownership among low- and very-low-income households. The intent of the program was to consolidate a number of existing department programs and provide the flexibility to offer funding through a single application process. The program allows the department to make both loans and grants to local governments and nonprofit organizations for a variety of purposes, including downpayment assistance, rehabilitation, self-help housing, predevelopment costs, and

Figure 1**HCD Funding for Major Housing Programs**

*General Fund
1999-00 Through 2001-02
(In Millions)*

	1999-00	2000-01 ^a	Proposed 2001-02
Local Government Incentives			
Jobs-Housing Balance Improvement Program:			
Incentive grants	—	\$100.0	\$200.0
Economic development grants	—	5.0	—
Mass transit predevelopment loans	—	5.0	—
Homeownership			
CalHome:			
Base program	—	\$40.0	—
Mobilehome ownership	—	10.0	—
Homebuyer's Downpayment Assistance	—	50.0	—
Farmworker Housing:			
Base program	\$3.5	35.5	\$18.5
Manufactured housing	—	3.0	—
Unhealthy and unsafe units	—	3.0	—
Health services demonstration	—	5.0	—
Self-help housing	2.0	2.1	2.1
Multifamily Housing			
Base program	\$11.0	\$188.0	\$31.0
Downtown Rebound:			
Project loans	—	22.6	3.0
Local government planning grants	—	2.4	1.4
Homeless			
Emergency Housing Assistance Program:			
Operating grants	\$2.8	\$14.0	\$14.0
Capital grants	—	25.0	—
Other Programs			
Code enforcement incentives	—	\$5.0	—
Interregional Partnership Pilot	—	5.0	—
Child Care Facilities	—	16.0	—
Central Valley Infrastructure Grants	—	—	\$20.2
Predevelopment loans	\$1.5	1.5	4.0
Totals	\$20.8	\$538.1	\$294.2

^a This column shows the appropriations for these programs. The expenditures of these funds will occur over 2000-01 and 2001-02.

shared housing. Of the \$50 million appropriated to the program in 2000-01, \$10 million was set aside to fund local programs that allow homeowners to repair or replace manufactured housing.

Downpayment Assistance Program. Chapter 81, Statutes of 2000 (AB 2865, Alquist), created the California Homebuyer's Downpayment Assistance Program. The 2000-01 Budget Act appropriated \$50 million to the department to contract with the California Housing Finance Agency (CHFA) for the administration of the program. The program, which is targeted to moderate-income families, is discussed in more detail in the analysis of CHFA's budget (please see Item 2260).

Farmworker Housing Grant Program. The farmworker housing grant program provides local governments and nonprofit organizations with grants for the construction and rehabilitation of housing for the families of agricultural workers. The 2000-01 budget provided \$35.5 million for the base grant program and the department has received about \$28 million in application requests thus far. An additional \$10 million was appropriated for three separate components:

- ***Manufactured Housing Component.*** The budget set aside \$3 million for sites using manufactured housing for 12 or fewer employees in a cooperative arrangement between the employer and a nonprofit organization.
- ***Health and Safety Component.*** The budget reserved an additional \$3 million for manufactured housing projects needing assistance due to health and safety problems.
- ***Health Services Demonstration.*** The budget allocated \$5 million for a demonstration project funding farmworker housing projects that include health services. The department expects to enter a contract for the full amount with the Rural Community Assistance Corporation to administer the grants.

Each of these separate components will be eligible for future funding under the base program.

Multifamily Housing Programs

Multifamily Housing Program. Previously, the department funded multifamily projects through a variety of special purpose programs, such as a welfare-to-work housing program and a rehabilitation program. Similar to the CalHome program, Chapter 637, Statutes of 1999 (SB 1121, Alarcon), consolidated a number of multifamily housing programs, allowing the department to fund a variety of project types through a single application. The new program received a \$188 million appropriation in 2000-01, with a proposed ongoing appropriation of \$31 million. In its ini-

tial funding application process this year (which made \$50 million available), the department received requests totaling \$175 million.

Downtown Rebound. The Downtown Rebound program which was created by Chapter 83, Statutes of 2000 (AB 2870, Cedillo), and appropriated \$25 million in the 2000-01 budget for three components, intended to promote the revitalization of urban areas:

- ***Adaptive Reuse Loans.*** Most of the funds, \$19 million, are available for projects to reuse commercial or industrial buildings for residential units.
- ***Additional Housing Projects.*** Another \$3.6 million in loans is available for a variety of multifamily housing purposes, including adaptive reuse, in-fill of vacant sites, and housing near transit centers. The Governor proposes \$3 million in ongoing funds for the Downtown Rebound program to be eligible for these purposes.
- ***Local Government Planning Grants.*** The remaining \$2.4 million is available to local governments for planning grants for site inventories and feasibility studies, updates of general plans and zoning ordinances, and related purposes. The Governor proposes \$1.4 million in ongoing funds for planning grants.

Homeless Programs

The state's primary program for the funding of homeless shelter services is the department's Emergency Housing and Assistance Program (EHAP). The 2000-01 budget contained \$39 million for two components of EHAP:

- ***Operating Grants.*** \$14 million of the funds are available to fund the ongoing services of homeless shelters. This level of funding is again proposed for 2001-02.
- ***Capital Loans.*** Forgivable loans totaling \$25 million are available for the construction, rehabilitation, or acquisition of shelter facilities.

Other Programs

Code Enforcement Incentives. Two new programs—designed to improve local enforcement of building codes—were created by Chapter 664, Statutes of 2000 (AB 1382, Lowenthal), and appropriated \$5 million in one-time funds. The department has received about \$30 million in applications for the two programs.

- **Code Enforcement Incentive Program.** This program (\$2.75 million) provides three-year grants to local jurisdictions to increase staffing for local code enforcement activities. The maximum grant amount is \$1 million, and local matching funds must increase over the life of the grant.
- **Community Code Enforcement Pilot Program.** This program (\$2.25 million), with a maximum grant amount of \$450,000, emphasizes improving cooperation between code enforcement officials and prosecution agencies, health departments, housing agencies, and schools.

Interregional Partnership Pilot Program. This program, funded at \$5 million, will provide grants to assist local governments undertaking interregional planning for housing and employment issues, with a particular emphasis on improving geographic mapping.

Child Care Facilities. The budget appropriated \$16 million for the Child Care Facilities Financing Program. The funds can be used for either direct loans or loan guarantees for child care facility purchases, expansions, or renovations. In the *2000-01 Analysis*, we reported that the program was having administrative difficulties in distributing \$7 million in funds appropriated in the 1997-98 budget. In the past year, the department has made only \$485,000 in new direct loans and another \$614,000 in loan guarantees. As a result, \$3.7 million of the original 1997 appropriation is still available for loans and guarantees, and the department has yet to use any of the current-year's appropriation. The 2000-01 budget requires that the department report on the program by March 15, 2001, including a discussion of any impediments to increased participation.

NEW HOUSING PROPOSALS

Payments to Local Governments Unlikely to Change Behavior

We recommend redirecting the proposed \$200 million augmentation for incentive payments to local governments to a more effective approach to addressing the state's lack of housing development. As a one-time program, the payments will fail to change the underlying disincentives for local governments to build housing. In the program's place, we suggest more targeted options for either one-time or ongoing appropriations. (Delete Item 2240-114-0001 and Item 2240-114-3006.)

Background. The current system of local government finance generally does not encourage local governments to approve housing projects, particularly multifamily and affordable housing developments. The jurisdiction which approves the housing receives a relatively small share of

the property taxes generated from the new development. These revenues, in many cases, are not enough to pay for the costs of providing services to the new housing.

The state's major oversight of local housing policy is the housing element process. As part of their general plan, cities and counties must develop a housing element which adequately plans for future needs in housing, particularly a "fair share" of the region's expected affordable housing needs. In order to be in compliance with state law, HCD must approve a community's housing element. Less than 70 percent of communities are currently in compliance with the housing element law.

Program Created in 2000-01. The Jobs-Housing Balance Improvement Program was created last year and appropriated \$100 million to make incentive payments to local governments with the intention that the payments would encourage greater housing production. Early in 2001, the department will issue its guidelines to local governments on what basis these funds will be distributed. While the department is still finalizing its guidelines, it has outlined the following framework for the payments:

- Payments will be made in January 2002, based on the level of housing permits issued in calendar year 2001.
- Jurisdictions will be eligible for payments only if they (1) have their housing element in compliance with state law by the end of 2001 and (2) issue housing permits in 2001 that exceed their average permit issuance from the prior three years by a yet-to-be-determined percentage (in the range of 10 percent to 25 percent).
- If jurisdictions meet these two criteria, then payments would be made on a per-unit basis to each jurisdiction for the following: (1) all permits issued above the three-year average percentage threshold; and (2) additional amounts for priority units: multifamily, "in-fill", those with affordability restrictions, and those sold within county affordability limits. Units which met more than one of these criteria would be eligible for multiple incentive payments.

In its guidelines, the department will outline a range for the per-unit payments, but the department plans to finalize the amounts of the payments and their criteria only once the total number of units built is known at the end of 2001. Current law restricts the use of the payments by local governments for capital outlay projects.

Governor Proposes Expanding the Program. The Governor proposes augmenting the program by \$200 million in this year's budget. Under the proposal, \$50 million would be added to the current-year's payments so that \$150 million would be paid to local governments in both 2001 and

2002. In addition, the Governor proposes allowing local governments to spend the payments for any purpose.

The department correctly assesses that housing production will not dramatically change without significant market-based incentives. Unfortunately, the program that they have developed suffers from fundamental shortcomings that will prevent it from providing significant enough incentives to change most local governments' behavior.

One-Time Program Will Fail to Influence Long-Term Decisions. Local government decisions about whether to authorize housing construction are made with a view to their long-term impact—for instance, service costs for the coming decades, the impact on the community's long-term character, and other potential land uses for the area. In most cases, a *one-time* receipt of funds is unlikely to outweigh a community's long-term considerations.

Benefits Unknown at the Time of Housing Approval. Increasing the amount of revenues generated by the approval of a housing project (through incentive payments) would reduce the gap between the revenues generated and the costs of providing services to that project. This could, in turn, encourage local governments to approve more housing projects. The method in which the program is proposed to be implemented, however, would limit the change in incentive structure. Since the program's incentive payments would be made (1) after the end of the year and (2) based on the *total* amount of housing approved, a local government will be unable to depend on any increased revenues when approving an individual project. For example, if a city council is considering the approval of a housing project in June, it has little way of knowing if it will approve enough housing during the following six months to meet the various thresholds necessary to receive incentive payments. Thus, the city council can not count on the incentive payments in its calculations of the costs and revenues associated with the particular housing project.

Moreover, the department is reserving the right to adjust the payment amounts and criteria after the end of the year. This will further prevent a local government from knowing exactly how much to expect in increased revenues at the time of housing approvals.

Fails to Improve Current System of State Oversight. In order to be eligible for the incentive payments, some additional communities will likely comply with state housing law. The current system of state oversight, however, makes limited efforts to ensure that any community stays in compliance between periodic updates. Furthermore, the system makes no effort to determine if a community actually builds enough housing to accommodate the growing demand. Thus, the current system fails to provide significant rewards to local governments which comply with state

housing law, and appropriate consequences to those governments which do not. By maintaining the existing housing law system separate from the incentive payments, the administration misses a significant opportunity to make state housing oversight a more meaningful, long-term process.

Without Changing Behavior, Windfall Payments Only. Most communities are likely to produce a similar amount of housing in 2001 as they have in the past three years. Whether they produce enough housing to meet the department's thresholds will depend on a variety of factors, such as general economic conditions, amount of available land, developer interest, and community support for more housing. As outlined above, we do not find reason to believe that many communities will dramatically alter their approach to housing as a result of this program proposal. Consequently, the vast majority of the program funds will make payments to local governments for actions that they would have taken regardless of the program's existence. For these governments, the payments will serve as a "windfall." While windfall payments may *reward* communities for supporting housing, the program would fail in its aim to *alter* the behavior of local governments.

Search for Better Solution. Given our analysis that the program will fail to change local government behavior, we recommend redirecting the proposed \$200 million augmentation. (The same analysis applies to the current-year appropriation of \$100 million, but we recognize that the Legislature already made this commitment of funds to local governments.) We propose two alternatives based on the level of funding that the Legislature is willing to commit to this purpose.

- ***Fund More Multifamily Housing.*** If the Legislature wishes to maintain the funding on a one-time basis, we would instead recommend appropriating funds to the department's multifamily housing program. The program funding would ensure that a sizable amount of affordable multifamily units is produced (the least likely units to be developed under the current incentive system).
- ***Develop More Focused Ongoing Program.*** We believe that with ongoing funding an incentive program could be developed that would be better able to alter local government behavior. In developing such a program, we would emphasize that: (1) governments know the specific benefits of the program *at the time* of issuing housing permits, (2) the program integrates with the state's oversight system, and (3) the amount of windfall payments are limited to the extent possible. Specifically, we would recommend more explicitly integrating the program with the housing element process—rewarding those local governments that implement, rather than just get approval for, their housing elements.

Such a system could award dollars to local governments for each unit of housing provided to meet its share of the region's affordable housing demand. The \$200 million could be sufficient to fund a number of years of such a program, if the payments were more targeted to the most difficult to develop affordable units (rather than all housing units).

Infrastructure Program Not Targeted to Problem

We recommend deleting the proposed \$20.2 million in funding for a new Central Valley Infrastructure Grant Program. The program would not address the underlying problem, other infrastructure programs already exist, and the funding would not make a significant impact. Improving locally controlled infrastructure financing tools or better targeting the existing state programs would be more effective approaches to financing local infrastructure projects. (Reduce Item 2240-001-0001 by \$200,000 and Item 2240-101-0001 by \$20 million.)

The Governor proposes a one-time appropriation of \$20.2 million for a new Central Valley Infrastructure Grant Program. The program would provide grants of up to \$1 million to local governments in the Central Valley for selected infrastructure projects related to water and wastewater systems, utilities, streets, or communications. Grants would only be given to projects determined to promote economic development, and the department expects to fund no more than 25 projects with the funds. We have a number of concerns with this proposal, which we outline below.

Does Nothing to Address Underlying Problem. Infrastructure funding for local governments is generally a local responsibility in California. The administration has proposed this program presumably with the belief that Central Valley local governments are unable to fulfill this responsibility on their own. However, the program would do nothing to change the underlying problem facing these local governments—the difficulties communities face in financing their own infrastructure needs. Moreover, it is unclear why other rural governments outside of the Central Valley, or local governments more generally, do not face the same problems. Yet, the program would provide no funds to these other communities.

Other State Programs Already Exist. Two state programs already exist with very similar purposes to the proposed program.

- ***The CDBG Program.*** Most large cities and counties receive CDBG funds directly from the federal government and can use the funds at their discretion for a variety of housing and economic development projects. The CDBG program administered by HCD provides federal funds to small jurisdictions (cities with populations

less than 50,000 and counties less than 200,000) through a competitive application process. The HCD component of CDBG will distribute an estimated \$47 million to local governments in the budget year. While the federal government sets basic guidelines for the distribution of these funds, the state—through statute and program regulations—has broad authority to set funding priorities. Infrastructure projects are currently an eligible use for nearly all of the HCD funds. The department reports that in recent years, however, the majority of projects funded have been housing rehabilitation projects.

- **Infrastructure Bank.** The state infrastructure bank, administered by the Technology, Trade, and Commerce Agency, was created in 1994 and provided a total of \$475 million through the 1998-99 and 1999-00 budgets. The bank provides low-interest loans for local government infrastructure projects similar in nature to those proposed to be funded by the Central Valley Infrastructure Program.

Given the existing programs that can fund local infrastructure projects, it is unclear why the state needs another, more specialized infrastructure financing program.

Amount of Funding Will Not Make Significant Impact. The Governor's proposed program would not significantly change the status of infrastructure in California, due primarily to (1) the limited number of projects funded and (2) the high cost of infrastructure projects. Compared to the hundreds of millions of dollars of funding for infrastructure from local sources, the CDBG program, and the infrastructure bank, the impact of the Governor's proposal would be marginal.

Better Options to Address Problem. Given these concerns with the program, we recommend deleting the proposed \$20.2 million in funding. If the Legislature decides that Central Valley infrastructure, and rural infrastructure more generally, is a funding priority for the state, there are a number of options that would more effectively address the lack of infrastructure financing options for local governments.

- **Improve Infrastructure Tools Available to Local Governments.** The *long-term* solution to a local government infrastructure financing problem would be to improve the existing local government finance system to allow communities to better meet their own needs. Locally controlled financing tools would allow communities to determine which projects are the highest priority locally.
- **Better Target Existing Infrastructure Programs.** A more immediate approach to addressing local infrastructure needs would be

to adjust the state's existing infrastructure programs to better match the Legislature's funding priorities. If the state CDBG program and the infrastructure bank are not meeting the Legislature's objectives, then the funding criteria for these programs should be revised to reflect current priorities.

Employee Housing Costs Should Not Be Paid Twice

We recommend deleting a \$50,000 request for performing employee housing plan checks, as the department should collect the necessary funding from the local governments which already received the payment of permit fees for the work. (Amend the Employee Housing Act and reduce Item 2240-001-0001 by \$50,000.)

The Employee Housing Act (EHA) gives the department responsibility for developing and enforcing standards for "employee housing"—generally defined as housing for five or more employees (1) provided in conjunction with employment or (2) provided for agricultural workers in rural areas. The majority of employee housing involves housing for farmworkers. Local jurisdictions may elect to implement the EHA on their own; otherwise, the department is responsible for enforcement.

Concern Over Timeliness of Housing Approvals. When seeking to construct, rehabilitate, or repair employee housing, the housing owner must apply for a construction permit from the local building or health department and pay the corresponding fee for the permit. There has been some concern that the development of housing could be delayed through the permit process by local communities resistant to employee housing. Specifically, an entity could prevent the housing by simply not acting on the permit application in a timely manner and by not performing the necessary check of the submitted plans for consistency with the appropriate building and health codes.

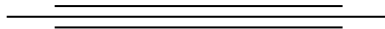
Department Given New Responsibility in 2000. In response to this concern, Chapter 702, Statutes of 2000 (SB 1545, Costa), provides an alternative approval procedure for any employee housing application for agricultural workers that has not been either approved or denied by the local department within 60 days. In those instances, Chapter 702 gives HCD the authority to check the permit plans and approve the application, if appropriate. The owner can then proceed with the project as if it had received local approval.

Request for Funding. As a result of the new plan-checking responsibility, the budget proposes an ongoing General Fund augmentation of \$50,000. The department proposes to use these funds to contract with the Department of General Services for the engineering services necessary to

perform the plan checks. Since this is a new responsibility that depends on the actions of local governments, the department is unsure how many plan checks it will be required to perform. The requested funds would allow about 350 plan checks to be performed annually.

General Fund Commitment Creates Wrong Incentives. We agree with Chapter 702's intent to prevent the unnecessary delay in the approval of farmworker housing projects. By granting the department's funding request, however, the state would create a fiscal incentive for some communities not to act on permit applications. Under current law and with the approval of HCD's funding proposal, the local department would be able to keep the fees collected for plan checks (generally several hundred dollars) without performing the associated work—by simply deferring to HCD's evaluation after 60 days. Chapter 702 gives no authority for HCD to collect the fees paid by an applicant to the local building department for the plan check. The Governor's proposal, in essence then, requests that the plan check be paid for twice—once by the applicant and once by the state's General Fund.

Recommend Allowing Department to Recover Costs From Local Governments. We recommend that the department, by amending the EHA, be given the authority to collect the already paid plan-check fees from local governments for any plan checks that HCD performs. This would both prevent local governments from keeping the fees for services that they did not provide and allow the requested \$50,000 to be deleted from the budget.



CALIFORNIA HOUSING FINANCE AGENCY (2260)

The California Housing Finance Agency (CHFA) was established by the Legislature in 1975 to provide below market-rate mortgage loans for single- and multi-family housing. The CHFA serves as the state's "mortgage bank" by selling tax-exempt bonds and then using the revenues to provide below market-rate loans. The bonds are not general obligations of the State of California, and the debt is repaid through revenues generated by the repayment of the mortgage loans. In 1999-00, CHFA made \$1.1 billion in loans, with 88 percent of that amount for single-family housing.

Although CHFA is financially self-sufficient, the agency has received General Fund appropriations for two programs in recent years.

Downpayment Assistance Program. Chapter 81, Statutes of 2000 (AB 2865, Alquist), created the California Homebuyer's Downpayment Assistance Program. The 2000-01 Budget Act appropriated \$50 million in one-time funds to the Department of Housing and Community Development to contract with CHFA for the administration of the program. The program provides moderate-income first-time home buyers with downpayment assistance of 3 percent of their purchase price. The assistance is provided in the form of a loan with deferred principal and interest. Since beginning operations in mid-October 2000, the program has received approximately \$4 million in applications, requesting an average of about \$4,000 in assistance.

School Facility Fee Reimbursements. Upon the passage of the state school bond measure Proposition 1A in 1998, Chapter 407, Statutes of 1998 (SB 50, Greene), went into effect and appropriated \$160 million for the School Facility Fee Affordable Housing Assistance Programs, designed to increase the affordability of new housing. The funds are appropriated to the Department of General Services (DGS) and then provided to CHFA through contract. Chapter 407 required the Legislative Analyst's Office to evaluate the effectiveness of these programs. Our evaluation was published in a January 2001 report and is summarized below.

ELIMINATE FUTURE APPROPRIATIONS FOR SCHOOL FACILITY FEE REIMBURSEMENTS

Given the school facility fee programs' sunset date at the end of calendar year 2002, the funds already appropriated should be sufficient to fund the programs through their conclusion. In addition, our analysis raises a number of concerns with the programs. Accordingly, we recommend that the Legislature eliminate the \$60 million in scheduled appropriations for the programs in 2001-02 and 2002-03—making the one-time funds available for other, more-targeted housing programs or other legislative priorities.

Changes to School Facility Developer Fees

School districts have a variety of funding mechanisms available to them to pay for the financing of school construction, including local general obligation bonds, local Mello-Roos bonds, developer fees, and state funding. Developer fees are charged by school districts on new residential and commercial construction to help offset the costs of the new school construction that the development will require. Prior to the passage of Proposition 1A, school districts were limited in the amount of school facility developer fees they could charge. Also, as a result of a series of court decisions in the years preceding the passage of Proposition 1A—known as the *Mira*, *Hart*, and *Murietta* decisions—cities and counties were able to impose additional school facility fees on development as a condition of obtaining land use approval.

Proposition 1A and Chapter 407 created different levels of developer fees. The former cap on fees—now known as “level I” fees—remains the maximum amount that a school district can charge except under specified circumstances. These level I fees are adjusted for inflation biennially, and as of January 2000, were \$2.05 per square foot for residential construction and \$0.33 per square foot for commercial construction.

For a school district to impose a fee in excess of the level I amount, it must meet specified conditions relating to local bond activity, year-round student enrollment, and use of “relocatable” classrooms. The amount of fees that can be charged over the level I amount is determined by the district's total facilities needs and the availability of state matching funds. If there is state facility funding available, districts are able to charge fees equal to 50 percent of their total facility costs, termed “level II” fees. If, however, there are no state funds available, “level III” fees may be imposed for the full cost of their facility needs (that is, twice the amount of the level II fees). Chapter 407 also prevents cities and counties from im-

posing their own school facility fees until 2006, thereby suspending the previous court decisions until that time.

Single-Family Housing Programs

In response to the concern that developer fees can reduce housing affordability, Chapter 407 created three separate programs that provide new home purchasers with state funding for a portion or all of school district facility fees paid on their homes. These housing assistance programs were then modified by Chapter 127, Statutes of 2000 (AB 2866, Migden), to expand program eligibility and extend their sunset an additional year, from January 1 to December 31, 2002. The differences among these programs are summarized in Figure 1.

Figure 1			
Comparison of Single-Family Housing Programs			
	Program 1 Economically Distressed Areas	Program 2 Sales Price Limit	Program 3 Moderate-Income First-Time Home Buyers
Income Limits	None.	None.	Moderate-income household limits.
Eligible Locations	Limited to "economically distressed counties" (currently 12 counties).	Available statewide.	Available statewide.
Sales Price Limits	175 percent of county median five-year sales price.	\$130,000.	None.
Limited to First-Time Home Buyers?	No.	No.	Yes.
Amount of Grant	School facility fees paid above level I amounts.	School facility fees paid above level I amounts.	Total amount of school facility fees paid.

Each program shares the following characteristics:

- The building permit on the new home must have been issued after January 1, 1999.
- Funds are available on a first-come, first-serve basis by application to CHFA.
- Funding may be combined with other government or private financing programs.

- State funds offsetting the cost of developer fees are deposited into the home buyer's escrow account prior to closing.
- If the home buyer does not occupy the home for five years, a prorated portion of the assistance must be repaid.

Multifamily Housing Program

In addition to the single-family programs discussed above, Chapter 407 also created a funding program for the reimbursement of school facility developer fees for the construction of new multifamily housing units. A development is eligible for the reimbursement of all fees paid to school districts in exchange for dedicating a portion of the project's units for very-low-income households (50 percent of county median income, adjusted for household size) for a period of 55 years. The number of units required to be dedicated must be in the same proportion to total units as the share of fees paid is to total construction costs. For example, if developer fees were 2 percent of total construction costs, a developer would have to dedicate four units of a 200-unit project to very-low-income households.

Program Funding

Chapter 407 appropriated \$160 million over five fiscal years from the General Fund to DGS for the developer fee programs. The department contracts with CHFA for the administration of these programs. Figure 2 shows the fiscal-year appropriations to the four programs. For the economically distressed areas and sales price limit programs, any funds not expended within 18 months of their appropriation may be transferred to the moderate-income first-time home buyers' program. Any unspent funds at the time of the program's sunset—December 31, 2002—will revert to the General Fund.

Experience to Date

Single-Family Programs. Although they have been functioning since the beginning of 1999, the single-family programs have expended few of their available funds (see Figure 3). Of the 748 applications that have been approved through the three programs, home buyers have received an average reimbursement of less than \$2,500.

After some experience with the programs, CHFA identified a number of problems and proposed a series of statutory changes to increase their use. These changes were incorporated into Chapter 127, effective beginning July 1, 2000. For the sales price limit program, very few homes in California were being constructed for less than the original purchase price limit of \$110,000. Therefore, the limit was raised to \$130,000 and is

now adjusted annually for changes in statewide home sales prices. The first-time home buyer program was originally limited to households of low-income. Few households of this income level, however, are in the position of purchasing homes. Thus, this program was expanded to include moderate-income households.

Figure 2

Appropriations of Funding for the School Facility Fee Programs

(In Millions)

Program	1998-99	1999-00	2000-01	2001-02	2002-03	Total
Economically Distressed Areas	\$3.5	\$7.0	\$7.0	\$7.0	\$3.5	\$28.0
Sales Price Limit	3.5	7.0	7.0	7.0	3.5	28.0
Moderate-Income First-Time Home Buyers	6.5	13.0	13.0	13.0	6.5	52.0
Multifamily Housing	6.5	13.0	13.0	13.0	6.5	52.0
Totals	\$20.0	\$40.0	\$40.0	\$40.0	\$20.0	\$160.0

Figure 3

Single-Family Program Expenditures

*Through August 31, 2000
(Dollars In Millions)*

Program	Available Funds	Expenditures	Number of Approved Applications
Economically Distressed Areas	\$17.5	\$0.2	75
Sales Price Limit	17.5	0.0	1
Moderate-Income First-Time Home Buyers	32.5	1.6	672
Totals	\$67.5	\$1.8	748

As of September 2000, home buyers in 22 counties had received funding from the state. Four counties—Fresno, Kern, Riverside, and Tulare—represent more than 60 percent of the single-family programs’ expenditures. The concentration of applicants in the Central Valley should not be particularly surprising, given that this area is one of California’s fastest

growing housing markets and often relies on the use of developer fees to finance new school construction.

Multifamily Program. Likewise, the multifamily housing program has had limited success in funding applicants. From its allocation of \$32.5 million so far, seven projects have been funded for a total of \$1.1 million, and another 34 projects have been approved with expected expenditures of \$3.7 million. Due to the complexities of multifamily affordable housing financing and construction, the program takes a particularly long time to move from initial application to finished construction—typically a minimum of one year.

Concerns About the Programs

Our review of these housing assistance programs indicates a number of concerns with their operation, which we discuss below.

Lack of Applications Threatens Viability of Programs. Without a dramatic expansion in home buyer and multifamily developer interest in the programs, the programs will continue to be an ineffective effort to increase housing affordability. So far, CHFA has limited its marketing efforts primarily to the real estate industry, such as lenders, brokers, and real estate agents. The department is now in the process of developing a marketing strategy aimed at the general public. The CHFA hopes that a greater awareness by the public of the programs will expand applications.

While increased public awareness and the changes to the single-family programs implemented by Chapter 127 will increase their use somewhat in the future, the programs will be unlikely to expend their total funding allocations by the programs' sunset date of December 31, 2002. In order to expend all of the program funds by the sunset, applications would need to grow by more than 30 times over their current levels in the next two years.

Similar Home Buyers Treated Differently. Home buyers will typically pay for the local cost of their school facilities through a combination of developer fees, Mello-Roos bonds, and property tax overrides for general obligation bonds. Each of these financing mechanisms adds to the cost of housing, while providing revenues for local school facilities. The CHFA developer fee programs, however, only provide assistance for one type of these financing mechanisms. As a result, a home buyer who elects to buy a home in a school district using developer fees would be eligible for state assistance. Another similar home buyer opting to purchase a home in a district using Mello-Roos bonds would not be eligible for any assistance. Similarly, purchasers of resale homes, including first-time home

buyers, are not eligible for any assistance—even though they will likely bear the cost of school facility repair or reconstruction costs through some other financing means.

Because developer fees are not the sole method of taxing home buyers for the cost of school facilities, providing assistance based on the amount of developer fees paid excludes home buyers taxed in the alternate ways. We find little policy rationale for assisting home buyers in districts financing school facilities with developer fees but providing no assistance to others in districts which opt for other financing alternatives.

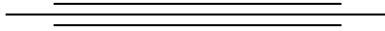
Programs Not Targeted to Highest Need. The developer fee reimbursement programs do not appear to be targeted to the Californians most in need of housing assistance. Given the limited level of housing assistance available to Californians, these programs fail to strategically target assistance for the “highest and best use” of state General Fund housing dollars.

- ***Funds Spent in Most Affordable Areas.*** The Central Valley—where the majority of program funds have been allocated—is one of the state’s most affordable markets for home buyers. For instance, measured in terms of the percentage of households that can afford a median-priced home in a region, the Bay Area, Central Coast, and most of Southern California are less affordable than the Central Valley. Consequently, the program is not providing significant amounts of assistance in the regions of the state where housing affordability problems are most severe. While developer fees may increase the cost of housing in the Central Valley, other regions suffer from more severe housing affordability problems due to a variety of other factors, such as high land costs, other types of development fees, and regulatory barriers.
- ***Recipients May Not Have the Highest Need.*** Both the economically distressed areas and the sales price limit programs are available to existing home owners, regardless of income, who are moving to a newly constructed home. Existing home owners have already overcome the major barriers to first-time home ownership. While the developer fee reimbursement may provide them the flexibility to purchase a slightly more expensive home, the programs will not represent the difference between renting and home ownership.

Recommend Eliminating Future Appropriations

The four developer fee programs have spent less than \$3 million of the \$100 million that has already been appropriated to them. The effect of Chapter 127’s modifications, combined with CHFA’s intensified market-

ing efforts, should increase the use of the programs somewhat. Yet, with the programs' sunset date at the end of calendar year 2002, the funds already appropriated should be sufficient to fund the programs through their conclusion. Given that, along with the above concerns raised about the programs, we recommend that the Legislature amend state law to eliminate the additional appropriations scheduled for the programs in 2001-02 and 2002-03. This action would make an additional \$60 million in one-time funds available for other, more-targeted housing programs or other legislative priorities.



DEPARTMENT OF MANAGED HEALTH CARE (2400)

The Department of Managed Health Care (DMHC) was created by Chapter 525, Statutes of 1999 (AB 78, Gallegos), to regulate health maintenance organizations. The Department of Corporations previously had this responsibility until DMHC began operations on July 1, 2000. (The Department of Insurance regulates health insurance companies.) The Knox-Keene Act specifies what regulatory activities the state must perform in this program area. These include (1) licensing health plans; (2) taking and investigating consumer complaints regarding health plans; (3) performing medical and financial exams of health plans every three and five years, respectively; (4) taking enforcement action against plans that are in violation of the act (up to and including taking over a health plan); and (5) providing an ombudsperson to assist in resolving complaints and providing information.

The budget proposes total expenditures of \$30.6 million in 2001-02—\$29.6 million for regulatory activities and \$1 million for the Office of Patient Advocate.

Financial Examinations Proposal

We recommend that the Legislature delete the \$300,000 request for consultant funds to increase the number of financial examinations of health plans performed annually because it does not provide sufficient resources to substantively increase the frequency of exams. (Reduce Item 2400-001-0933 by \$300,000.)

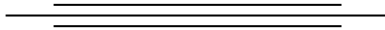
The DMHC requests \$300,000 in consultant funds to perform financial examinations of health plans more frequently. Current law requires DMHC to examine the financial status of each health plan at least once every five years. Department staff perform this function.

Citing the increasingly prevalent financial problems of health plans and the medical groups they contract with to provide medical care to

patients, DMHC proposes to increase the frequency of these examinations. This would allow closer monitoring of health plans and should result in the department detecting and resolving financial solvency issues and problems sooner. This concept has merit; however, the budget proposal would make little progress toward meeting this goal. Based on information from the department, we estimate that the \$300,000 would, at most, put health plans on an examination schedule of once every four and a half years instead of every five years. This marginal change in frequency would not appreciably increase the effectiveness of the department's oversight responsibilities.

In addition, this activity is an ongoing department responsibility for which department staff perform the examinations. The DMHC does not use consultants to perform financial examinations. Thus, it is not clear why this portion of the work would be contracted out.

An alternative discussed by DMHC in the document submitted to justify the budget proposal involved increasing the examination staff by 12 positions. This alternative would cost approximately \$1.2 million but would increase the frequency of examinations to once every three years. This three-year frequency would address the goal of early detection and resolution of financial problems. With more detailed justification, this alternative may warrant legislative consideration.



STEPHEN P. TEALE DATA CENTER (2780)

The Stephen P. Teale Data Center (TDC) is one of the state's two general purpose data centers. The other is the Health and Human Services Agency Data Center. The TDC provides a variety of information technology (IT) services to numerous state agencies which reimburse the data center for its operational costs.

The budget proposes \$92.4 million from the TDC Revolving Fund for support of the TDC in 2001-02. This is an increase of \$2.3 million, or 3 percent, above estimated current year-expenditures. The budget includes a number of increases for workload, the largest of which is a request for \$7 million for additional data processing and storage capacity equipment.

Permanent Positions Are Needed to Support Various Data Center Activities

We recommend that the Legislature decrease the Teale Data Center's proposed expenditures for staff overtime by \$116,000 and instead authorize five personnel-years to provide (1) ongoing security support for non-mainframe systems and (2) technology assistance on state information technology procurements. (Reduce Item 2780-001-0683 by \$116,000.)

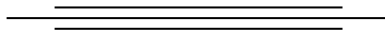
The budget proposes an on-going increase of \$454,000 for staff overtime. This includes (1) \$121,000 to implement and maintain security systems for TDC's nonmainframe systems supporting e-government projects and (2) \$333,000 to provide specialized technology assistance for the state's information technology procurements.

The TDC Provides Ongoing Support for Nonmainframe Systems. The TDC's nonmainframe services have grown by 400 percent since 1997. This growth reflects increased costs due to implementation of the Department of Information Technology's (DOIT) Data Center Consolidation initiative and the growth in Internet-based systems. The TDC is responsible for ensuring that these systems have adequate security to prevent unau-

thorized access. To perform this responsibility, TDC must conduct daily monitoring and intrusion detection checks. In addition, TDC must continue to install and maintain security software and hardware on all nonmainframe systems.

The TDC Provides Technology Expertise on Business-Based Procurements. In an effort to reduce project failures, the DOIT and the Department of Finance have required that procurements for large state IT projects which support critical services be “business based” as opposed to “technology based.” This means that the department describes its operations and vendors propose technology solutions to improve those operations. According to TDC, departments and the Department of General Services request TDC staff to act as technical advisors on these large procurement efforts to ensure the proposed technology is sound and has the capacity to meet the state’s business requirements. The TDC has never been staffed to perform these functions.

The TDC Should Not Use Overtime for Security Maintenance and Procurement Advisement Tasks. Both of the proposed activities—the security maintenance and the procurement assistance—which TDC proposed to staff through overtime are ongoing in nature. As a result, these functions are more appropriately carried out by permanent departmental staff assigned on a daily basis to perform these functions. An additional advantage is that permanent staff can perform these functions at less cost than overtime, resulting in a expenditure authority reduction of \$116,000. For these reasons, we recommend that the Legislature authorize five additional personnel years and decrease TDC’s expenditure authority by \$116,000 for personnel services. This would leave a total of \$338,000 from the original proposal.



TECHNOLOGY, TRADE, AND COMMERCE AGENCY (2920)

The Technology, Trade, and Commerce Agency, created in 1992, is the state's primary economic development entity for promoting the establishment, retention, and expansion of business, employment, and international trade in California. It promotes tourism and foreign investment as well. The agency also has been designated as the entity leading the state's efforts in defense conversion.

The budget proposes expenditures of \$331.2 million from various funds, including \$100.9 million from the General Fund, for the agency in 2001-02. The total budget is \$16.4 million, or 4.7 percent, less than estimated current-year expenditures. This decrease is due primarily to an \$8 million reduction in one-time General Fund expenditures for the Small Business Loan Guarantee program and an \$8.9 million reduction in spending for the removal and replacement of underground storage tanks.

Vague Proposal for Consultant Funds for Military Base Retention and Reuse

We recommend that the Legislature (1) delete \$100,000 of the requested contract funds because they are proposed for lobbying activities and (2) approve the remaining \$400,000 request for contract funds for one year only because the agency has not provided a more definite plan for the funds. (Reduce Item 2920-001-0001 by \$100,000.)

The budget proposes \$3.6 million General Fund in each of the next two years for the Office of Military Base Retention and Reuse, which was established by Chapter 952, Statutes of 1998 (AB 639, Alby). This amount includes:

- \$3 million to continue the Defense Adjustment Matching (DAM) Grant program at its current funding level, as commu-

nities move from planning to implementation of base reuse strategies. These grants are to help local entities meet federal grant matching requirements.

- \$500,000 in contract funds.
- \$98,000 to change funding from the California Economic Development Grant and Loan Fund to the General Fund to support the existing position that administers the DAM Grant program. (Fewer outstanding loans have reduced repayments into the current fund source.)

Chapter 425, Statutes of 1999 (SB 1099, Knight), created the California Defense Retention and Conversion Council and specified particular activities related to retaining existing military bases and converting closed military bases for other uses. During last year's budget process, the Legislature approved \$100,000 in consultant funds each for 2000-01 and 2001-02 for projects required by Chapter 425, including a study on the encroachment of development upon military bases, development of a base retention strategic plan, and an update of the existing base reuse strategic plan. However, according to the agency, the budgeted funds are not sufficient to complete these required reports. Thus, the agency proposes an additional \$500,000 in contract funds for each of the next two years to develop the state's base retention efforts for anticipated base closure decisions. This funding includes \$300,000 for data collection and research-related work, \$100,000 for "development of a clearinghouse" for information related to the federal Department of Defense, and \$100,000 for lobbying activities—"marketing, travel, congressional/legislative interface and Department of Defense networking."

Although the proposed research and clearinghouse activities are authorized by Chapter 425, the agency should have more definite plans for the proposed additional consultant funds to better inform the Legislature of planned retention-related activities. Consequently, we recommend approval of the funds requested for these purposes for the budget year only. In addition, it is not clear why the agency needs to spend consultant funds on lobbying activities, given the state's representation by the California congressional delegation and the presence of the Governor's Washington, D.C. office. Therefore, we recommend that the Legislature delete the \$100,000 for lobbying efforts and approve the remaining \$400,000 requested for one year only. Future funding requests should include more detailed plans as these retention programs authorized by statute get underway.

Augmentation Proposed for the California Technology Investment Partnership (CalTIP) Program Lacks Specifics

We recommend that the Legislature delete the \$6.2 million request to augment the California Technology Investment Partnership program because the proposal lacks necessary specifics to keep the Legislature informed of proposed program activities. (Reduce Item 2920-001-0001 by \$6.2 million.)

The budget proposes a \$6.2 million increase in funding for the CalTIP program. The program is budgeted at \$8 million in the current year—\$6 million in ongoing funding, and a one-time additional \$2 million allocation. The CalTIP program provides matching grants of about \$200,000 on average to small- and medium-sized businesses receiving federal grant funds to assist in the development of marketable technologies. The \$6.2 million requested includes:

- \$5 million (on a one-time basis) to increase the number of grants.
- \$1 million for the regional technology alliances (RTAs), nonprofit organizations that administer the program for the agency.
- \$113,000 for additional grant audits, which are currently performed by the Department of Finance (DOF).
- \$50,000 for outreach and communications—such as attendance at regional events, Web site design and maintenance, and miscellaneous expenses like postage.

This proposal lacks firm plans for the proposed funding. First, according to the agency, as much as \$1.5 million of the \$5 million for additional grants may be set aside for four existing university-affiliated institutes that provide small technology-related businesses access to research and development activities. (These institutes are located at the California Institute of Technology; University of Southern California; University of California, San Diego; and University of California, Berkeley.) It is not clear what specific activities this would entail or how the funds would be allocated. Similarly, the agency states that the RTA funding is for administrative costs and expanding the “geographical coverage of the RTA network” by establishing new centers. The agency mentions Sacramento, the San Joaquin Valley, and the Inland Empire as areas that are underserved by the existing RTAs. However, the agency has not made a specific RTA proposal to justify the requested funds.

With respect to the outreach and communications request, funding for these items should come from the program’s or agency’s existing allocations. In particular, we note that the agency received funding and positions in the current year for Web site development. With respect to the

auditing request, the current auditing performed by DOF should be sufficient. Thus, the request for additional audit funds is not necessary.

Given the concerns discussed above, especially the lack of definite plans for the proposed funding, we recommend that the Legislature delete the \$6.2 million request.

ENERGY RESOURCES CONSERVATION AND DEVELOPMENT COMMISSION (3360)

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

The budget proposes commission expenditures of \$210.8 million from various state and federal funds in 2001-02. This is \$106.1 million, or 33 percent, less than current-year estimated expenditures. This large reduction is mainly due to (1) one-time General Fund monies appropriated in Chapter 329, Statutes of 2000 (AB 970, Ducheny), for a \$50 million energy conservation grant program and an expedited power plant siting process; (2) Public Interest Energy Research (PIER) program funds carried over into the current year and an assumption that no PIER funds will be carried over into 2001-02; and (3) the near exhaustion of Petroleum Violation Escrow Account (PVEA) funds in the current year. These reductions are partially offset by increased expenditures in the budget year of (1) \$10.6 million General Fund for alternative fuel projects, (2) \$5.9 million (\$3.2 million General Fund) for electricity-related analysis and energy efficiency standards development, and (3) \$3.1 million General Fund for increasing workload associated with the Energy Facilities Siting Program.

Petroleum Violation Escrow Account

In the "Crosscutting Issues" section of this chapter, we discuss the history of PVEA and the fall off of settlement revenues into the account. We recommend that the Energy Commission report to the Legislature, prior to budget hearings, on a multiyear projection of expected administrative costs and interest earnings, so that the Legislature can determine

how many years PVEA can be expected to provide some funding for energy-related projects.

ENERGY-RELATED PROPOSALS

Additional Resources for Siting Program

We withhold recommendation on the \$3.1 million General Fund request for 19 three-year limited-term positions (16 continuing and 3 new positions) and consulting funds for anticipated workload in the Energy Facilities Siting program until the commission provides an updated schedule of expected application filing dates and corresponding workload projections prior to budget hearings. Further, we recommend that if the Legislature approves an augmentation, it should be funded from the Energy Resources Programs Account rather than the General Fund.

The commission's Energy Facilities Siting program was budgeted at \$19.2 million and 90 positions for the current year. The budget proposes \$3.1 million from the General Fund for 19 three-year limited-term positions (continuation of 16 positions created pursuant to Chapter 329, plus 3 new positions) and additional consultant contracts for the program in 2001-02. The proposal is based on the commission's projection of increased workload related to reviewing energy facility siting applications the commission currently expects to receive in 2001-02.

The Warren-Alquist Act requires commission approval of the construction of electricity-generating power plants, unless the plant generates less than 50 megawatts of electricity or is a hydroelectric, wind, or solar facility. After approving a proposed power plant, the act requires the commission to ensure that the facility is in compliance with all applicable federal, state, and local laws, as well as any conditions of certification required by the commission. The commission must approve any modifications to these plants. For plants not subject to its jurisdiction (such as those that predate the siting approval process), the commission must approve plant modifications unless the modifications meet the megawatt or type-of-facility exclusions noted above.

Anticipated Filing Dates Tend to Slip. The commission periodically updates its schedule of when it expects project proponents to file applications for the siting review process. This schedule is adjusted frequently as project details often change as projects develop, requiring proponents to file the siting application later than initially expected. These adjustments then alter the commission's staffing needs. As a result, we withhold recommendation on the \$3.1 million request until the commission provides an updated schedule of expected application filing dates and

corresponding workload projections prior to budget hearings. In addition, the commission should report on the status of new plant construction and actions to expedite approval and construction of power plants.

Fund Source. The commission's power plant siting program has historically been funded from the Energy Resources Programs Account (ERPA), which is supported by a surcharge on ratepayers' electricity bills. However, the budget request proposes an ongoing amount of \$3.1 million from the General Fund to support this activity. We recommend that if the Legislature approves an augmentation to the siting program, it should be funded from ERPA, consistent with program and department history. We note that the proposed ERPA fund balance at the end of the budget year, if all proposals in the Governor's budget were adopted, would be \$2.7 million, or \$0.4 million less than necessary to support this proposal. However, as discussed below, we recommend the Legislature shift \$3.5 million of one-time expenditures proposed for energy efficiency and alternative energy grant programs from ERPA to the General Fund. Thus, for the Governor's energy-related proposals, our recommendations would result in one-time expenditures receiving General Fund support, while ongoing responsibilities would be supported by ERPA. This would provide sufficient resources in ERPA to support the siting proposal.

Long Term Energy Baseload Reduction Initiative

We recommend that the Legislature approve the \$2.8 million General Fund request proposed for electricity demand analysis on a one-time basis as the Energy Commission has not made the case that General Fund support is needed on an ongoing basis. We further recommend that the Legislature approve \$3.5 million for one-time energy efficiency proposals and solar and distributed generation grant programs from the General Fund instead of the Energy Resources Programs Account. (Augment Item 3360-001-0001 by \$3.5 million and reduce Item 3360-001-0465 by \$3.5 million.)

The Governor's budget proposes \$5.9 million (\$3.2 million General Fund) for a Long-Term Energy Baseload Reduction Initiative as outlined in Figure 1 (see next page).

Customer Characteristics Survey. Most of the General Fund augmentation is requested for a proposed customer characteristics survey. The commission would collect and analyze data on electricity use across all sectors—residential, commercial, and industrial—to improve its demand analysis models. According to the commission, the total annual cost of this proposed survey is \$4.5 million. While the commission requests \$2.8 million General Fund annually, the remaining \$1.7 million would be provided by the Public Utilities Commission (PUC) from a ratepayer surcharge

Figure 1

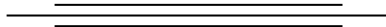
California Energy Commission Long Term Energy Baseload Reduction Initiative

(In Thousands)

	Proposed Amount		
	General Fund	Special Funds	One-Time/ Ongoing
Electricity Analysis			
Customer characteristics survey. Collect and analyze data on electricity use for demand analysis models.	\$2,800		Ongoing
New market functions. Analyze (1) market mechanisms and (2) consumer response to choice of electricity provider, price, and demand reduction programs.	300		One-time
Updates of existing models. Modify models of (1) the electricity transmission system and (2) natural gas supply to capture short-term issues like pipeline capacity and price trends.	130		Ongoing
Renewable Energy			
Renewable Energy Program. Additional consultant funds for program administration.		\$175	Ongoing
Energy Efficiency			
Building energy efficiency standards. Update as required by Chapter 329, Statutes of 2000 (AB 970, Ducheny).		\$1,351	One-time
Building department enforcement. Data collection, local assistance, and updates to improve compliance.		300	One-time
Training building departments, builders, and consumers. Local and interactive Internet-based training.		300	One-time
PLACE³S. Demonstration project for local governments to incorporate energy efficiency and alternative generation in land use plans.		300	One-time
Appliance database. Maintain an existing database of energy efficiency ratings on appliances.		200	One-time
Totals	\$3,230	\$2,626	

that supports conservation and energy efficiency programs administered by the utilities and overseen by PUC. These utility program funds currently provide approximately \$3 million for such surveys. The PUC, however, based on its assessment of priorities, has reallocated \$1.3 million in funding to other purposes and has decided to fund only \$1.7 million for this survey in the budget year. In view of the current energy situation, the PUC decision to only partially fund this program in the budget year may be appropriate. It is not clear, however, that partial funding should be on an ongoing basis. Thus, we recommend that the Legislature approve the \$2.8 million request for one year only. This recognizes the fact that PUC could reassess priorities next year and allocate additional funds for this purpose.

Switch Funding to General Fund From ERPA. As discussed above, we believe the ongoing commission programs, such as power plant siting, should be funded from ERPA. To accommodate this, one-time proposals could be supported by the General Fund as necessary to free up ERPA funds for the ongoing programs. As noted above, the \$3.1 million siting proposal exceeds the proposed \$2.7 million fund balance at the end of 2001-02. The budget, however, proposes \$3.5 million in ERPA support for one-time projects—\$2.5 million for energy efficiency activities (see Figure 1) and \$1 million for Solar and Distributed Generation Grant programs, pursuant to Chapter 537, Statutes of 2000 (SB 1345, Peace). These proposals appear to have merit. As a result, we recommend that the Legislature approve this \$3.5 million in proposed one-time spending from the General Fund instead of ERPA. This would provide sufficient resources in ERPA to support the siting proposal.



ENERGY INITIATIVES (3365)

General Fund Monies Set Aside For Energy-Related Programs

We withhold recommendation on the \$1 billion General Fund request for energy-related projects pending receipt and review of proposals for allocating these funds.

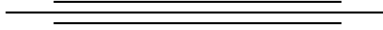
The Governor's budget includes a \$1 billion General Fund set-aside for energy initiatives to address the state's energy crisis. Proposed budget bill language specifies that (1) the funds are for "projects awarded by the Governor's Clean Energy Green Team" and (2) allocation of the amount appropriated will be subject to legislation.

Chapter 329, Statutes of 2000 (AB 970, Ducheny), created the Green Team to (1) provide pertinent information (pollution control technology and air emissions offsets, for example) and assistance (such as acquiring local permits) on request to companies wanting to build power plants. Chapter 329 also requires the Green Team to develop recommendations for low- or zero-interest financing for renewable energy. The Green Team consists of the following government entities:

- **State Departments.** Heads of the Electricity Oversight Board, Public Utilities Commission, Energy Commission, and Governor's Office of Planning and Research.
- **State Agencies.** Secretaries of Environmental Protection; Resources; and Technology, Trade, and Commerce.
- **Local/Regional.** Representatives from air quality management districts.
- **Federal.** Representatives from the Environmental Protection Agency, and Fish and Wildlife Services.

Prior to appropriating funds for energy initiatives, the Legislature should have information on the types of projects that would be funded,

how the projects would be selected, and the criteria projects must meet to qualify for funding. This information, at a minimum, is needed for the Legislature to evaluate the appropriate level of funding and the benefit of undertaking proposed initiatives. At this time, however, there are no supporting documents for this \$1 billion proposal. Pending receipt and review of this information, we withhold recommendation on the request.



HEALTH AND HUMAN SERVICES AGENCY DATA CENTER (4130)

The Health and Human Services Agency Data Center (HHSDC) provides information technology services, including computer and communications network services, to the various departments within the Health and Human Services Agency (HHSA). The center also provides services to other state entities and various local jurisdictions. The cost of the center's operations is fully reimbursed by its clients.

The budget proposes \$306.1 million for support of the data center in 2001-02, which is an increase of \$19.4 million, or 6 percent, above estimated current-year expenditures. The budget includes a number of increases for workload, the largest of which is a request for \$7.5 million for additional data processing and storage capability and telecommunications equipment. It also includes a number of decreases for completion of various aspects of certain large information technology (IT) projects.

SYSTEM MANAGEMENT SERVICES

Expenditure Authority for Additional Oversight Activities Is Unnecessary

We recommend that the Legislature reduce the Health and Human Services Agency Data Center (HHSDC) expenditure authority by \$524,000 for additional oversight activities by the Department of Information Technology (DOIT) since HHSDC has never used this expenditure authority nor can DOIT identify the activities that will be funded. (Reduce Item 4130-001-0632 by \$524,000.)

In 1999, the Department of Information Technology (DOIT) required HHSDC to increase its expenditure authority by \$370,000 so that DOIT, through the use of consultants, could provide additional oversight for its

county-based projects. The budget proposes to increase HHSDC's expenditure authority by an additional \$154,000 to allow DOIT to acquire additional oversight consulting services on its county-based projects.

The DOIT Has Never Used Additional Expenditure Authority. At that time this analysis was prepared, DOIT has never acquired consulting services for the additional oversight activities, and therefore HHSDC has never needed the additional expenditure authority for this purpose. In addition, DOIT is unable to specify exactly what oversight activities the additional consulting services will provide. For these reasons, we recommend that the Legislature reduce HHSDC's expenditure authority by \$524,000.

Software Costs Absorbable Within Current Overhead Rate

We recommend that the Legislature reduce expenditure authority by \$78,000 since the Health and Human Services Agency Data Center's overhead rate provides adequate expenditure authority to fund project management software for county-based projects. (Reduce Item 4130-001-0632 by \$78,000.)

The budget proposes to increase HHSDC's expenditure authority by \$78,000 to purchase project management software for the Child Welfare System/Case Management System (CWS/CMS) project and the Statewide Automated Welfare System (SAWS) oversight project. In 2000, the HHSDC required that its county-based projects all use the same software product to create project management plans. The HHSDC proposes to charge a portion of the software purchase and maintenance costs to each project.

The HHSDC Overhead Charge Should Cover the Cost of Software. Currently, the HHSDC charges each of its county projects a 20 percent overhead rate to reimburse it for providing overall support to the projects. The HHSDC's total overhead charge for the budget year is \$4.6 million. Since HHSDC already receives funds to cover the cost of providing overall support to the projects, we recommend that the Legislature reject the proposal. We further recommend the Legislature direct HHSDC to fund the software and ongoing maintenance within its current 20 percent overhead rate.

Child Welfare Services/Case Management System Maintenance and Operations Issues

We recommend that the Legislature decrease the proposed expenditures for the Child Welfare Services/Case Management System Maintenance and Operations (M&O) by \$411,000 and instead authorize three personnel-years for the Health and Human Services Agency Data Center (HHSDC) to provide ongoing support for the local area network. In

addition, we recommend that the Legislature adopt budget control language requiring HHSDC to update its five-year M&O plan prior to an increase in its expenditure authority. (Reduce Item 4130-001-0632 by \$411,000.)

The budget proposes to increase HHSDC's expenditure authority by \$20.4 million for the ongoing maintenance and operation (M&O) of the Child Welfare Services/Case Management (CWS/CMS) system. The CWS/CMS system provides a statewide database, case management tools, and reporting system for the state's Child Welfare Services program. The project has completed development, is operational in all counties, and has now moved into the M&O phase.

The CSW/CMS M&O Plan. The M&O phase of a system consists of activities related to the ongoing performance, availability, and usability of a completed system. A typical M&O activity would be the replacement of obsolete personal computers and printers and annual modifications to the software. The budget proposes an expenditure authority increase of \$19.6 million to replace personal computers, printers, telecommunications equipment, and upgrade software. This proposal represents the second year in CWS/CMS' five-year M&O plan.

The CWS/CMS Project Should Support Its Own Local Area Network (LAN). The budget also proposes \$625,000 in consulting services to support the CWS/CMS project's LAN. The HHSDC intends to transition the support of the CWS/CMS project LAN from the current M&O contractor to another contractor.

Analyst's Concerns. We have two concerns with this budget proposal. First, the proposed LAN support activity already is ongoing in nature. As a result, it is more appropriate to use permanent departmental staff assigned to perform these functions on a daily basis than contract consultants. An additional advantage is that permanent staff can perform these functions at a lower cost than a contractor.

Our second concern is that the budget proposal is inconsistent with CWS/CMS' approved five-year M&O plan. It is our understanding that HHSDC has shifted some M&O activities between years. These shifts were made to address incompatibilities between the current and proposed replacement hardware and software. We agree with the need to replace the specified hardware and software; however, we believe that the five-year M&O plan should be updated to appropriately reflect the funding shifts in activities prior to expenditure of funds. Such a process would also be consistent with DOIT's project approval letter which requires HHSDC to update the CWS/CMS plan on an annual basis. The CWS/CMS plan was last updated November 1999.

Analyst's Recommendations. To address these concerns, we recommend that the Legislature take two actions. First, with regards to the ongoing LAN support activities, we recommend that the Legislature authorize three additional personnel-years and decrease HHSDC's expenditure authority by \$411,000. This would leave a total of \$213,000 from the original proposal which would fully fund these positions.

Second, we recommend that the Legislature adopt the following budget control language requiring HHSDC to update its five-year M&O plan for CWS/CMS prior to an increase in its expenditure authority.

Upon notification by the Department of Information Technology of its approval of the amended Child Welfare Systems/Case Management System Five-Year Maintenance and Operation plan, the Department of Finance may authorize no sooner than 30 days after providing notification to the Chair of the Joint Legislative Budget Committee and the chairs of the fiscal committees of both houses an expenditure authority increase of \$19,600,000 to Item 4130-001-0632.

Risk Mitigation Plan Needed for Replacement of CWS/CMS Servers

We recommend that the Legislature adopt budget bill language requiring the Health and Human Services Agency Data Center to complete a risk mitigation plan for the child welfare services/case management system prior to an increase in its expenditure authority.

The budget proposes to increase HHSDC's expenditure authority by \$7.6 million to replace the servers supporting the CWS/CMS system. The proposal would replace 432 servers and upgrade the server operating systems by July 2002.

Server Replacement Project Does Not Have a Risk Mitigation Plan. State policy requires that every automation project complete a risk mitigation plan that considers (1) the potential business disruptions that could occur while implementing the project and (2) the actions the state will take to reduce or "mitigate" those risks. For example, a server replacement project could cause a business disruption when a server is replaced and, for unknown technical reasons, cause case workers to be unable to access case files. With a risk mitigation plan, the state and the counties would predetermine (1) what to do to *prevent* such a disruption and (2) what to do should the disruption actually *take place*. To our knowledge, the HHSDC did not complete a risk mitigation plan for this proposal.

Analyst's Recommendation. For this reason, we recommend that the Legislature direct HHSDC to complete a risk mitigation plan prior to replacing the CWS/CMS servers. The plan should specify (1) the potential business disruptions that could happen while replacing the CWS/CMS

servers and (2) the actions that HHSDC, the Department of Social Services, and the counties will take to minimize those disruptions. The plan shall be adopted prior to an increase in HHSDC's expenditure authority for CWS/CMS's server replacement. The following budget bill language is consistent with this recommendation.

Upon notification by the Department of Information Technology of its approval of a risk mitigation plan for Child Welfare Systems/Case Management System Server Replacement Project, the Department of Finance may authorize no sooner than 30 days after providing notification to the Chair of the Joint Legislative Budget Committee and the chairs of the fiscal committees of both houses an expenditure authority increase of \$7,600,000 to Item 4130-001-0632.

STATEWIDE AUTOMATED WELFARE SYSTEM (SAWS)

Background

Statewide Automation Welfare System. The purpose of SAWS is to provide improved and uniform IT capability to county welfare operations. The system is being delivered through a state partnership with the counties, each of which has chosen to be in one of four consortia. Figure 1 shows the four consortia, the participating counties, and the current status of each. The HHSDC provides oversight for the four SAWS consortia by preparing project documents, procuring Independent Verification and Validation services, reviewing consortia deliverables, and approving and tracking expenditures. The actual implementation of the systems is done by private contractors.

The SAWS Technical Architecture (SAWS-TA) Project Terminated. The final component implementing the overall SAWS project is the exchange of data between all four consortium systems. This final project component was originally named the SAWS-TA Project. This project was intended to (1) exchange data among the four consortia for eligibility, fraud detection, and case management purposes; (2) provide an interface for the consortia with other state automation systems; and (3) connect the consortia and state agencies to meet state and federal reporting requirements. The HHSDC discontinued the project in February 1999 due to difficulties in implementing the proposed technology within a reasonable budget.

Welfare Data Tracking Implementation Project (WDTIP) to Be Completed. The SAWS-TA project was replaced by four separate projects, each designed to share data and provide connections between the consortia. The first of these projects is WDTIP which would allow the four consortia to share client information to determine time-on-aid. In December 2001,

the WDTIP project will be complete, and the budget proposes a reduction of \$2.2 million to reflect WDTIP's statewide implementation.

Figure 1**Statewide Automated Welfare System (SAWS) Consortia**

	Status	Proposed Budget Change
Interim SAWS (ISAWS)		
35 counties: Alpine, Amador, Butte, Calaveras, Colusa, Del Norte, El Dorado, Glenn, Humboldt, Imperial, Inyo, Kern, Kings, Lake, Lassen, Madera, Marin, Mariposa, Mendocino, Modoc, Mono, Monterey, Napa, Nevada, Plumas, San Benito, San Joaquin, Shasta, Sierra, Siskiyou, Sutter, Tehama, Trinity, Tuolumne, Yuba	Working in all 35 counties.	\$3.2 million
Los Angeles Eligibility Automated Determination, Evaluation, and Reporting (LEADER) System		
1 county: Los Angeles	Implementation suspended in January 2000 due to technical problems. Implementation resumed in October 2000; completion scheduled for April 2001.	None
Welfare Client Data System (WCDS)		
18 counties: Alameda, Contra Costa, Fresno, Orange, Placer, Sacramento, San Diego, San Francisco, San Luis Obispo, San Mateo, Santa Barbara, Santa Clara, Santa Cruz, Solano, Sonoma, Tulare, Ventura, Yolo	Software development in progress. Consortium wide implementation to begin 2002.	None
Consortium IV (C-IV)		
4 counties: Merced, Riverside, San Bernardino, Stanislaus	Software development in progress. Consortium wide implementation to begin 2003.	None

Need for SAWS Strategic Plan

We recommend that the Legislature direct the Health and Human Services Agency and the Department of Social Services to complete a Statewide Automated Welfare System (SAWS) strategic plan that (1) describes the program objectives the state will achieve with SAWS implementation and (2) identifies the project "check-points" where the state will reassess its strategy for welfare automation.

Background. During the 2000-01 budget hearings, the Legislature directed the administration to assess the state's strategy for welfare automation and the continued need for four distinct consortium systems. In response, HHSA acquired consulting services and completed this assessment in July 2000. The assessment concluded that the state's welfare automation strategy was still viable and would meet the needs of the state and counties. In addition, the assessment concluded that the state should develop a SAWS strategic plan to ensure that the automation systems were meeting specific program goals and objectives. The assessment also recommended that the state identify "check-points" which would allow the SAWS development efforts to be periodically reassessed. The purpose of the checkpoints is to ensure that the automation goals were still achievable and the program goals and objectives were being met.

Need for SAWS Strategic Plan and Project Check-Points. We agree with the recommendations made to the agency which are consistent with good IT practices. (For a discussion of IT best practices, see our December 1998 report entitled *State Should Employ "Best Practices" on Information Technology Projects.*) In addition, we understand that the administration is committed to implementing these recommendations. Therefore, we recommend that the Legislature adopt the following supplemental report language directing HHSA and the Department of Social Services (DSS) to complete a SAWS Strategic Plan.

The Health and Human Services Agency and the Department of Social Services shall, by May 1, 2002, provide a report to the chairs of the budget committees in each house and the Chair of the Joint Legislative Budget Committee which describes the state's program objectives in implementing the Statewide Automated Welfare System (SAWS). The report shall identify: (1) measurable program objectives and benefits that the state will achieve through automation and (2) the SAWS milestones at which the state will reassess the automation approach for the state's welfare system.

The LEADER Has Significant Performance Problems

We recommend that the Health and Human Services Agency Data Center and the Department of Social Services report at budget hearings

on (1) the implementation status of the Los Angeles Eligibility Automated Determination, Evaluation and Report (LEADER) project and (2) the actions the state can take to prevent future performance and capacity problems.

The LEADER Has Significant Performance Problems. In the summer of 1999, Los Angeles County began implementation of its welfare automation system, Los Angeles Eligibility Automated Determination, Evaluation and Report (LEADER). By the fall of 1999, Los Angeles County began experiencing severe performance problems when the LEADER mainframe systems were unable to process large volumes of caseload data. In response, Los Angeles County, in consultation with HHSDC, directed the vendor to address the technical problems. The LEADER implementation was suspended for ten months while the vendor implemented and tested various technical fixes. In October 2000, Los Angeles County resumed LEADER implementation and anticipates county-wide implementation by April 2001.

Administration Should Report on Implementation of LEADER and Actions to Prevent Future Problems. Because of the recent significant delays, we recommend that HHSDC and DSS report at budget hearings on the current status of LEADER implementation. In addition, we recommend that HHSDC and DSS describe what actions they plan to take should future performance problems be encountered.

Interim SAWS Will Need to Operate for Another Five Years

We recommend that the Legislature direct the Health and Human Services Agency Data Center and the Interim Statewide Automated Welfare System (ISAWS) Consortium to develop a five-year Maintenance and Operation Plan which describes the activities and funding needs for the ongoing support and operation of the ISAWS system.

The budget proposes a \$3.2 million expenditure increase and a decrease of one position for the ongoing support and maintenance of the Interim Statewide Automated Welfare System (ISAWS).

Background. The ISAWS system consortium was completed in 1998 and continues to operate in its 35 counties. The system itself consists of mainframes and midrange servers housed at HHSDC, and personal computers located throughout the 35 counties. The current contract for the software maintenance vendor is set to expire in December 2003.

In addition, the ISAWS consortium also is planning to replace its current ISAWS system with either the Welfare Case Data System (WCDS) or the Consortium IV (C-IV) system; however the new replacement system

will be unavailable to the ISAWS consortium until 2004 or 2005 when the WCDS and C-IV implementations are complete.

Direct Administration to Develop a Five-Year Maintenance and Operation (M&O) Plan. Since the ISAWS system will need to operate at least another five years, including the time needed to move all counties from ISAWS to the new system, we recommend that the Legislature direct the administration to develop a five-year M&O Plan similar to the one developed for the CWS/CMS system. The following supplemental report language is consistent with this recommendation.

The Health and Human Services Agency Data Center and the Department of Social Services, in consultation with the Department of Information Technology (DOIT) and the Department of Finance, shall, by January 1, 2002, provide a report to the chairs of the budget committees in each house and the Chair of the Joint Legislative Budget Committee which describes the five-year maintenance and operation plan for the Interim Statewide Automated Welfare System. The plan shall be prepared in accordance with DOIT's policy for maintenance and operation planning.

STATUS OF OTHER PROJECTS

Electronic Benefits Transfer Should Submit Revised Proposal

We recommend that the Legislature not take action on the proposed \$104,000 expenditure and instead direct the administration to (1) complete its review of the Electronic Benefit Transfer contract and final funding estimates and (2) submit a revised budget proposal at the time of the May Revision.

The budget proposes a \$104,000 increase to HHSDC's expenditure authority to reflect project schedule adjustments on the Electronic Benefit Transfer (EBT) Project.

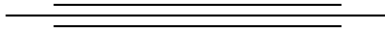
Background. Federal welfare reform legislation required all states to implement EBT systems for food stamps by October 1, 2002. The system uses debit card technology and retailer terminals to automate benefit authorizations, delivery, redemption, and financial settlement. Chapter 329, Statutes of 1998 (AB 2779, Aroner), required that the state contract with a single vendor for the implementation of California's EBT system and that the HHSDC provide the project management for the EBT project.

Procurement Has Taken Longer Than Expected. In October 1999, HHSDC began the procurement process to acquire contract services for

California's EBT system. The procurement process was delayed, and the contract is now expected to be awarded in June 2001.

Our review of the EBT project schedule indicates that HHSDC had intended to submit by January 2001 a negotiated contract and final project cost estimates to DOIT and the Department of Finance (DOF). At the time this analysis was prepared, it had not submitted these documents. The HHSDC estimates that it will receive DOIT and DOF approval of these items in June 2001 at which time it will notify the Legislature of the final cost estimates through Section 11.00 of the *2000-01 Budget Act*.

Direct Administration to Complete Cost Reviews Earlier and Submit Revised Budget Proposal. Our review indicates that the EBT Project schedule will allow DOIT and DOF four months to complete their reviews of the contract and revised cost estimates. This time schedule, however, will not permit cost information to be made available to the Legislature until after the budget hearings have been completed and the budget has been enacted. We believe it is feasible for the administration to revise its time frames for reviewing the proposed contract and funding needs and provide this information to the Legislature prior to final budget hearings. For this reason, we recommend that the Legislature direct the administration to provide an updated budget proposal at the time of the May Revision.



CALIFORNIA ARTS COUNCIL (8260)

The California Arts Council carries on a range of activities in order to further the arts in California. The council's enabling legislation directs it to (1) encourage artistic awareness and expression, (2) assist local groups in the development of arts programs, (3) promote the employment of artists in both the public and private sectors, (4) provide for the exhibition of artworks in public buildings, and (5) ensure the fullest expression of artistic potential. In carrying out this mandate, the Arts Council has focused its efforts on the development of competitive grant programs to support artists and organizations in various disciplines. In addition, in recent years the Legislature and Governor have also included funds in the Arts Council's budget for distribution to specific museums and other cultural institutions.

The Governor's budget proposes expenditures of \$75 million, mostly from the General Fund, for support of the council in 2001-02. This amount represents a decrease of \$6.7 million, from estimated current-year expenditures. This decrease is misleading, however, because the current-year budget included one-time grants to museums and cultural institutions. After adjusting for these one-time expenditures, the budget for 2001-02 actually increases ongoing programs and operations by \$6.6 million and creates a new \$20.4 million Cultural Infrastructure Development Fund (CIDF). These proposals represent a 96 percent increase to the council's ongoing programs. The Governor's budget also includes a one-time \$3 million augmentation for the "Finding Our Families. . . Finding Ourselves" exhibit at the Simon Wiesenthal Center.

New Cultural Infrastructure Development Fund Poses Questions

The Governor's budget proposes \$20.4 million for the creation of the Cultural Infrastructure Development Fund to provide grants to museums and other cultural institutions for local capital needs. We withhold recommendation on the proposed increase and recommend that the Arts

Council report to the Legislature prior to budget hearings on (1) the policy and fiscal significance of formally expanding the council's mission, (2) provisions for incorporating the proposal into the state's five-year capital outlay plan, and (3) priorities and procedures for choosing grant recipients.

Background. The California Arts Council currently funds artists and arts organizations to provide a variety of arts programs to the public. Funds are provided through a competitive grant process that relies on peer review of proposals. Over the past three years, the budget also has appropriated an average of \$27 million annually to numerous museums and other cultural institutions. These funds were earmarked for specific organizations and distributed with limited expenditure guidelines.

Budget Request. The budget requests \$20.4 million to establish the CIDF to provide grants to museums and other cultural institutions for capital needs. These capital needs are broadly defined to include rehearsal and gallery space, community centers and extra-curricular arts education facilities, renovations for handicapped accessibility and earthquake retrofitting, adapting new technology, and building management capacity. This is the first time the council would establish a formal procedure for funding infrastructure needs for the arts community. The request states that the CIDF would provide a competitive, strategic, equitable mechanism through which the state can invest resources in cultural infrastructure. The council indicates grants will be awarded pursuant to a review process developed by the administration in consultation with the Legislature, but has not provided any details for that process.

Proposal Represents a Significant Expansion of Council's Mission. Up until this year, the Arts Council has focused primarily on providing support to artists and arts organizations. We recognize that in the past the council's budget has been augmented to provide funds for specific cultural and museum projects, including capital outlay. The budget proposal, however, represents a significant new direction for the council in that it would formalize a procedure for funding local infrastructure needs for the arts community. Presumably, the council intends for creation of the CIDF to serve as an ongoing source of support for arts infrastructure. Before the council embarks on a formal new role for funding arts community infrastructure and capital outlay, it is important that it lay out what the level and scope of the state's role should be in providing such support.

Proposal Does Not Incorporate Infrastructure Funding Into State's Capital Outlay Process. Chapter 606, Statutes of 1999 (AB 1473, Hertzberg) requires the state to develop and annually update a five-year plan for identifying and establishing priorities for all state infrastructure needs. The first plan will be submitted to the Legislature along with the

2002-03 budget proposal. This new proposal for cultural infrastructure development does not address how funding the capital needs of the arts community would be part of the state's capital outlay process. We note that the most recent estimate of need exceeded \$40 billion over a five-year period. In the event that the Legislature wishes to appropriate funds for the capital outlay needs of local museums and cultural institutions beyond the budget year, it is important that the Arts Council develop a permanent process for identifying and ranking these needs in accordance with the process set forth in Chapter 606.

Development of Selection Criteria and Competitive Peer Review Process Needed. Whether the Legislature decides to provide funding for the capital needs of museums and other cultural institutions is a policy decision. If the Legislature chooses to provide additional funds in the budget year, there are a number of ways to ensure their efficient and equitable distribution. For example, establishment of a peer review panel similar to that used by the council in other program areas would allow grants to be distributed to museums and cultural organizations on a competitive basis.

A competitive peer review panel would allow funding decisions to be based on established standards and criteria. Some issues to consider when establishing these review criteria include whether the grant would: (1) be based on a formula that considered museum size, number of visitors, and educational components; (2) make funds available for capital outlay, facility purchases, or ongoing operations and programming; and (3) require a local match.

Regardless of the eligibility and criteria standards agreed upon, the competitive grant process would allow for greater accountability and oversight than the recent practice of earmarking museum and cultural institution funding.

Analyst's Recommendation. We withhold recommendation on the proposed increase and recommend the Arts Council report to the Legislature prior to budget hearings on the following: (1) the policy and fiscal significance of formally expanding its role in funding local museum and cultural infrastructure needs, including capital outlay; (2) how the council intends to conform its proposal to the state's new planning process for capital outlay as outlined in Chapter 606; and (3) additional information on funding priorities and procedures for distribution of the new fund.

Funding for Museum Exhibit Not Justified

We recommend a General Fund reduction of \$3 million for an exhibit at the Simon Wiesenthal Center, Museum of Tolerance. Earmarking funds for a specific project, rather than awarding funds on a peer review and

competitive grant basis, undermines the council's ability to establish spending priorities consistent with the statewide goals, enforce guidelines, and ensure accountability of state monies. If the Legislature approves funds for cultural infrastructure discussed above, the Simon Wiesenthal Center could apply for a grant through that program. (Delete Item 8260-103-0001 for a savings of \$3 million.)

Last year, the 2000-01 Budget Act provided a one-time appropriation of \$3 million for the initial planning and construction costs of the "Finding Our Families. . . Finding Ourselves" exhibit at the Simon Wiesenthal Center, Museum of Tolerance. At that time, the project was expected to cost \$5 million. Last year's budget also appropriated \$2 million for the center as part of an ongoing appropriation for teacher training on tolerance and diversity. The Governor's budget continues the \$2 million for training and requests an additional \$3 million for the exhibit.

We have several concerns with this proposal. First, the earmarking of funds for the Wiesenthal exhibit is inconsistent with the direction in which the council is moving both in its current procedures as well as in its budget proposal for cultural infrastructure whereby funds are disbursed as part of a peer review and competitive grant process. As an alternative, if the Legislature approves funds for cultural infrastructure as proposed by the Governor's budget, then the center could apply directly to the Arts Council for such funds and have its proposal considered alongside other projects proposed by organizations throughout the state.

In addition, there is little information to explain why the total cost of the exhibit appears to be exceeding earlier estimates by more than \$1 million. For these reasons, we find the proposal is not justified and recommend that it be deleted.

DEPARTMENT OF INDUSTRIAL RELATIONS (8350)

The mission of the Department of Industrial Relations is to protect the workforce of California, improve working conditions, and advance opportunities for profitable employment. These responsibilities are carried out through three major programs: the adjudication of workers' compensation disputes; the prevention of industrial injuries and deaths; and the enforcement of laws relating to wages, hours, and working conditions. In addition, the department regulates self-insured workers' compensation insurance plans, provides workers' compensation payments to injured workers of uninsured employers and other special categories of employees, offers conciliation services in labor disputes, and conducts and disseminates labor force research.

The Governor's budget proposes expenditures totaling \$268 million for the department in 2001-02. This is 3 percent more than estimated expenditures for the current year. The request includes \$175 million from the General Fund, 4 percent more than 2000-01 estimated expenditures.

Budget Realignment

We recommend the Legislature delete \$1.3 million from the General Fund and \$320,000 from special funds because the department has not justified the need for additional resources to fund existing salaries. (Reduce Item 8350-001-0001 by \$1.3 million and Item 8350-001-0223 by \$320,000.)

The budget includes \$1.3 million from the General Fund and \$320,000 from the Workers' Compensation Administration Revolving Fund in order to fund salaries within the Division of Workers' Compensation. According to the department, judicial and administrative positions within the division have routinely been held vacant in order to fund salaries for other employees. This request would provide additional resources to eliminate the need to hold positions vacant. However, in the budget year, the De-

partment of Finance (DOF) deleted a total of 17 vacant positions from the division but left the associated funds in the division's budget. It is not clear why the department still reports a need to hold additional positions vacant to fund existing staff salaries.

In addition, this request is based on an evaluation of one particular area of the division. However, this division has a \$101 million budget and more than 1,000 authorized positions. The department should evaluate the *overall* budget and workload for the division to determine if additional resources are needed. For these reasons, we recommend the Legislature delete the requested \$1.6 million.

Staff Redirected From Garment Manufacturing Program

We recommend the Legislature not redirect 11 positions from the garment industry wage claim resolution program because (1) insufficient workload information is available to justify the redirection, (2) the impact on the garment industry regulatory process has not been identified, and (3) the shift is inconsistent with previous legislative actions. (Reduce Item 8350-001-0001 by \$565,000 and increase Item 8350-001-3004 by \$565,000.)

The budget proposes to redirect 11 previously authorized administrative staff positions (and \$565,000 from the General Fund) from the garment wage claim resolution program to other areas within the Division of Labor Standards Enforcement (DLSE). These 11 positions were authorized on a two-year limited-term basis for DLSE in the *2000-01 Budget Act* in order to administer a new wage claim resolution process for the garment industry established by Chapter 554, Statutes of 1999 (AB 633, Steinberg). Funding for the positions was authorized from fees collected under the program.

Last year, the department indicated that the 11 positions were necessary in order for the department to meet the legislative mandates and process wage claims in a timely manner. This proposal would now shift the positions away from the garment industry program to several other areas of the division (such as the Public Works unit). The department has not shown why these positions are needed in these other areas or what impact this redirection would have on the wage claim resolution process. In addition, because the garment program is self-funded, the department agreed last year to assess a sufficient level of fees to fund the authorized positions and administer the program. This proposal would instead fund the positions from the General Fund. The department also indicates it is their intent to administratively reestablish the 11 positions for the garment program during the budget year.

Due to insufficient justification of the proposal and previous expression of legislative intent, we recommend the Legislature not approve the redirection of 11 positions. (Reduce Item 8350-001-0001 by \$565,000 and increase Item 8350-001-3004 by \$565,000.)

Workers' Safety Training Grant Program

We recommend the Legislature delete \$2.5 million and three positions from the General Fund to administer a new workers' safety training grant program because of insufficient information on how the program will be administered. (Reduce Item 8350-001-0001 by \$2.5 million.)

The budget includes \$2.5 million from the General Fund and three positions to administer a new workers' safety training grant program. The proposal would target high-hazard industries—including construction, agriculture, and government (excluding federal)—by awarding grants to employers for safety training programs. According to the department, these industries have higher rates of nonfatal occupational injuries than other industries.

While the new program targets worker safety, this proposal raises a number of policy issues that may be more appropriate to consider in separate legislation. The department reports that the Division of Occupational Safety and Health will be responsible for (1) evaluating and approving the program administration, (2) determining which employers would qualify for funding, and (3) evaluating the effectiveness of the program. The proposal, however, does not detail how eligibility for grants will be determined, what types of programs could qualify for funding, or what measures will be used to determine the effectiveness of the programs at reducing workplace hazards.

In view of the lack of information, we recommend the Legislature delete \$2.5 million under Item 8350-001-0001.

Increased Employer Education

We recommend the Legislature delete \$1.7 million from the General Fund for increased public information because the department (1) currently has sufficient resources for printing additional materials, (2) has Information Technology staff authorized to develop Internet-based information, and (3) has not prepared a Feasibility Study Report. (Reduce Item 8350-001-0001 by \$1,736,000.)

The Governor's budget includes \$1.7 million from the General Fund and one position to (1) prepare and mail informational packets four times a year to 130,000 employers statewide regarding the state's labor laws

and (2) fund a private consultant to develop new Internet-based informational resources for the department. According to the department, it received a total of \$1.3 million in the 2000-01 Budget Act for printing services to prepare written documents and publications. (As of January 2001, the department had spent a total of \$173,000 on printing services, including public information brochures.) This request would nearly double the department's printing services budget to \$2.5 million.

With regard to the information packet, it is not clear how effective the proposed 130,000 additional quarterly mailings would be at increasing workplace safety or decreasing industrial hazards. Instead of mailing 520,000 additional documents annually, the department could instead, on a priority basis, use existing resources to mail a smaller number of packets and assess the value of this approach. A future request would warrant legislative consideration if the department could demonstrate the value of such a program.

The department also has requested \$350,000 to fund a web-development consultant (\$300,000) and to conduct informational surveys (\$50,000). However, the department already has 77 authorized information technology positions, including 4 positions specifically dedicated to Internet web development. It is not clear why these positions could not implement the department's proposal. Furthermore, the department has not prepared a Feasibility Study Report, required for all such information technology projects, which would detail the business problem, the proposed solution, management plan, and economic analysis of alternatives. This is a document departments routinely prepare for information technology requests which must be reviewed by DOF and the Department of Information Technology. This document would also allow the Legislature to fully evaluate the problem identified and the solution proposed. This document should be prepared *before* funds are requested to implement this technology development project.

Based on the issues discussed above, we recommend the Legislature delete \$1.7 million under Item 8350-001-0001.

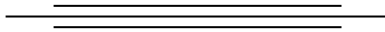
Amusement Ride Regulatory Process

We recommend the department report to the Legislature at the time of budget hearings regarding the status of the new amusement ride regulatory process established by Chapter 585, Statutes of 1999 (AB 850, Torlakson).

In 1999, the Legislature approved, and the Governor signed into law, Chapter 585 (AB 850, Torlakson), which initiated a new inspection and regulatory process for permanent amusement rides administered through

the Division of Occupational Safety and Health. The *2000-01 Budget Act* included a total of 26.5 personnel-years and \$2.2 million for the program—the same levels proposed in the budget year. The program is funded by fees collected through the regulatory process.

As of January 2001, the department had not finalized the regulations necessary to implement the program. Given the delays in implementing the program, we recommend the department report to the Legislature at the time of budget hearings regarding the status of the amusement ride inspection program and the development of administrative regulations.



DEPARTMENT OF PERSONNEL ADMINISTRATION (8380)

The Department of Personnel Administration (DPA) manages the nonmerit aspects of the state's personnel system. (The State Personnel Board manages the merit aspects.) The Ralph C. Dills Act provides for collective bargaining for most state employees. Under this act, DPA is responsible for (1) reviewing existing terms and conditions of employment subject to negotiation, (2) developing management's negotiating positions, (3) representing management in collective bargaining negotiations, and (4) administering negotiated memoranda of understanding (MOUs). The DPA also is responsible for the compensation and terms and conditions of employment of managers and other state employees not represented in the collective bargaining process.

The budget proposes total expenditures of \$51.7 million for support of the department in 2001-02. The principal funding sources are:

- \$28.1 million from the General Fund.
- \$16.6 million from reimbursements from other state departments.
- \$6.3 million from the Deferred Compensation Plan Fund.

The proposed expenditures for DPA support are \$17.2 million, or 25 percent, less than estimated current-year expenditures. This is due primarily to a reduction of \$17.2 million from the General Fund for (1) one-time expenditures in 2000-01 related to work and family issues, as negotiated in MOUs, and (2) a doubling up of costs for the rural health subsidy program in the current year.

One-Time Current-Year Funds For Collective Bargaining Consultant Should Be Deleted

We recommend that the Legislature delete \$50,000 from the department's General Fund appropriation to remove one-time, current-year consultant funds related to collective bargaining from the department's budget. (Delete \$50,000 from Item 8380-001-0001.)

The 2000-01 Budget Act includes \$50,000 (General Fund) for DPA to hire a consultant to assist with preparation of the state's policies and strategies for collective bargaining during spring 2001. This work should not be required on an ongoing basis since the bargaining is for MOUs that expire this spring. The department's budget, however, includes this item as an ongoing expenditure. Therefore, we recommend that the Legislature delete \$50,000 from DPA's budget-year General Fund appropriation.

New Collective Bargaining Agreements to Be Negotiated

The Department of Personnel Administration should report to the Legislature during budget hearings on the administration's collective bargaining proposals and the status of negotiations.

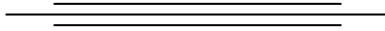
In September 1999, the Legislature approved MOUs for all of the state's 21 collective bargaining units. (This does not include employees in higher education.) These agreements are effective through June 30, 2001. The MOUs provided two 4 percent general salary increases effective July 1, 1999 and September 1, 2000. For employees not covered by collective bargaining (such as managers and supervisors), DPA approved a compensation package similar to that approved in the MOUs.

The Governor's budget does not include any budget-year funding for employee compensation. However, DPA will begin collective bargaining negotiations to replace the expiring MOUs this spring. Consequently, we anticipate the state will face some increased costs for employee compensation in 2001-02.

The Ralph C. Dills Act directs the administration and employee representatives to endeavor to reach agreement before adoption of the budget act for the ensuing year. The act further specifies that provisions of MOUs requiring the expenditure of state funds be approved by the Legislature in the annual budget act before the provisions may take effect. Historically, however, agreements often have not been reached in time for legislative consideration as part of the budget process.

In recognition of the statutory intent and the importance of these negotiations for the 2001-02 budget, we recommend that DPA report to the Legislature during budget hearings on the administration's collective

bargaining proposals and the status of negotiations. Furthermore, in our analysis of "Augmentation for Employee Compensation" (Item 9800) in this section of the *Analysis*, we have recommended that the Legislature (1) require a minimum 30-day review period between the submittal of proposed MOUs to the Legislature and hearings on the proposals to ensure that their fiscal and policy implications are fully understood and (2) review the administration's MOU proposals at the budget hearings and adopt them in the budget act (or as amendments to the act if they are not available for review during budget hearings).



DEPARTMENT OF FOOD AND AGRICULTURE (8570)

The California Department of Food and Agriculture (DFA) promotes and regulates the state's agriculture industry through marketing programs and industry inspections. The department is responsible for developing California's agricultural policies and assuring accurate weights and measures in commerce. The department also provides financial oversight to county, district, and citrus fairs.

The *2001-02 Governor's Budget* proposes \$251 million (\$99 million General Fund) in support of the department for the budget year. This is a 2 percent decrease from estimated current-year expenditures.

Comprehensive Statewide Strategic Plan Not Yet Available

We withhold recommendation on the \$112.7 million (\$71.5 million General Fund) for the Department of Food and Agriculture's Plant Pest Prevention, Detection, and Eradication programs pending receipt and review of the department's comprehensive statewide strategic plan that is to be sent to the Legislature by March 1, 2001.

The DFA's Plant Pest Prevention, Detection, and Eradication programs include screening incoming parcels for contaminated agricultural products, inspecting vehicles entering the state, monitoring pest detection traps, operating the plant pest diagnostic laboratory, administering various pest control programs, and implementing numerous emergency pest eradication programs (including the red imported fire ant and the Glassy-Winged Sharpshooter [GWSS]).

In our *Analysis of the 2000-01 Budget Bill*, we noted that because the department does not have a comprehensive statewide strategic plan for these programs, it is increasingly difficult for the Legislature to evaluate the need for funding or the impact of the total program. For example, an important function of the department is partnering with counties to pre-

vent the introduction and establishment of serious plant pests and diseases. The department, however, does not clearly lay out the responsibilities between the levels of government regarding these programs. Also, the distinction between a control versus eradication program has important programmatic and budgetary implications. Typically, a control program is funded by the agricultural industry and eradication by the General Fund. The industry directly benefits from both types of programs. In our *Analysis* we pointed out that the department needed to address the issue of appropriate cost sharing between the state and industry for the various programs. In view of these issues, we recommended that the department initiate a statewide planning process. This process would begin with identification of the state's goals and challenges with regard to these programs and result in a comprehensive statewide strategic plan.

The Legislature concurred with the need for a comprehensive plan and adopted supplemental report language directing the department to submit such a plan to the Legislature by March 1, 2001. The plan is to be a comprehensive statewide strategic plan for management and coordination of all invasive plant and pest prevention programs. In addition, in last year's budget deliberations, the Legislature denied the department's request to make several programs permanent. Instead, the programs were continued for one year and subject to reevaluation in the context of the new plan. The *2001-02 Governor's Budget* is again proposing that the Legislature approve these as permanent programs as discussed below.

Medfly Preventative Release Program. The Governor's budget proposes \$8.7 million from the General Fund and 138 positions to make this program permanent. The department began efforts to control the impact of the Mediterranean Fruit Fly (Medfly) on California's agricultural industry in 1975. Since 1980, the state has spent around \$130 million from the General Fund to support this effort, with a similar amount provided by the federal government. The department has used aerial and ground spraying, and sterile Medfly releases to fight the pest.

The current program began in 1996 and involves raising sterile Medflies and releasing them throughout a 2,100 square mile area of the Los Angeles Basin. Total program costs are \$16 million annually, shared equally between the state and the federal government. This program was approved as a five year program with a June 30, 2001 sunset date. Pending receipt of the comprehensive plan, it is not clear how this program fits into the state's overall goals for a coordinated invasive plant and pest program. Additionally, since this program is an ongoing control effort (rather than eradication), it is not clear why this program should not be funded in part, or in whole, by the agriculture industry.

Parcel Inspection Dog Teams. The Governor's budget includes \$1.9 million from the General Fund and 30 positions to make permanent the Agricultural Parcels Inspection program. This program was initiated in the 1996-97 *Budget Act*, when the Legislature approved \$895,000 from the General Fund and 14.6 personnel-years for a two-year pilot program. In the 1998-99 *Budget Act* the Legislature doubled the size of the pilot program and extended it for an additional two years. During the course of the program, the department has submitted two legislatively mandated reports on program activities.

The program includes 12 teams—consisting of an agricultural biologist, an agricultural inspector, and a dog trained to detect plant material—that are deployed in the San Francisco Bay Area, the Los Angeles Basin, and the San Diego area. As noted last year, the teams screen a small portion of all packages entering the state—approximately 1 percent to 6 percent, depending on location—and it is not clear that these inspections have a significant impact on preventing pest infestations.

Pest Detection. The department is requesting \$1.3 million from the General Fund to make permanent its trapping and detection activities for the Medfly using a new type of pest trap. This is the same program and level of funding included in the 2000-01 *Budget Act*.

Public Outreach. The department is requesting \$515,000 from the General Fund to increase public outreach activities—such as producing and distributing brochures, maintaining a telephone hotline, and maintaining a Web site. This is a \$15,000 increase from the current-year expenditure level for these purposes.

The appropriate level of state funding for the various programs in the Plant Pest Prevention, Detection, and Eradication program is dependent, to a great extent, on the information that should be included in the comprehensive statewide strategic plan. Consequently, pending receipt and review of the comprehensive statewide strategic plan, we withhold recommendation on the department's \$112.7 million request for these programs.

THE GLASSY-WINGED SHARPSHOOTER PROGRAM

We recommend the department report to the Legislature, prior to budget hearings, on the development of clear goals and measurable outcome criteria for the Pierce's Disease/Glassy-Winged Sharpshooter program.

The Governor's budget includes \$19.6 million (\$8.9 million from the General Fund, \$4.9 million from federal funds, and an anticipated \$5.8 million contribution from the wine and grape industry). This program is part of the department's Plant and Pest Prevention program and also

needs to be considered in the context of the Comprehensive Statewide Strategic plan due to the Legislature March 1, 2001.

Background

In August 1999, an outbreak of Pierce's Disease (PD), a bacteria that infects several plant species and can be particularly devastating to grape vines, was confirmed in the Temecula area in southern Riverside County. It was determined that the cause for the spread of the disease was due to a nonnative insect—the Glassy-Winged Sharpshooter (GWSS). In response to the potential harm this disease poses to the wine grape industry, the Legislature has to date appropriated \$16 million to combat the spread of the disease. In addition, the federal government and the wine industry have committed \$22 million and \$750,000, respectively, that will be spent over at least three years. Thus, to date a total of about \$39 million has been committed to this program.

These funds are to be spent in two general areas: (1) efforts to limit the spread of the disease by controlling the GWSS and (2) research on both the disease and methods to control the sharpshooter.

State-Level Responsibilities

The DFA has developed a response to the threat from PD and the GWSS by coordinating the efforts of various organizations including the U.S. Department of Agriculture (USDA), the University of California (UC), county agricultural departments, and a variety of industry representatives. With additional input from the Science Advisory Panel, the PD Advisory Task Force, and its own technical staff, the department has developed the content of the program and its goals and objectives. Although the development of program information, expertise, and structure originates on the state level, most of the implementation of the program is carried out at the county level. The state accomplishes this through contracts it has entered into with the counties. The department created and provided the counties with the PD Control Program Workplan to guide the counties in program implementation and budgeting. Thus far, the state has entered into contracts with 48 counties, at a total contract amount of approximately \$14 million. In addition the department maintains an informational Web site. Figure 1 (see next page) shows the department's current-year spending plan and what it has spent as the half-way point as of the fiscal year.

Research. In October of 1999, Chapter 627 (AB 1232, Cardoza) made available \$750,000 from the General Fund per year for three years to fund PD/GWSS research. These funds are contingent upon receiving an in-

dustry match of \$250,000 per year. The PD Research Advisory Task Force—made up of state and local agency representatives, various industry representatives, and UC scientists—evaluate the research proposals and advise the secretary on funding priorities. The federal government, through the USDA, has provided an additional \$4.2 million to aid in the research effort. To date, over 50 projects have been approved by DFA and USDA and funded. These projects include research in areas such as determining the most effective pesticides against the GWSS, how PD works inside various plants, and how GWSSs move and transmit the disease. The research effort is primarily conducted by UC.

Figure 1		
Glassy-Winged Sharpshooter Program Spending		
<i>(In Thousands)</i>		
	Budgeted	Spent^a
DFA personal services	\$2,191	\$636
DFA operation expenses and equipment	4,554	677
Contracts with counties	13,575	1,394 ^b
Totals	\$20,320	\$2,707

^a As of December 28, 2000.
^b Actual payments to counties.

Biological Controls. The department has identified possible natural predators to the GWSS. Biological controls, if effective, can replace, or at least minimize, the use of pesticides as a control agent. The DFA, USDA, and UC scientists are currently working on collection, rearing, and re-release programs.

County Level Responsibilities

As mentioned above, the counties take the lead in implementing the program on the local level. The PD Control Program Workplan developed by DFA lays out a county program made up of (1) detection and inspections, (2) containment, (3) public outreach, and (4) environmental monitoring. The county Agricultural Commissioner’s Office enters into a contract with DFA based on the county’s work plan and an estimated budget to accomplish the tasks called for in the plan.

Detection and Inspection. Most of the county level funds are spent on detection and inspection, deploying and checking a network of traps for the presence of GWSS, and inspecting nurseries and commodities throughout the county. As the program first developed the traps were “piggy backed” onto Medfly traps. This methodology has since been found to be ineffective. The department continues to adjust its trapping procedures to improve results.

Containment. If the GWSS is found, the county implements the containment response plan as required in the state contract. This includes increased surveying (searching for the GWSS) and chemical treatments if appropriate. Since this is the first full year of operation of the program, spraying done last summer and fall has yet to be fully assessed to determine the extent to which the GWSS has been eradicated.

Public Outreach. The counties also engage in a variety of public outreach programs that include meeting with growers, nursery operators, and commodity shippers. The counties hold local task force meetings and when chemical treatments are required on private residences, community information meetings are held to answer individual homeowner questions.

Environmental Monitoring. Counties work in cooperation with the state to arrange for environmental monitoring. Monitoring is conducted by the California Department of Pesticide Regulation. Decisions as to whether environmental monitoring should be adjusted or, if sufficient data show no negative effects to the environment, deleted rest with both the state and the counties.

Information Needed

As mentioned earlier in this analysis, the department is preparing a comprehensive statewide strategic plan (due to the Legislature March 1, 2001) to address the state’s overall plan for pest prevention and eradication. The GWSS program is contained within the department’s Pest Prevention and Eradication program. Accordingly, this plan should cover—specific to the PD/GWSS program—the program goals, milestones, and outcome measures for reaching these goals. Additionally, the department has not shown that it has in place a process that holds counties accountable for funds spent through county contracts. Therefore, to assist the Legislature in its oversight and appropriation of funds for this program, the department—prior to budget hearings—should provide information on:

- The process for determining that (1) the contract amount with the counties is reasonable, (2) the county spends the funds as called for in the contract, and (3) there are measurable outcomes as a result of these expenditures.

- The current- and budget-year county expenditures for each program element (detection, containment, environmental, public outreach, and research) and how each contributes, in a measurable way, to the program's goal.

Environmental Task Force Report

Concerns about the environmental and public health impacts of pesticide application to eradicate the GWSS prompted the Legislature to include language in the *2000-01 Budget Act* requiring the department to convene an Environmental Task Force made up of representatives from state and county agencies and a variety of other organizations. Members were drawn from the following:

- The Department of Pesticide Regulation.
- The State Water Resources Control Board.
- The Department of Fish and Game.
- A university-affiliated researcher.
- A grower.
- A County Agricultural Commissioner.
- Environmental and public health nongovernmental organizations.

The task force was to provide input concerning the potential adverse effects on public health and the environment from the application of pesticides to eradicate the GWSS. Also, the task force was to suggest measures that would reduce possible harm to public health and the environment while effectively and expeditiously managing the GWSS threat.

The task force submitted its recommendations to the department on December 1, 2000, as required by the budget act language. The task force recommended that DFA:

- Adequately document, within 45 days of receipt of the task force report, the basis for the emergency declaration concerning the GWSS.
- Conduct and document regular review of the status of GWSS and PD in California to determine if an emergency exists and if local control programs are necessary, while effectively and expeditiously managing the occurrence and preventing the spread of PD using the guiding principle of least possible harm to public health and the environment.
- Conduct a full review, evaluation, and disclosure of the program, alternatives, and mitigation of potential adverse impacts pursu-

ant to California environmental policy and the California Environmental Quality Act.

- Initiate statewide dialogue on the issue of eradicating or controlling the GWSS in backyards and private property, in order to reduce the risk to the agricultural industry. The task force indicated that this should begin with a review of state law that gives the authority to the Secretary of Agriculture and County Agricultural Commissioners to spray private property against the will of the property owner.

The Legislature also adopted supplemental report language directing the department to report to the Legislature, by January 1, 2001, the results of their consultations with the task force and their evaluation of the potential adverse effects on public health and the environment. It also requires the department to report on the overall strategy developed for reviewing the county work plans to ensure that they result in the least possible harm to the public and the environment while effectively and expeditiously combating PD and the insects that carry it.

The department's report was received late in January, too late to review for this analysis. Upon review of the report, we will make recommendations, as appropriate, to the Legislature during budget hearings.

HEADQUARTERS RELOCATION NOT JUSTIFIED

We recommend the Legislature delete the \$729,000 augmentation request to move the Department of Food and Agriculture's headquarters from state-owned buildings into leased facilities because it is both costly and unnecessary to move the department. (Reduce Item 8570-001-0001 by \$566,000, Item 8570-001-0191 by \$66,000, and Item 8570-001-0111 by \$97,000.)

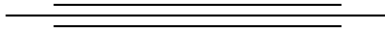
The Governor's budget includes a \$729,000 augmentation for DFA's facilities operations to support increased leasing costs to permanently move the department's headquarters from two state-owned buildings to leased space. According to DFA, additional costs are anticipated for tenant improvements at the leased facilities and for relocation and moving costs. Therefore, DFA indicates that it may submit a deficiency request regarding the proposal.

Currently, the headquarters is located near the State Capitol at 1220 N Street and 1215 O Street. The proposed move is based on the assumption that DFA must vacate the buildings because of the Department of General Services (DGS) plan to renovate them. The renovation plan is included in the Governor's budget under DGS's capital outlay program.

The estimated future cost for the renovations totals \$38 million. The Legislature has previously approved design funds to renovate the 1220 N Street building, but has deferred construction because of the potential to locate the governor's residence on this site. The Legislature has not previously reviewed the proposal to renovate the 1215 O Street building. In our analysis of the DGS proposal, we have raised several issues and have recommended that the Legislature delete the requested funds. (Please see the "Capital Outlay" chapter of this *Analysis* for a discussion of the renovation proposal.)

As mentioned above, the proposal to move the headquarters to leased space is based on the assumption that the existing building must be vacated for renovation. However, the 1220 N Street building is about 30 percent vacant and the original plan for renovations of this building did not include relocating the department. It is not clear why the administration now proposes to relocate the department to leased space. In view of the vacant space in the building, if the renovations are undertaken, the work could proceed as originally planned without moving DFA into leased space.

Based on (1) our recommendation that the Legislature not approve funding for the proposed renovations and (2) the ability to renovate the building as originally planned without moving DFA, we recommend the Legislature delete the \$729,000 requested for increased facilities lease costs.



PUBLIC UTILITIES COMMISSION (8660)

The Public Utilities Commission (PUC) is responsible for the regulation of privately owned “public utilities,” such as gas, electric, telephone, and railroad corporations, as well as certain passenger and household goods carriers. The commission’s primary objective is to ensure adequate facilities and services for the public at equitable and reasonable rates. Throughout its various regulatory decisions, the commission also promotes energy and resource conservation.

The budget proposes total expenditures for PUC in 2001-02 of \$100.1 million from the General Fund (\$2.7 million), various special funds (\$83.7 million), federal funds (\$1 million), and reimbursements (\$12.7 million). This is about \$4.3 million, or 4.1 percent, less than estimated current-year expenditures. This decrease results mainly from a decrease of \$10.5 million in reimbursements offset by increases of (1) \$5.4 million in activities funded by the PUC Utilities and Transportation Reimbursement Accounts and (2) \$0.4 million in electricity-related activities supported by the General Fund. The Governor’s budget also proposes an increase of 14.8 personnel-years (PYs) over the current-year level of 871.5 PYs.

UNIVERSAL SERVICE TELEPHONE PROGRAMS

Background

The PUC administers four universal service programs that seek to expand access to basic telephone services. It does so by subsidizing the cost of service for certain people (such as low-income persons and persons living in remote areas) through surcharges on all telephone users’ monthly bills. Currently, these surcharges total slightly more than 4.5 percent of billed services, supporting more than \$850 million in expenditures. The following is a brief description of these programs.

Universal Lifeline Telephone Service, also known as the Lifeline program, provides basic telephone service for low-income persons at 50 percent of the standard rates. By PUC decision, basic service includes features such as a single-party line, unlimited incoming calls, and touch tone dialing.

The California High Cost Fund-A (CHCF-A) subsidizes basic telephone service provided by 17 small local telephone companies serving high-cost, predominantly rural areas of the state. These companies cannot charge customers more than 150 percent of Pacific Bell's basic service average rates for urban areas. If a company's cost to provide basic service exceeds this ceiling, the fund reimburses the company for the difference.

Similarly, the **California High Cost Fund-B (CHCF-B)** subsidizes basic service in high-cost areas of the service territories of the four large local telephone companies—Pacific Bell, Verizon (formerly GTE), Roseville, and Citizens. Companies providing telephone services in above-average cost areas within a territory receive a subsidy for the amount over the average.

The **California Teleconnect Fund (CTF)** subsidizes telephone service for various entities—50 percent for schools and libraries, 25 percent for community-based organizations, and 20 percent for city- and county-owned hospitals and clinics.

The **Deaf and Disabled Telecommunications Program (DDTP)** provides three services to hearing-impaired and disabled persons.

- **Telecommunications Devices for the Deaf**—Loans telecommunications devices like teletypewriters to eligible individuals, schools and organizations serving the deaf or hearing-impaired, and state departments with significant public contact.
- **California Relay Service**—Provides access, through the standard telephone system, to a third-party operator who relays the information between the parties talking with one another.
- **Supplemental Telecommunications Devices for the Disabled**—Provides specialized telecommunications equipment like amplifiers, speaker telephones, and cordless telephones to individuals with hearing, vision, mobility, speech, and cognitive disabilities.

Program Budgets. The PUC annually approves a budget and surcharge level for each program. Figure 1 lists each universal service program with its current surcharge level and budgeted funding as approved by PUC.

The PUC's Report

In December 1999, the PUC issued a legislatively required report on the universal service telephone programs, addressing four issues.

Figure 1		
Universal Service Telephone Programs^a		
<i>(Dollars in Millions)</i>		
Program	Surcharge^b	PUC-Approved Budget
Universal Lifeline Telephone Service	1.450%	\$281.6
California High Cost Fund-A ^c	—	7.0
California High Cost Fund-B	2.600	482.8
California Teleconnect Fund	0.185	35.4
Deaf and Disabled Telecommunications ^{c d}	0.281	57.4
Totals	4.516%	\$864.2

^a Approved surcharge and budget is for 2001-02 unless otherwise noted.

^b Surcharge is a percent of billed services each month.

^c Approved budget for calendar year 2000.

^d Governor vetoed legislation extending the program beyond its January 1, 2001 sunset. Continuation of the program is contingent upon new legislation.

- **Funding Mechanism.** The effectiveness of the program's funding mechanism in ensuring "equitable and nondiscriminatory" contributions to support universal service.
- **Competitively Neutral and Flexible Services.** The ability of the programs to offer current services on a competitively neutral basis, while being flexible enough to incorporate additional services as telecommunications technology advances.
- **Comparability of Rates and Service.** The success in providing universal access in rural and high-cost areas to services that are comparable in cost and content to service provided in urban areas.
- **Reducing Subsidies and Auctioning.** The possibility of (1) reducing or eliminating subsidies where competition exists and (2) auctioning the right to provide universal service in high-cost areas.

Chapter 931, Statutes of 2000 (AB 994, Wright), requires the Legislative Analyst's Office to (1) review the findings of PUC's report and con-

sider whether any issues we identify affect continued implementation of the programs or warrant changes to existing law and (2) report our findings in the *Analysis of the 2001-02 Budget Bill*.

Below, we first summarize PUC's responses to the four issues specified in current law.

Funding Mechanism. In its report, PUC states that contributions to fund the universal service programs are equitable and nondiscriminatory because all companies providing local telephone service must apply the surcharges for these programs to their customers' bills. Furthermore, PUC notes that the Federal Communications Commission showed that California had met its goal of 95 percent of households subscribing to telephone service.

Competitively Neutral and Flexible Services. The PUC requires all companies providing local telephone service to provide the basic services as defined by the commission. The PUC states that this meets the requirement to provide current services in a manner that treats companies equally. In addition, PUC planned to begin a triennial review of its universal service programs in 2000. The PUC cites this effort as demonstrating flexibility to incorporate new services as telecommunications technology advances. This triennial review, however, has not yet begun. Furthermore, the review itself provides the *opportunity* for PUC to be flexible and incorporate new technological developments in the universal service programs. But it does not demonstrate that flexibility itself. The PUC's response to such a review would show that flexibility or lack thereof.

Comparability of Rates and Service. As mentioned above, all companies providing local telephone service must provide the same basic services. Thus, basic telephone service is comparable for all areas of the state. With respect to rates, PUC notes in its report that under CHCF-A the rate paid by customers for basic residential service does not exceed 150 percent of Pacific Bell's average rates for the same basic service in urban areas, as required by law. For CHCF-B, however, PUC only states that the fund subsidizes areas with above-average costs. The PUC does not address whether this is a reasonable standard and why it differs from the standard for CHCF-A. In addition, while CHCF-A subsidizes *all* telephone lines serviced by the small telephone companies, CHCF-B only subsidizes one telephone line per residence serviced by the large telephone companies. The PUC does not address whether these differences treat customers in high-cost areas served by small and large companies in an equitable manner.

Reducing Subsidies and Auctioning. The PUC states that a lack of interested bidders precludes using an auction to determine an appropriate subsidy amount to provide basic telephone service in high-cost areas. In fact, according to PUC, competition is just beginning to develop in urban

areas, which typically develop competitive markets first. The PUC indicates that it will monitor these auction issues in the triennial review of universal service programs. Currently, in the absence of an auction, PUC determines the companies' costs of service and sets subsidy amounts accordingly.

More Specific Programmatic Information Needed

To improve legislative oversight, we recommend that the Legislature adopt supplemental report language that requires PUC to submit to the Legislature an annual report that includes detailed programmatic information for each of the universal service programs.

Currently, there is little information provided to the Legislature on the performance and effectiveness of these universal service programs. For example, only the Lifeline program and DDTP have annual reporting requirements in statute. For the Lifeline program, PUC must annually report the services included, rates charged, eligibility criteria, and telephone penetration rates broken down by income, ethnicity, and geography. However, these reports have only been completed periodically. In addition, there is no readily available information showing what proportion of eligible households participate in the program or are in urban or rural areas. The board that markets the Lifeline program plans to conduct a market research study in 2001 that should include all this information. Lacking this information, it is not possible to determine the overall effectiveness of the program in reaching eligible households or various segments of the eligible population.

The DDTP annual report simply shows the total numbers of telecommunications devices in service and otherwise available. The report, however, does not address the effectiveness of the program. For example, there is no information on how the equipment is distributed to eligible individuals, the extent to which individuals use the telecommunications devices put in public places, or the provisions of the contracts with MCI Worldcom and Sprint for operating the relay service.

For the remaining programs—the two high-cost funds for subsidized basic telephone service and the teleconnect fund for school, library, hospital, and organization subsidies—PUC does not report the costs and accomplishments to the Legislature. Thus, information such as the following is not provided:

- The number of households that receive subsidized service from each of the high-cost funds and their locations.
- The number of schools, libraries, community-based organizations, and hospitals that receive subsidized service from the teleconnect fund and their locations.

- The proportion of schools and other eligible entities benefiting from the teleconnect fund.

Lacking this information, the Legislature cannot determine the effectiveness of the programs.

Legislation Addresses Need for Better Information. Before PUC submitted the December 1999 report required by law, the Legislature adopted Chapter 677, Statutes of 1999 (SB 669, Polanco), which made several changes to the universal service programs that address some of the concerns we have discussed. For each program, Chapter 677 does the following:

- ***Creates a State Fund and an Advisory Board.*** Chapter 677 requires program funds—currently held in bank trusts—to come under state control and be subject to appropriation by the Legislature. Chapter 677 conforms to current practice with respect to having boards oversee program operations.
- ***Requires PUC to Approve an Annual Budget Subject to Appropriation in the Budget Act.*** The PUC currently approves program budgets, but funding has not been subject to appropriation by the Legislature.
- ***Requires an Annual Report on Board Activities.*** As noted previously, only the Lifeline program and DDTP have statutory reporting requirements.

The requirement that program funding be appropriated in the budget act ensures that the Legislature will be informed of the cost of each of the universal service programs. In addition, the reporting requirement should keep the Legislature informed of the accomplishments of and performance data for each program. To improve legislative oversight further, we recommend that the Legislature adopt supplemental report language requiring the annual reports for each program to include the kind of detailed programmatic information we have described above.

Compliance With Recent Legislation

We recommend that the Legislature amend the Public Utilities Commission's (PUC's) appropriation in the budget act to include funding, on a line-item basis, for each of the universal service programs. Further, we recommend that prior to budget hearings, PUC report on the plan for and progress of the required investigation of the universal service programs, issues PUC expects to address, and the schedule for completing the report.

The Governor's budget does not include the universal service programs in PUC's budget item. Therefore, it is not clear how the adminis-

tration plans to fund these programs in the budget year, in accordance with the Chapter 677 requirement that funding be appropriated in the budget act. Chapter 677 also requires PUC to submit a transition plan for implementing the statute to the Legislature by July 1, 2000, with estimates of annual revenue and expenditures for each program. The PUC has not submitted this plan. This plan, as well as a proposed budget for each program, should be submitted to the Legislature for review prior to budget hearings. We recommend that upon receipt and review of this information, the Legislature include funding as appropriate, *on a line-item basis*, for each of the universal service programs.

Revisit Definition of Universal Service. Chapter 943, Statutes of 2000 (SB 1712, Polanco), requires PUC to begin an investigation to consider incorporating recent technologies into the definition of universal service. Chapter 943 specifies that this investigation is to begin by February 1, 2001, and PUC must report its results to the Legislature by January 1, 2002. The PUC should report to the Legislature prior to budget hearings on the plan for and progress of the investigation, issues PUC expects to address, and the schedule for completing the report.

OTHER ISSUES

Monitoring of San Diego Gas & Electric (SDG&E) Electricity Purchases

We recommend that the Legislature approve \$682,000 and four positions for monitoring of electricity purchases on a two-year limited-term basis because of the uncertainty surrounding the electricity industry.

The budget proposes \$682,000, including four permanent positions and \$359,000 for consultant contracts, for the duties specified in Chapter 328, Statutes of 2000 (AB 265, Davis). Chapter 328 requires PUC to (1) track the cost of electricity purchased by SDG&E above the rate cap imposed by the statute and (2) start a proceeding to determine the reasonableness of prices the utility paid beginning June 1, 2000 to purchase electricity for distribution to its customers.

Chapter 328 imposed a 6.5 cent per kilowatt-hour rate cap on the retail price SDG&E charges its customers for electricity through December 31, 2002 (December 31, 2003 if extended by PUC). This was in response to dramatically higher electricity costs during the summer of 2000. In addition to the rate cap, Chapter 328 requires PUC to track the difference between the rate the utility paid to acquire electricity for its customers and the 6.5 cents per kilowatt-hour it could charge those customers. The utility would then be permitted to recover any "reasonable" difference from its customers at a fu-

ture date. Chapter 328 also required PUC to begin a proceeding to determine the “prudence and reasonableness” of the prices SDG&E paid to purchase electricity for its customers beginning June 1, 2000.

The proposed positions would form a team of auditors to track the utilities’ costs. According to the commission, the workload created by Chapter 328 is not for a limited term because PUC will conduct regular reviews of the manner in which the utilities purchased electricity. However, the rate cap imposed in the SDG&E service territory expires on December 31, 2002 (December 31, 2003 if the commission extends the cap). Given the uncertainty and changing circumstances in the electricity industry, we recommend that the Legislature approve the funding and positions requested on a two-year limited-term basis. This would give the Legislature an opportunity to review the need to extend this effort beyond 2002-03.

Consultant Funds for Office of Ratepayer Advocates (ORA)

We recommend that the Legislature delete the \$456,000 request for additional consultant funds because (1) the complaint trend monitoring duplicates work performed by the Consumer Services Division and (2) the proposed commission proceedings workload should be prioritized within the Office of Ratepayer Advocates’ existing budget for consultants. (Reduce Item 8660-001-0462 by \$456,000.)

The budget proposes \$456,000 for ORA, which represents ratepayers in PUC proceedings, to augment existing funds for consultants. The ORA would use these funds to (1) begin monitoring trends in complaints taken by the commission’s Consumer Services Division and (2) increase its involvement in commission proceedings (for example, rate making cases, applications for mergers or asset sales or transfer, and regulatory framework proceedings).

The PUC budget includes a budget-year augmentation for the Consumer Services Division to implement a more systematic analysis of trends in customer complaints. Thus, ORA’s proposal duplicates this effort.

With respect to increased involvement in commission proceedings, ORA has had a budget of \$550,000 for contracts since 1998-99 and has prioritized its use of these funds for its involvement in PUC cases. The ORA should continue to prioritize the allocation of its existing contract funds, and—if appropriate—use them for increased involvement in commission proceedings.

As a result, we recommend that the Legislature delete the \$456,000 request for additional consultant funds.

ELECTRICITY OVERSIGHT BOARD (8770)

The Electricity Oversight Board was created by Chapter 854, Statutes of 1996 (AB 1890, Brulte), which restructured California's electricity industry. The board oversees the electricity market and the activities of the Independent System Operator, the nonprofit organization that manages the portion (approximately 75 percent) of the electricity transmission system owned by the state's three investor-owned utilities—Pacific Gas and Electric, Southern California Edison, and San Diego Gas and Electric. In addition, the board is responsible for representing the state before the Federal Energy Regulatory Commission, which has jurisdiction over some aspects of California's restructured electricity market.

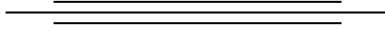
The budget includes \$4.4 million for the board's activities in the budget year, which is \$1.6 million more than estimated current-year expenditures due to proposals for additional staff and consultant funds to enhance its market monitoring and oversight activities in response to the electricity crisis. Proposed 2001-02 funding would support 30.4 person-years (PYs), an increase of 10.4 PYs.

Consultant Funds for Electricity Market Analysis

We withhold recommendation on the \$500,000 requested to contract with the University of California Energy Institute for electricity market analysis until the board reports to the Legislature prior to budget hearings on specific proposals to allocate the requested funds.

The budget proposes \$500,000 on an ongoing basis for the board to contract with the University of California Energy Institute to analyze the state's electricity market. According to the board, the institute would (1) perform independent, long-term research on topics such as congestion management reform, supply issues, competition in the retail market for electricity, price responsiveness of demand, and market design; (2) develop methods for detecting market abuses; and (3) assess different mar-

ket structures. Beyond mentioning these general research topics, the board does not include a definite proposal for using the funds. Consequently, we withhold recommendation on the \$500,000 request. The board should report to the Legislature prior to budget hearings on specific proposals to allocate the requested funds.



DEPARTMENT OF FINANCE (8860)

The Department of Finance (DOF) advises the Governor on the fiscal condition of the state; assists in developing the Governor's budget and legislative programs; evaluates the operation of the state's programs; and provides economic, financial, and demographic information. In addition, the department oversees the operation of the state's accounting and fiscal reporting system.

The Governor's budget proposes expenditures of \$40.5 million (\$30.5 million General Fund and \$10 million reimbursements) to support the activities of DOF in 2001-02. This is an increase of \$1.2 million from the General Fund, or 4 percent, above estimated current-year expenditures to accommodate workload growth.

Information Technology Innovation Grant Program Has Not Started

We recommend that the Department of Finance report at budget hearings on progress made in issuing grant application guidelines, forming the Information Technology Innovation Council, and identifying and funding innovative information technology projects.

The 2000-01 Budget Act appropriated \$10 million from the General Fund for allocation through 2003 for innovative information technology (IT) projects. At the time this analysis was prepared, DOF had not allocated any of these funds. The administration, however, does expect allocations to be made in the budget year.

Background. The Information Technology Innovation Activities budget item supports the grant program established by Chapter 608, Statutes of 2000 (AB 2817, Honda). The intent of this program is to provide one-time funding to departments for innovative IT projects as defined by guidelines issued by the Information Technology Innovation Council. Departments have up to three years (2000-01 through 2002-03) to expend allocated funds. Projects needing additional funds above the initial allo-

ation are required to address those funding needs through the annual budget process.

Chapter 608 required a number of steps to occur within three months of its enactment. First, the Department of Information Technology and the DOF were required to issue guidelines for grant applications. Second, the Information Technology Innovation Council, composed of two members of the Governor's Office, two Agency Secretaries, the State Chief Information Officer, the Director of DOF, a member of the Assembly, and a member of the Senate, is required to evaluate and rank grant proposals based on the issued guidelines. Third, DOF is required to award grants as recommended by the council from funds appropriated in the annual budget act. Chapter 608 states approved grants can be funded 30 days after written notification is provided to the Legislature. At the time this analysis was prepared, none of these steps were completed.

The DOF Should Report at Budget Hearings. We recommend that DOF report at budget hearings on the progress it has made in implementing Chapter 608.

Departmental Funding Issues Continue

We recommend that the Department of Finance report during budget hearings on the extent to which the proposed 2001-02 budget has reduced the need for departments to hold positions vacant to cover unbudgeted costs.

Background. For many years and through several administrations, departments have had to absorb a number of cost increases without receiving corresponding increases to their budgets. These include (1) inflationary cost increases for operating expenses and equipment; (2) merit salary adjustments (MSAs) that departments must provide to eligible employees each year; and (3) "unallocated reductions" in which departmental budgets are reduced, but no accompanying changes are made to modify or reduce workload or program responsibilities. One strategy used by departments to cover such costs is to deliberately hold positions vacant in order to generate "salary savings."

The DOF Directed to Examine Reasons for High Vacancy Rate. In spring 2000, the Legislature expressed concern that the state had a 15 percent vacancy rate at the same time the administration was proposing almost 6,000 new positions. Since it appeared that the state was unable to fill its existing positions, the Legislature directed DOF to (1) examine the vacancy issue further and (2) present recommendations during the May Revision on steps the administration could take to resolve the state's vacancy issue.

To meet this directive, DOF examined the budgets of 29 departments. During the May Revision of 2000, DOF presented its findings, which are summarized in Figure 1. As indicated in this figure, DOF found that about half of the positions reported vacant (47 percent) were used to meet budgeted salary savings (that is, to reflect normal employee turnover and hiring delays). Most of the remaining positions, however, were left vacant to generate “savings “ to cover anticipated costs for which the departments had not received funds. These included primarily personnel-related salary costs such as *actual* salaries that were higher than originally approved (20 percent). The remainder included staff overtime costs (15 percent), shortfalls for federal funds that did not materialize (11 percent), and other purposes (9 percent).

As a result of its investigation, DOF proposed the elimination of 1,736 positions in 2000-01.

The DOF Conducts Second Vacancy Report. Between July and October 2000, DOF conducted a second vacancy study which examined budgets in 50 departments. The findings from the second DOF study, also summarized in Figure 1, were presented to the Legislature in January 2001.

Figure 1		
Findings From DOF Vacancy Reports		
Reason Position Vacant	Percent of Positions Reported Vacant	
	Spring 2000 Report	January 2001 Report
Salary savings	47%	47%
Meet higher salary cost	18	20
Fund overtime	15	16
Cover federal funds shortfall	11	7
Other purposes	9	10
Totals	100%	100%

The data confirmed the earlier findings that departments are meeting their day-to-day operating needs—such as paying employee salaries and covering federal fund shortfalls—by holding positions vacant. In addition, the DOF reported it would abolish an additional 837 vacant positions in 2001-02.

The DOF Has Taken Some Steps to Address Vacancy and Under-Funding Issues. As a result of the Legislature’s focus on this issue, the DOF has

eliminated positions (as discussed earlier) and taken some steps to fund activities that previously had been unfunded. For example, DOF has allowed departments to budget new positions at midstep instead of first step, where appropriate. Others, such as the Department of Social Services, have received funding for MSAs in the proposed 2001-02 budget plan. The administration has also funded department costs for various salary adjustments resulting from collective bargaining agreements. These are positive steps that should reduce pressure on some departments to leave positions vacant for budget balancing purposes. We would note, however, these steps have been selectively applied, making it difficult for the Legislature to ascertain how much “forced” salary savings for budgetary purposes remains.

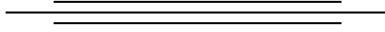
What Additional Steps Can the Administration Take? We believe there are additional steps the administration could take to address the vacancy and under-funding issues. Some of these may require additional funds—such as paying for MSAs—and some will not. In the latter category, for example, the administration could develop statewide strategies for addressing the “hard-to-recruit” vacancy problem. This would require the State Personnel Board, the Department of Personnel Administration, and other affected departments to take joint action to recruit for certain state positions. Implementation of measures such as these would improve the integrity of the state’s budgetary process so that funds appropriated for a particular purpose are in fact spent for that purpose.

Analyst’s Recommendation. As noted above, about half of the vacant departmental positions reported by DOF were used to meet salary savings requirements. Departments, however, left the remaining positions vacant to generate savings and cover costs for which they did not receive sufficient funds.

The steps undertaken by DOF to address this under-funding of departmental costs have been limited and selective. Consequently, it is not possible to determine the extent to which these steps have addressed departmental funding requirements on a statewide basis, thereby reducing the need to leave positions vacant. Therefore, we recommend that DOF report at budget hearings on the extent to which it has reduced the need for departments to hold positions vacant to cover unbudgeted costs. Specifically, the department should identify:

- The departments which received funds in the 2001-02 budget proposal specifically for the purpose of reducing the number of positions they hold vacant to cover unfunded costs.
- The extent to which those funds will address the problem.

- Steps the administration proposes to take in the future to reduce the level of “forced” salary savings. In addition, if DOF proposes to address these issues on a department-by-department basis, it should identify the criteria it would use to adjust departmental budgets.



MILITARY DEPARTMENT (8940)

The Military Department is responsible for the command and management of the California Army, Air National Guard, and four other related programs. To support the operations of a force of 23,000, the department maintains a headquarters complex in Sacramento, 127 armories, 33 equipment maintenance facilities, and 10 air bases throughout the state.

The missions of the National Guard are to provide combat-ready forces to the federal government at the direction of the President, to contribute emergency public safety support at the direction of the Governor, and to otherwise assist the community as directed.

The 2001-02 Governor's Budget proposes departmental expenditures of \$538 million. Of that sum, \$487 million would come from the federal government, although only \$46.5 million in federal funds would be appropriated through the budget bill. The remainder of the federal funds are allocated directly to the National Guard by the federal government. The budget bill also authorizes \$47.6 million from the state General Fund, an increase of \$9.5 million, or 25 percent, in the budget year. The balance of the request (\$3.7 million) is from reimbursements and a special fund.

Continue Cadet Corps Positions as Limited Term Until Evaluation is Complete

We recommend that the Legislature reject the Governor's budget proposal to make the California Cadet Corps (CACC) administrative positions permanent, because the Military Department has not submitted an evaluation demonstrating CACC program effectiveness.

Background. The CACC is a voluntary extracurricular program that serves about 6,500 middle and high school students in California schools. School districts are responsible for much of the implementation and maintenance of the program, with the National Guard providing uniforms, equipment, and statewide administration. Last year, the Governor's bud-

get proposed \$1.5 million from the General Fund, and six active duty positions to support and administer the program. The Legislature approved the funding, but made the positions limited term pending the results of an evaluation included in the budget proposal. At the time this analysis was prepared, the department had not submitted an evaluation.

Budget Proposal. The Governor's budget proposes to continue the funding for CACC and makes the six active duty positions permanent at a total cost of \$588,000 to the General Fund.

Recommendation. Because the Military Department has not submitted an evaluation demonstrating the effectiveness of this program as required by the Legislature, we recommend that the Legislature continue to fund these positions on a limited-term basis only.

Oakland Military Institute Funds Available for Reappropriation

We recommend that the Legislature delete the \$1.3 million proposed for the Oakland Military Institute (OMI). The OMI has not yet begun operations, therefore, an identical amount—which was appropriated in separate legislation for the current year—will be available for reappropriation in the budget year. (Reduce Item 8940-001-0001 by \$1.3 million.)

Background. The 2000-01 Governor's Budget requested \$1.3 million to allow the Military Department to provide staff support to a nonresidential military charter school in conjunction with the City of Oakland. While the academic curriculum was to be provided by civilian teachers, National Guard personnel were to provide military training and help instill classroom discipline. The OMI was intended to open in September 2000, with a first class of 162 7th graders. Each subsequent year, the plan was to add another class until it reached a capacity of 972 cadets in grades 7 through 12. The Legislature deleted the proposed funding from the budget bill, but provided a \$1.3 million appropriation in Chapter 127, Statutes of 2000 (AB 2866, Migden). Chapter 127 further required that OMI provide a dollar for dollar match for the \$1.3 million. The Department of Defense subsequently awarded OMI a \$2 million federal grant that insures that it will be able to meet the state matching funds requirement.

The City of Oakland subsequently was unable to obtain approval for its charter petition from either the Oakland Unified School District or the Alameda County Office of Education. As a result, OMI's start date was postponed. The state Board of Education did approve OMI's charter petition, but required OMI to secure oversight from a local educational agency. The National Guard now projects that it will be able to accom-

plish these tasks in time to open OMI in September 2001 with the 162 7th graders originally proposed.

Budget Proposal. The Governor's budget proposes a \$1.3 million General Fund expenditure for OMI, but includes no requirement for matching funds.

Current-Year Funds Available for Reappropriation. Chapter 127 appropriated \$1.3 million to the Military Department to allow it to operate a nonresidential military institute in conjunction with the City of Oakland and a school district. At the time this analysis was prepared, the Military Department had expended \$125,000 of the \$1.3 million appropriation. Because the institute will not begin operation until the budget year, we believe that the costs of those operations should be covered by reappropriating the funds still remaining from the current year. Because OMI will not begin operation until the budget year, additional funds are not justified.

Turning Point Academy Overbudgeted

We withhold recommendation on the \$10.6 million proposed for the Turning Point Academy and recommend that the Legislature direct the Military Department to provide, by the time of the May Revision, a revised budget proposal based on a more accurate estimate of the number of cadets that it will be able to serve.

Background. The 2000-01 Governor's Budget proposed \$9.2 million for the Military Department to establish the Turning Point Academy (TPA), a residential military academy at Camp San Luis Obispo for juvenile offenders found to have committed an offense at school for which expulsion is mandatory ("zero-tolerance" offenses). The Legislature deleted the money from the budget bill, but subsequently appropriated \$9.2 million in separate legislation, Chapter 366, Statutes of 2000 (SB 1542, Schiff). This measure revised the Governor's original proposal in several ways. Most notably, it made TPA subject to the existing standards and regulations for local juvenile facilities and restricted the group of eligible offenders to juveniles found to have brought a firearm to school.

During the current year, the Military Department has been working to implement Chapter 366 and projects enrolling its first class of cadets in March 2001. To prepare for the arrival of the cadets, it has been upgrading facilities, putting in portable classrooms, training staff, and working out a contract with Cuesta College (San Luis Obispo County) to provide the academic curriculum. Once TPA is fully operational, the Military Department projects that it will serve 160 cadets every six months, for a total of 320 per year.

Budget Proposal. The Governor's budget proposes \$10.6 million from the General Fund for the ongoing costs of TPA. This includes support for 103 positions and operational costs. The budget assumes that TPA will be fully operational in the budget year and serve 320 cadets.

Eligible Population Unlikely to Meet Department's Projections. All referrals to TPA will come from local juvenile courts. In order for a court to refer an offender a number of conditions must be met. First, the court must be located in a county whose Board of Supervisors has adopted a resolution that makes it subject to the provisions of Chapter 366. Among these provisions, is a requirement that the county provide significant aftercare services for the cadets who have completed the TPA program. As a result, some counties may not opt into Chapter 366. At the time this analysis was prepared, six counties had passed the required resolution and thirteen others were considering a resolution.

Once a county has decided to participate, the second requirement is to identify eligible offenders. In order to be eligible for TPA, an offender must meet the following criteria:

- Found to have committed a firearms-related offense at school or a school activity.
- Be 15 years of age or older and have no previous offense record.
- Have no mental illness or sexual problems.

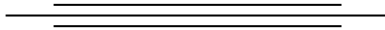
Third, for minors who meet these criteria, the court must find that the minor is likely to benefit from the program and is unlikely to suffer harm due to physical or developmental limitations.

Chapter 366 also requires that an evaluation of the program be conducted with an experimental design. Such an evaluation requires the identification of a comparison group of youth randomly matched to those who will be attending TPA. The practical result is that each county must identify two eligible minors and then randomly select one of them to attend TPA.

Based on its facility capacity, the Military Department has designed a program to serve 160 cadets every six months. Thus, the budget proposal assumes that juvenile courts will refer 320 cadets per year to TPA. We strongly question this assumption because the California Department of Education reports that only 168 high school students were expelled for firearms-related offenses in the 1998-1999 school year. Given that expulsion is mandatory for these offenses, we believe that the largest universe of eligible offenders will be less than 200. Once the other criteria are applied, this number could shrink substantially, particularly if a significant number of counties do not opt into the program. Furthermore, potential referrals must be divided into treatment and comparison groups for evalu-

ation purposes. As a result, we believe that the \$10.6 million proposed for the budget year is too high and that there is likely to be money available from the \$9.2 million appropriated in the current year.

Military Should Submit a Revised Proposal in May. A large discrepancy exists between the population the department is budgeted to serve and that which is likely to be referred. As a result the department needs to revise its proposal to reflect a more realistic estimate. Once TPA has opened and begun enrolling cadets, it will be easier to estimate how many minors are likely to be referred. Moreover, once the department identifies all of the counties who are planning to participate, it can survey them individually to determine how many offenders would be eligible for referral. Based on this information, the department can revise its budget proposal and estimate what funds will remain from the current year appropriation. As a result, we withhold recommendation on the proposed \$10.6 million and recommend that the Legislature direct the department to submit a revised proposal in the May Revision.



DEPARTMENT OF VETERANS AFFAIRS AND VETERANS' HOMES OF CALIFORNIA (8955-8966)

The Department of Veterans Affairs (DVA) provides services to California veterans and their dependents, and to eligible members of the California National Guard. The principal activities of the DVA include: (1) providing home and farm loans to qualifying veterans using the proceeds from the sale of general obligation and revenue bonds; (2) assisting eligible veterans and their dependents to obtain federal and state benefits by providing claims representation, subventions to county veterans service offices, and direct educational assistance to qualifying dependents; and (3) operating veterans' homes in Yountville, Barstow, and Chula Vista, with several levels of medical care, rehabilitation services, and residential services.

The budget proposes total expenditures of \$338 million for DVA in 2001-02. This is \$739,000 less than estimated current-year expenditures. Total budget-year expenditures of \$67 million from the General Fund are proposed, which is \$1.3 million, or 2 percent, less than the estimated current-year level.

Serious Problems in Management and Operation Of the Veterans' Home in Barstow

We recommend that the Legislature not approve funding for the Barstow Veterans' Home (Item 8965-001-0001), until such time as the department reports to the Legislature on the progress and timetable for obtaining recertification of the facility.

The Veterans' Home in Barstow is a 400 bed facility that provides multiple levels of care, including a 180 bed skilled nursing facility (SNF), a 56 bed residential care facility for the elderly, and a 164 bed independent living domiciliary. The Governor's budget proposes \$20.7 million (\$12.2 million General Fund, \$3.5 million Federal Trust Funds, and \$5 mil-

lion reimbursements) for the support and operation of the home. The population for all levels of care as of December 31, 2000 was 242 residents. This is 66 fewer residents, or a 21 percent decline, from last year's census. In view of the problems at the Barstow home (discussed below), it is not clear that the home will receive the budgeted level of federal funds and reimbursements.

Serious Problems Cited at Barstow. The Veterans' Home in Barstow has had a number of serious problems since it opened in February 1996. These problems include poor management, inadequate staff training, and difficulty hiring health care workers. This situation led to a series of events that culminated in inspections of the home by both the California Department of Health Services (DHS) and the US Department of Veterans Affairs (USDVA). Based on these inspections, the home, in June 2000, lost its Medi-Cal and Medicare certifications along with its federal per diem payments (received for each resident). The department has estimated that due to these actions and the lower number of residents, the home will lose \$5.9 million of federal funds and other reimbursement in the current year. Figure 1 (see next page) shows a chronology of major events that led to the current situation at the Barstow home.

In order to regain certification, DVA entered into a stipulated agreement with DHS that called for DHS to appoint a contractor to serve as the temporary manager for the 180 bed SNF at Barstow. Based on this agreement, DHS appointed Country Villa Health Services to fill this role and, on January 16, 2001, DVA signed a contract with this company. The term of the contract is from January 15, 2001 through June 30, 2001, at a cost of \$530,500. As temporary manager, the contractor is charged with bringing the SNF into substantial compliance with federal requirements by June 30, 2001. Some of the major services to be provided by the contractor are:

- Manage and operate the SNF.
- Conduct an in-depth assessment of the status of the SNF operation (to be completed by January 31, 2001).
- Provide a proposed plan of corrective action to permit the SNF to obtain certification by June 30, 2001.
- Consult with the department in selecting a permanent SNF administrator for the home.
- Prepare and conduct training courses and institute corrective action by March 30, 2001.

As called for in the contract, Country Villa Health Services is to have the Barstow facility recertified, staffed with well-trained personnel, and capable of operating in substantial compliance on its own by June 30,

2001. The contract allows for the extension of time and an increase in costs. The administration is seeking funding to pay for the Country Villa Health Services contract (approximately \$530,000) and to replace the loss of federal and other reimbursements in the current year (approximately \$6 million) through separate legislation (SB 45, Johannessen).

Figure 1

Events Involving Decertification at the Barstow Home

Date	Action
August 1999	DHS performs annual survey.
October 1999	Medicare payment for new admissions stopped.
November 1999	USDVA surveys facility. Requests plan of correction.
February 2000	DHS revisits Barstow. Requires additional plan of correction.
February 2000	Resident dies in choking/heart attack incident.
March 2000	USDVA revisits Barstow. Requires home to correct physician services elements.
May 2000	DHS Licensing, MediCal Fraud Investigations and CDVA Office of Inspector General perform unannounced visit and recertification survey.
June 2000	Home found not in compliance and fined. Loss of Medi-Cal and Medicare certification reimbursement payments.
July 2000	USDVA halts per diem payments.
December 2000	USDVA surveys domiciliary units (unassisted living).
January 2001	USDVA reinstates per diem payments for domiciliary units only, retroactive to December 2000.
January 2001	DVA contracts with Country Villa Health Services as interim skilled nursing facility (SNF) manager.
February 2001	Home prepares for DHS resurvey.

Source: California Department of Veterans Affairs.

In view of the serious problems in the management and operation of the Barstow home, we recommend the Legislature not approve the home's budget until the department reports to the Legislature detailing the progress made in correcting the deficiencies identified by DHS, USDVA, and the contractor, and identifies the remaining steps to be taken and the timetable to obtain recertification and receive federal funds and reimbursements.

TAX RELIEF (9100)

The state provides tax relief—both as subventions to local governments and as direct payments to eligible taxpayers—through a number of programs contained within this budget item. The budget proposes total relief of \$3.1 billion, of which almost \$1.2 billion is appropriated in the budget bill.

The largest ongoing program appropriated in the budget bill is the homeowners' exemption. This provision, which is required by the State Constitution, grants a \$7,000 property tax exemption on the assessed value of owner-occupied dwellings, and requires the state to reimburse local governments for the resulting reduction in property tax revenues. The exemption reduces the typical homeowner's taxes by about \$75 annually. The Governor's budget proposes an expenditure of \$417 million on this program in 2001-02. This is an increase of \$8 million, or 2 percent, which reflects the expected growth in the number of homeowners claiming the exemption.

VEHICLE LICENSE FEE BACKFILL

The largest program of tax relief pays for the costs of reimbursing local governments for reductions in the vehicle license fee (VLF). The VLF is an annual fee on the ownership of a registered vehicle in California, levied in place of taxing vehicles as personal property. The revenues are distributed to cities and counties. As part of the 1998 budget agreement, the VLF was permanently cut by 25 percent, with the potential of future reductions of up to 67.5 percent (dependent on the growth of General Fund revenues). For all VLF reductions, cities and counties continue to receive the same amount of revenues as under prior law, with the reduced VLF amounts replaced by General Fund spending. This spending, known as the "VLF backfill," is reflected in the tax relief budget item.

The VLF Rebate Begins in 2001. As part of the 2000 budget agreement, vehicle owners will permanently receive the equivalent of a 67.5 percent reduction in the VLF beginning in calendar year 2001. For calendar years 2001 and 2002, vehicle owners will receive this reduction in two parts:

- **Offset on Registration Bill.** As done with the prior reductions, vehicle owners will receive a credit on their vehicle registration bill for a portion of their VLF owed. In 2001 and 2002, this offset will be equal to 35 percent of the VLF owed.
- **Rebate Check.** Vehicle owners will also receive from the State Controller in the weeks following their registration payment a rebate check totaling 32.5 percent of their VLF paid.

Beginning in 2003, vehicle owners will receive the full 67.5 percent reduction as an offset on their registration bill.

Only a Portion of Costs Are Contained in the Budget Bill. The amount of General Fund spending necessary to backfill local governments for the registration bill offsets is continuously appropriated. These costs, therefore, do not appear in the budget bill. As shown in Figure 1, we estimate this cost to be \$1.9 billion in 2001-02. On the other hand, the amount necessary to pay for the rebated portion of the tax reduction *is* appropriated in the budget bill. We estimate the rebate will cost \$1.7 billion in 2001-02 (with half-year costs in both 2000-01 and 2002-03). Of this amount, however, \$1.2 billion was previously appropriated by Chapter 107, Statutes of 2000 (AB 511, Alquist). Therefore, the appropriation in the budget bill totals less than \$600 million. The amount of VLF tax relief will total \$3.6 billion in 2001-02.

Figure 1

Vehicle License Fee (VLF) Projected Backfill Costs

(Dollars in Billions)

	Offset Costs	Rebate Costs	Total Costs	Total Percentage Reduction
2000-01	\$1.8	\$0.8	\$2.6	35.0/67.5% ^a
2001-02	1.9	1.7 ^b	3.6 ^b	67.5
2002-03	3.0	0.9	3.9	67.5
2003-04	4.1	—	4.1	67.5
2004-05	4.3	—	4.3	67.5
2005-06	4.6	—	4.6	67.5

^a 67.5 percent reduction began January 1, 2001.

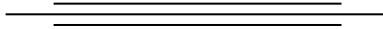
^b \$1.2 billion of this amount was appropriated in 2000-01.

Our estimate of the necessary appropriation for the VLF rebate in the budget year is about \$60 million lower than the administration estimate, due to a combination of a lower expected growth rate in VLF revenues and different estimates of the rebates' processing time. Since the rebates have just begun, a better estimate of the necessary appropriation should be available at the time of budget hearings.

Recommend Accelerating Transition to Offsets

We recommend accelerating, by one-calendar year, the beginning of the full 67.5 percent vehicle license fee offset on a vehicle owner's registration bill, resulting in one-time administrative savings of \$17 million.

As described above, vehicle owners are scheduled to receive rebate checks in both 2001 and 2002, with the full 67.5 percent offset on a vehicle owner's registration bill scheduled to begin in 2003. We recommend amending state law to accelerate that date forward a full year. Thus, vehicle owners would all receive rebate checks in 2001 and begin receiving the full tax relief offset on their bills in 2002. This would result in administrative savings for both the Department of Motor Vehicles and the State Controller's Office for processing rebate checks totaling an estimated \$17 million in one-time savings over the budget year and 2002-03.



LOCAL GOVERNMENT FINANCING (9210)

This budget item contains funding for six purposes:

- ***General Purpose Relief.*** The Governor proposes to provide local governments with \$250 million in the budget year on a one-time basis for general purpose fiscal relief. The proposal is discussed in detail below.
- ***Citizens' Option for Public Safety (COPS).*** The COPS program was created in 1996 to provide local governments with funds for law enforcement. The program was expanded in 2000-01 to include funding for local juvenile justice programs. The budget proposes to continue the program's funding at \$242 million, which we discuss below.
- ***Local Law Enforcement Technology Grants.*** The 2000-01 Budget Act provided \$75 million to local law enforcement agencies for the purchase of high technology equipment. The funds were allocated with a minimum \$100,000 to each agency, with the remaining funds allocated on a per capita basis. The Governor proposes to fund this program again in 2001-02 at \$75 million.
- ***Property Tax Administration Loan Program.*** This program was created in 1995 to provide forgivable loans to counties for additional spending on property tax administration. The program is due to sunset at the end of 2001-02. We discuss long-term financing for property tax administration below.
- ***Special Supplemental Subventions.*** Three programs provide specified local governments with special funding: (1) qualifying redevelopment agencies for revenues lost as a result of the repeal of the business inventory exemption in 1984 (\$1.2 million), (2) counties with no incorporated cities on the basis that they are not eligible to receive the city portions of the gas tax and vehicle license

fee distributions (\$147,000), and (3) local agencies which paid jail booking fees in 1997-98 (\$38 million, continuously appropriated).

- **State-Mandated Local Programs.** This item includes funding to reimburse local governments for costs incurred in complying with certain state-mandated local programs (\$6 million).

Provide Long-Term Improvements to Property Tax System

We recommend that the Property Tax Administration Loan Program not be extended beyond its sunset of 2001-02. In its place, we recommend that the Legislature consider implementing a long-term structural improvement to the property tax system.

Background. Counties are the level of government with the primary responsibility for assessing property and collecting property tax revenues, which are expected to total more than \$25 billion in 2001-02. County assessor offices assess the value of property, and then county tax collectors and auditors collect the revenues and allocate them among local governments. It is estimated that \$450 million is spent annually on the property tax administration system.

In the early 1990s, county assessor offices suffered two financial strains:

- The property tax shifts—which redirected over \$3 billion in property taxes from local governments to schools—forced counties to make budget cuts to many discretionary spending programs, including assessor offices.
- The statewide economic recession dramatically increased many assessors' workloads by requiring the processing of downward assessments and assessment appeals.

Since the property tax shifts reduced the share of each property tax dollar collected that goes to a county, counties experienced a decline in the financial incentive to invest in the property tax administration system. Although cities and special districts are required to pay for their share of property tax administration costs, school districts are not. As a result, counties pay more than 70 percent of property tax administration costs, yet they now receive less than 20 percent of the revenues.

Loan Program to Sunset. Although the property tax is a local tax, it nevertheless benefits the state as a result of California's education financing system. Under this system, increases in property taxes generally translate into reductions in the required state contribution for education. Recognizing the fiscal strains facing counties and the state interest in a well-administered property tax system, the Legislature created the Property Tax Administration Loan Program by enacting Chapter 914, Statutes of

1995 (AB 818, Vasconcellos). This program has been extended twice—most recently by Chapter 602, Statutes of 2000 (AB 1038, Wesson), which extends the program’s sunset date by one year—through 2001-02. The legislation appropriates \$60 million each year for loans to counties for additional spending on property tax administration. These loans may be forgiven if counties can demonstrate that they have generated or preserved sufficient revenues for schools to offset the costs of the loans. In recent years, 47 counties have participated in the program, with all the loans being forgiven (totaling \$50.9 million in 1999-00). The Department of Finance (DOF) is responsible for administering the program and determining whether to forgive the loans.

Short-Term Benefits But Long-Term Concerns. The program was designed as a short-term solution to the growth of assessor workload backlogs. In this regard, the program has been relatively successful. By both increasing property tax revenues to governments and helping to ensure that taxpayers receive a fair assessment, the program has strengthened the property tax administration system. Work backlogs in most counties have been significantly reduced or eliminated. In our view, however, extension of the program is not the most effective method for achieving a stable and efficient property tax administration system in the long term. Below, we discuss a number of the problems with the program.

- ***Does Not Address Underlying Disincentives.*** While providing an infusion of needed funding into many counties’ property tax administration systems, the loan program does nothing to alter the underlying disincentive for counties to invest in their own systems. A county continues to receive a very small proportion of the benefits for each dollar it chooses to spend on property tax administration.
- ***Awkward Governance Structure.*** For the majority of their budgets, assessors seek approval from their county boards of supervisors. However, for the portion of their budget funded from the loan program, the assessor instead seeks approval from DOF. The state must try to evaluate the funding needs of local departments, each with their own set of circumstances. Thus, the program creates an awkward system in which an assessor’s budget is reviewed twice but never from a comprehensive perspective. The current system also creates a sizable workload for DOF. Each year, the department must review and renew contracts with up to 58 counties and then evaluate each county’s performance to determine whether its loan ought to be forgiven. In fact, a recent State Auditor report found that because of “weak oversight,” DOF does not have adequate information to make “good business decisions” regarding the program.

- **Nonuniform Benefits.** While the loan program has benefitted many counties, 11 counties have elected not to participate for administrative or other reasons. Therefore, the benefits of the program have not been uniform across the state. Moreover, the program does not adjust to the changing demands of individual assessor offices. The maximum loan amounts for which each county is eligible is set in statute and has not been amended since the program's inception.

Options for a Permanent Solution. In its audit, the State Auditor recommended continuing the loan program—but this was only in comparison to having no state role in property tax administration. While we agree that the loan program is preferable to having no state role, we recommend allowing the program to sunset as scheduled and replacing it with a better long-term solution to the disincentives that counties face to invest in the property tax administration system. The program has generally been considered in two contexts: (1) improving the property tax administration infrastructure and (2) providing general fiscal relief to counties. Based on which of these goals is a higher priority, the Legislature could implement one of the following ongoing options in place of extending the sunset of the loan program.

- **State Share of Growth in Costs.** One option would be for the state to pay for the schools' pro rata share (about 52 percent) of all *growth* in property tax administration expenditures. Counties would be required to continue to maintain their baseline spending on property tax administration with the costs shared along their current ratios. However, increases in administration costs would be paid for by all of the entities benefitting from property taxes—according to their share of the benefits. Counties would, therefore, make future decisions about whether to spend additional dollars on property tax administration knowing that the benefits of such investments would be commensurate with their costs. If statewide property tax administration costs increased by 5 percent, this option would cost the state about \$12 million annually. This option is discussed in more detail in *The 1997-98 Budget: Perspectives and Issues* (please see pages 215 to 226).
- **State Share of All Costs.** Another option would be for the state to simply pay for the schools' *entire share* of property tax administration costs (base and growth), at a cost of about \$235 million. Since state funds would replace county funds already invested in the property tax administration system, we would expect counties to spend most of these savings on priorities outside of the property tax system. This option, therefore, is primarily one that promotes general fiscal relief to counties. It would, however, es-

establish the same type of positive incentives for future spending as the incremental cost option discussed above (though at a much higher state cost).

Funds Should Be Used Strategically for Reform

We recommend that the Legislature strategically use the \$250 million in proposed local government fiscal relief to achieve a specific reform goal. The proposed formula would do nothing to address the underlying problems of the local government fiscal system.

Legislature Has Recognized Need for Local Government Fiscal Reform. The Legislature has previously stated its desire to reform the existing system of local government finance. Problems with the existing system include outdated revenue allocation formulas, a lack of local control over finances, and development incentives which favor retail development over other land uses. The property tax shifts in the early 1990s magnified these existing problems by limiting local governments' discretionary dollars (through required contributions to the Educational Revenue Augmentation Fund [ERAF]).

Governor Proposes Relief. In both 1999-00 and 2000-01, the state provided cities, counties, and special districts with general purpose fiscal relief by allocating payments to jurisdictions half based on their contribution to ERAF and half based on their share of population. The Governor proposes \$250 million in 2001-02 for general purpose relief for local governments, again based on this formula. Under this proposal, cities would receive approximately \$121 million, counties \$118 million, and special districts \$11 million.

A Missed Opportunity. While the proposed relief would mitigate local governments' lack of discretionary revenue on a one-time basis, the payments would fail to reform the underlying problems of local government finance. As such, the proposal misses an opportunity to allocate the funds in a way which specifically addresses an existing problem with the local government fiscal structure.

Use Funds Strategically. Given the thousands of local governments involved, more than \$250 million on a one-time basis would be needed to implement a broad-based local government reform effort. At the same time, we believe that the \$250 million could be used more strategically to make improvements in the local government finance system. As discussed above, for instance, a long-term state role in property tax administration would benefit both local governments and the state. The \$250 million in one-time funds could provide a number of years of funding for paying a state share of growth in administration costs. Additionally, as discussed

in our report *Realignment Revisited: An Evaluation of the 1991 Experiment in State-County Relations* (please see the *2001-02 Perspectives and Issues*, Part V), a reserve for realignment would help mitigate the need for health, mental health, and social services program reductions during periods of economic difficulty. Alternatively, the Legislature could reserve the \$250 million for use as part of a broader funding package to help implement a future reform effort.

The COPS Program Expanded to Include Juvenile Justice Funding

The Schiff-Cardenas Crime Prevention Act of 2000 expanded the Citizens' Option for Public Safety program to include funding for local juvenile justice related programming and ensure that every local law enforcement agency receives a minimum grant of \$100,000. The Governor's budget continues funds for this purpose.

Background. In 1996, the Legislature enacted Chapter 134, Statutes of 1996 (AB 3229, Brulte), which created the COPS program to provide \$100 million for local public safety expenditures. Under Chapter 134 and its successor, Chapter 289, Statutes of 1997 (AB 1584, Prenter), the \$100 million was divided as follows:

- \$75 million to cities and counties for front line law enforcement.
- \$12.5 million to district attorneys for criminal prosecution.
- \$12.5 million to sheriffs for county jail construction and operations. Chapter 289 was due to sunset at the end of the 1999-00 fiscal year, and the Legislature took that opportunity to expand the program to include new components.

Schiff-Cardenas Crime Prevention Act of 2000. In September of 2000, the Governor signed Chapter 353, Statutes of 2000 (AB 1913), known as the Schiff-Cardenas Crime Prevention Act of 2000. This measure included funding for the programs previously included in the COPS program, as well as additional items. The bill appropriates \$243.4 million to be allocated as follows:

- \$121.3 million, including \$100 million for the public safety items previously in the COPS program plus an additional \$21 million to guarantee a minimum allocation of \$100,000 for every local law enforcement agency. (The rest of the funds are allocated on a per capita basis.)
- \$121.3 million to implement a comprehensive multiagency juvenile justice plan for each county.

- \$750,000 to the Board of Corrections to oversee the implementation of the juvenile justice component of the funding.

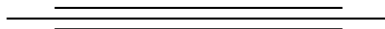
In order to receive their juvenile justice funds under the bill, counties must convene a local juvenile justice coordinating council with members representing a broad array of public safety and social service agencies as well as community-based organizations that work with delinquent youth. This council must then assemble a comprehensive multiagency juvenile justice plan that includes the following:

- An assessment of existing services for juvenile offenders and at-risk youth.
- An identification and prioritization of neighborhoods, schools, and other areas that bear a significant juvenile crime burden.
- A local action strategy that includes a continuum of responses to juvenile crime.
- A specific menu of programs that fit the strategy to be funded with the Schiff-Cardenas funds.

Programs to be funded under the bill can address a wide array of juvenile justice issues, from prevention to incapacitation, but they must be based on programs or approaches which have been demonstrated effective. In addition, they must adopt a collaborative, integrated services approach where appropriate, and adopt objectives and outcome measures that can be used to evaluate their effectiveness.

Budget Proposal. The Governor's budget proposes to continue to fund the expanded program at the \$242.6 million level (not including the funds for Board of Corrections) established by Chapter 353. It is intended that this money would continue to be subject to Chapter 353 and would be allocated in the manner described above.

Program Due to Sunset in 2002. Chapter 353 will become inoperative as of July 1, 2002. Thus, if the Legislature wishes to continue this program beyond the budget year, new legislation extending the sunset date needs to be enacted.



HEALTH AND DENTAL BENEFITS FOR ANNUITANTS (9650)

This appropriation provides for the state's contribution toward health and dental insurance premiums for annuitants of the Judges', Legislators', District Agricultural Employees', and Public Employees' Retirement Systems, as well as specified annuitants of the State Teachers' Retirement System. The program provides annuitants the option of selecting from 18 state-approved health plans (depending on where an annuitant lives).

Budget-Year Costs Are Uncertain

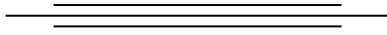
We withhold recommendation on the \$430.7 million General Fund request for annuitant benefits pending final determination of health insurance premium rates for calendar year 2002.

The budget proposes total expenditures of \$430.7 million from the General Fund for health and dental benefits for annuitants in 2001-02. This is \$20.5 million, or 5 percent, more than estimated expenditures for this purpose in the current year. This increase reflects expected growth in the number of annuitants. It does not include any changes in health insurance premiums that would go into effect January 1, 2002. Figure 1 (see next page) displays General Fund expenditures for annuitant health and dental benefits for the three fiscal years starting with 1999-00. Although these costs are initially paid from the General Fund, the state recovers a portion of these costs (about 33 percent) from special funds through pro rata charges.

The actual amounts needed in the budget year are dependent on negotiations over health insurance premiums currently underway between the Public Employees' Retirement System and providers. These negotiated premium rates—which will cover the 2002 calendar year—should be available for review during legislative budget hearings. Pending re-

ceipt of the new rates, we withhold recommendation on the amount requested under this item.

Figure 1			
Health and Dental Benefits For Annuitants			
<i>(In Millions)</i>			
Program	1999-00 Actual	2000-01 Estimated	2001-02 Budgeted
Health	\$309.6	\$364.3	\$382.6
Dental	41.7	45.9	48.1
Totals	\$351.3	\$410.2	\$430.7



AUGMENTATION FOR EMPLOYEE COMPENSATION (9800)

A significant portion of state government expenditures is for compensation of state employees. The Governor's budget projects \$16.7 billion in salary and wage expenditures for more than 317,000 authorized personnel-years in 2001-02 (including \$5.5 billion and more than 105,000 personnel-years in higher education). Including benefits (such as contributions to retirement and health insurance), estimated employee compensation expenditures are projected to exceed \$19 billion for the budget year.

Employee Pay/Benefit Increases

State Civil Service Employees. In September 1999, the Legislature approved memoranda of understanding (MOUs) for all of the state's 21 collective bargaining units. (This does not include employees in higher education.) These agreements are effective through June 30, 2001. The MOUs provided two 4 percent general salary increases effective July 1, 1999 and September 1, 2000. For employees not covered by collective bargaining (such as managers and supervisors), the Department of Personnel Administration (DPA) approved a compensation package similar to that approved in the MOUs. Figure 1 (see next page) shows a history of general salary increases for state civil service employees and the consumer price indices for the United States and California since 1981-82.

The Governor's budget does not include any budget-year funding for employee compensation. However, DPA will begin collective bargaining negotiations to replace the expiring MOUs this spring. Consequently, we anticipate the state will face some increased costs for employee compensation in 2001-02. Based on the estimated state employee salary level, we estimate that a 1 percent salary increase for state employees increases General Fund costs approximately \$55 million.

Figure 1			
State General Salary Increases			
<i>1981-82 Through 2001-02</i>			
Fiscal Year	State General Salary Increases	Consumer Price Indices	
		United States	California
1981-82	6.5%	8.8%	10.7%
1982-83	—	4.2	2.3
1983-84	6.0	3.7	3.6
1984-85	8.0	3.9	4.9
1985-86	6.0	2.9	4.0
1986-87	6.0	2.2	3.3
1987-88	3.8	4.1	4.2
1988-89	6.0	4.6	4.8
1989-90	4.0	4.8	5.0
1990-91	5.0	5.5	5.3
1991-92	—	3.2	3.6
1992-93	—	3.1	3.2
1993-94	5.0	2.6	1.8
1994-95	3.0	2.9	1.7
1995-96	—	2.7	1.4
1996-97	—	2.9	2.3
1997-98	—	1.8	2.0
1998-99	5.5	1.7	2.5
1999-00	4.0	2.9	3.1
2000-01 ^a	4.0	3.0	4.0
2001-02 ^a	— ^b	2.3	2.8

^a Legislative Analyst's Office estimate of consumer price indices.
^b To be determined through collective bargaining.

Employees in Higher Education. In higher education, the Governor's budget proposes \$131 million for the University of California and \$96 million for the California State University for employee compensation to provide salary and benefit increases to faculty and staff. Figure 2 shows how the budget proposes to allocate these amounts.

Strengthen Legislature's Collective Bargaining Oversight

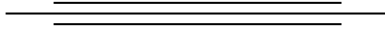
To strengthen the Legislature's oversight of collective bargaining, we recommend that the Legislature require a minimum 30-day review period for collective bargaining proposals and review proposals at budget

Figure 2	
Higher Education Salary and Benefit Increases 2001-02 Governor's Budget	
<i>General Fund (In Millions)</i>	
University of California	
Merit salary increases	\$43.0
Average 2 percent cost-of-living increase	38.4
Full-year cost of 2000-01 salary increases	19.5
Health benefit cost increases	13.1
Parity adjustments for staff and nonfaculty academic employees	10.0
Parity adjustments for faculty	7.1
Subtotal	(\$131.1)
California State University	
4 percent compensation pool (effective July 1, 2001)	\$81.5
Health and dental benefit cost increases	13.2
Full-year cost of 2000-01 salary increases	1.5
Subtotal	(\$96.2)
Higher Education Total	\$227.3

hearings for adoption in the budget act. Further, the Department of Personnel Administration should report to the budget committees during budget hearings on the administration's collective bargaining proposals and the status of negotiations.

In the past, the Legislature has received MOUs for approval late in the session. In addition, assessments of the total cost of the MOUs have not always been available or complete for consideration with the proposals. To ensure that the Legislature has the opportunity to appropriately review any proposed MOUs, we recommend that the Legislature (1) require a minimum 30-day review period between the submittal of proposed MOUs to the Legislature and hearings on the proposals to ensure that their fiscal and policy implications are fully understood and (2) review the administration's MOU proposals at the budget hearings and adopt them in the annual budget act (or as amendments to the act if they are not available for review during budget hearings). This is consistent with our recommendation in past analyses and with supplemental report

language adopted by the Legislature with the *1996-97 Budget Act*. Given this need to strengthen the Legislature's oversight of collective bargaining agreements, we further recommend that DPA report to the budget committees during budget hearings on the administration's collective bargaining proposals and the status of negotiations.



JANITORIAL/CONTRACT SERVICES (9908)

The budget proposes \$6 million (\$2 million each from the General Fund, special funds, and nongovernmental cost funds) to fund increased costs of personal services contracts as a result of providing employee benefits to janitors, housekeepers, custodians, food service workers, laundry workers, window cleaners, and security guards at a level valued at not less than 85 percent of the state employer cost of comparable benefits provided to state employees for performing similar duties.

Janitorial/Contract Services

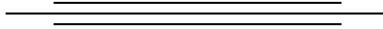
We withhold recommendation on the \$6 million requested for employee benefit cost related to janitorial/contract services pending receipt and review of information from the Department of Finance about how the funds appropriated in the 2000-01 Budget Act were used and the basis for the budget-year request.

Government Code Section 19134 requires that contractors providing the state with janitorial and related services provide their employees benefits equal to 85 percent of the employer (state) cost of benefits provided to state employees performing similar duties. Employers can also satisfy this requirement by providing an in-lieu cash payment in the same amount.

The cost of benefits provided to state employees is calculated by the Department of Personnel Administration (DPA) by February 1 of each year. Under regulations adopted by the Department of General Services, state janitorial contractors can apply for an increase in their contract rates if the DPA calculation results in increased costs for them to furnish the required employee benefits. The budget proposes a total of \$6 million for this purpose and authorizes the Director of Finance to augment the budgets of departments when the DPA calculation results in higher costs to the departments for contracts they have for janitorial services, and authorizes the Director to augment the appropriations if necessary for this

purpose. This is the same level of funding and budget language that was included for this purpose in the *2000-01 Budget Act*.

We withhold recommendation pending receipt, prior to budget hearings, of a report from the Department of Finance on the method used in the current year to allocate funds for this purpose, the amount paid (or owed) to each contractor, the balance available in the current-year appropriation, and the basis for the budget-year request.



UTILITIES COSTS (9911)

Increased Department Costs for Natural Gas and Electricity

We withhold recommendation on the \$50 million proposal (\$25 million General Fund and \$12.5 million each from special funds and nongovernmental cost funds) to fund departments' increased natural gas and electricity costs, pending receipt and review of documentation justifying the requested amount. Further, we recommend that the Legislature approve any funding on a one-time basis, instead of annually as requested, and delete proposed budget bill language that would authorize the Department of Finance to augment the \$50 million.

The Governor's budget proposes \$50 million (\$25 million General Fund and \$12.5 million each from special funds and nongovernmental cost funds) annually to fund higher costs departments face for various utility expenses such as natural gas and electricity. Proposed budget bill language specifies that with 30 day advance written notification to the Legislature, the Department of Finance (DOF) can (1) allocate funds to state departments and (2) augment the \$50 million appropriated in these items.

In view of the current situation concerning the price of natural gas and electricity, a set-aside of funds for increases in the price of these expenses may be warranted. The administration, however, has not provided any supporting documents to justify the amounts proposed. Further, given the uncertain circumstances surrounding these utility costs when this analysis was written, we withhold recommendation on the \$50 million proposal. The Legislature should have more information on the need for this item and an appropriate amount during the budget process.

In any case, however, we recommend that the Legislature delete the proposed budget language that would allow DOF to augment the \$50 million. We are not aware of any need to grant the department such open-ended authority.

CONTROL SECTION 3.60

This control section specifies the contribution rates for the various retirement classes of state employees in the Public Employees' Retirement System (PERS). The section also authorizes the Department of Finance to adjust any appropriation in the budget bill as required to conform with changes in these rates. In addition, the section requires the State Controller to offset these contributions with any surplus funds in the employer accounts of the retirement trust fund.

State Contribution Rates to PERS Expected to Increase

We withhold recommendation on 2001-02 state contribution rates for retirement benefits pending (1) final determination of the actual rates to be applied in the budget year and (2) receipt and review of information regarding the actuarial assumptions underlying the rates.

Under current law, PERS is responsible for developing employer contribution rates each year based on actuarial analyses. When this *Analysis* was prepared, a final determination of the 2001-02 rates had not been made. However, we believe the state's costs more than likely will increase in 2001-02 because of enhanced retirement benefits for all state employees that became effective January 1, 2000. Under the legislation that enhanced the benefits—Chapter 555, Statutes of 1999 (SB 400, Ortiz)—PERS was required to modify certain actuarial valuation methods in order to recognize excess assets more quickly. As a result, the state's costs for the new benefits were partially offset, and the budget year is the first year that PERS recognizes the increased liability in setting the state employer contribution rates. Based on the estimated state employee salary level, we estimate that each percentage point increase in the state's overall contribution rate increases General Fund retirement costs approximately \$55 million.

Consequently, we withhold recommendation pending final determination of 2001-02 rates and receipt and review of information from PERS regarding the actuarial assumptions underlying the determined rates. This information is typically available in March or April.

FINDINGS AND RECOMMENDATIONS

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Crosscutting Issues

Petroleum Violation Escrow Account

- F-18 ■ **The Future of the Petroleum Violation Escrow Account (PVEA).** Recommend that the Energy Commission report, prior to budget hearings, on a multiyear projection of expected (1) administrative costs, based on schedules for current and proposed projects, and (2) interest earnings, so that the Legislature can determine how many years PVEA can be expected to provide some funding for energy-related projects.

State Data Centers

- F-23 ■ **Data Center Study.** A number of factors have rendered the Department of Information Technology's (DOIT) 1997 Data Center Consolidation Report out-of-date. We recommend that the Legislature direct DOIT to report on the resources and time frames needed to conduct a study which (1) examines data center rates for nonmainframe activities, (2) identifies potential opportunities for specialization between the state's primary data centers, and (3) identifies data center functions that can be provided more efficiently by private industry.

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Department of Information Technology

- F-29 ■ **Supplemental Information Not Provided and Audit Underway.** Recommend no action on budget until the Department of Information Technology (DOIT) provides supplemental information on issued policies and the Bureau of State Audits provides its DOIT audit findings to the Legislature.
- F-32 ■ **Policy Needed on Replacing Information Technology Hardware and Software.** Recommend that the Legislature direct DOIT and the Department of Finance (DOF) to issue policies on scheduling and funding replacement of information technology hardware and software.
- F-34 ■ **Post-Implementation Evaluation Reporting (PIER) Needs to Be Improved.** Recommend that the Legislature: (1) fund only projects with identified measurable benefits, (2) require DOIT and DOF to issue policies on criteria and funding for independent evaluations, (3) require departments to report at budget hearings on completed current-year projects, (4) adopt budget control language requiring DOIT to report on results of PIER reviews, and (5) enact legislation requiring the administration to provide PIER information in ongoing years.

Office of Planning and Research

- F-40 ■ **Touch Screen Voting Pilot Program Not Justified. Reduce Item 0650-101-0001 by \$40 Million.** Recommend deletion because touch screen voting systems have already been certified and tested in California elections and key components of the proposal are missing.

California Gambling Control Commission

- F-44 ■ **Commission Responsibilities and Staffing Need Clarification.** Withhold recommendation on the pro-

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posed \$4.7 million for support of the California Gambling Control Commission because the commission's roles, responsibilities, and planned activities and the division of responsibilities between the commission and the Department of Justice need clarification.

- F-45 ■ **Legislature Needs to Be Informed of the Status of Indian Gambling Activities.** We recommend the California Gambling Control Commission report to the Legislature during the budget hearings on the status of funds received for deposit into the Revenue Sharing Trust Fund and the Special Distribution Fund and various other information required to conduct appropriate oversight of Indian gambling.

Secretary of State

- F-49 ■ **Business Automation Project.** Withhold recommendation on \$7.3 million to upgrade computerized systems for managing corporate and other public records because it lacks approval by the appropriate state agencies.

State Treasurer

- F-52 ■ **Additional Funds Not Needed to Fill Vacant Positions. Delete \$244,000 in Item 0950-001-0001.** Recommend deletion of \$244,000 because funding has already been provided for the positions which are proposed to be filled.
- F-53 ■ **Modified Workload Does Not Justify More Staff. Delete \$351,000 in Item 0950-001-0001.** Recommend deletion of \$351,000 because the office has not justified an increase in workload.

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Department of Consumer Affairs

- F-54 ■ **Smog Check Update.** Withhold recommendation on the Bureau of Automotive Repair's budget (Items 1111-002-1421 [\$91.6 million] and 1111-002-0582 [\$47.5 million]) pending receipt and review of information concerning (1) progress toward meeting requirements in the State Implementation Plan's proposed changes in the Smog Check program and (2) the expenditure of current-year funds and the results from spending these funds.

Department of Fair Employment and Housing

- F-60 ■ **Insufficient Justification of Increased Funding. Reduce Item 1700-001-0001 by \$151,000.** Recommend deletion of a total of \$151,000 and two positions because the department has not provided workload information for the requested positions.

Franchise Tax Board

- F-62 ■ **California Child Support Automation Project.** Recommend that the board update budget proposal consistent with latest report to the federal Administration of Children and Families.
- F-63 ■ **Child Support Collection Program.** Recommend that the board explain at budget hearings reasons it did not advise the Legislature of denial of federal funds, redirection of General Fund monies, and revised contracting strategy. Recommend that the Legislature consider amending existing law to delay a portion of arrearage collection time frame. Recommend that the board report on costs associated with deferring arrearage collection time lines.

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- F-68 ■ **Household and Dependent Care Expenses Credit Fraud.** Withhold recommendation on the board's request for \$3.8 million (General Fund) and 64.4 personnel-years for processing and fraud detection associated with implementation of the Household and Dependent Care Expense Credit pending receipt of additional information on actual filing for tax year 2000.

Department of General Services

- F-71 ■ **Positions in Division of the State Architect Should Be Report in Budget.** Recommend Legislature adopt supplemental report language directing the Department of Finance to report all positions, in the Division of the State Architect in the Governor's budget.
- F-72 ■ **Provision for Loan to Support DSAIs Not Needed. Delete Item 1760-001-0066, Provision 3.** Recommend deletion of authorization for loan up to \$4 million from the Service Revolving Fund to the Public School Planning, Design, and Construction Review Revolving Fund for support of the Division of the State Architect because it is not needed.
- F-72 ■ **Cost—and Cost of Living—Should Be Considered When Locating State Offices.** Recommend the Legislature direct the Department of General Services (DGS) to (1) relocate state offices leasing office space in high-cost areas that are not needed to serve the local community to less expensive areas when the current leases can be canceled.
- F-76 ■ **Reagan Building Costs Should Be Deleted From Statewide Building Rental Rate.** Recommend the Legislature approve budget bill language directing DGS to treat the Ronald Reagan Building in Los Angeles the same as other bond-funded buildings by excluding it

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from the statewide standard building rental rate and adjust all affected building rates accordingly.

- F-78 ■ **Asset Enhancement Consultant Services and General Fund Loan. Reduce Item 1760-012-0001 by 1.1 Million and Item 1760-015-0002 by \$1.9 Million.** Recommend deletion of proposal for property disposition studies because it is not clear there would be an economic benefit to state that would result from the studies.
- F-79 ■ **Need to Eliminate Deferred Maintenance.** Withhold recommendation on a \$2.7 million augmentation proposed for special repairs pending receipt of information from DGS detailing (1) the total deferred maintenance backlog, (2) a plan to eliminate the backlog, (3) annual funding needed for proper maintenance of state buildings, and (4) necessary adjustments to state building rental rates.
- F-80 ■ **Report on State's Telecommunications Contract.** Recommend that the Legislature take no action on proposal to reduce the DGS telecommunication expenditure authority until supplemental information on state's telecommunication contract has been received and reviewed.
- F-81 ■ **State's 911 Account and Surcharge.** Recommend that the Legislature direct DGS to identify (1) an appropriate reserve for the State Emergency Telephone Account Number and (2) adjustments to the 911 surcharge.
- F-82 ■ **Include Special Funds in Funding for eBusiness Center.** Recommend that the Legislature direct DGS to revise proposal to include special fund reimbursements for on-line activities.
- F-84 ■ **Distribute Costs for California Home Page and Governor's Office Network.** Recommend that the

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Legislature direct DGS to revise proposal to distribute costs among special funds and provide sufficient ongoing funding for California's home page.

Public Employees' Retirement System

- F-85 ■ **Cost Allocation Plan Reveals High Overhead Costs.** Recommend that prior to budget hearings the Public Employees' Retirement System advise the Legislature on (1) what actions it will take to ensure that expenditures to administer the state's health benefits program do not continue to exceed annual revenues and (2) the effect of reducing the 0.5 percent charge the state pays into the fund in order to reduce fund reserves.

Department of Alcoholic Beverage Control

- F-87 ■ **The ABC Fund Condition.** We recommend the Legislature enact legislation allowing the Department of Alcoholic Beverage Control to increase license fees to sustain current enforcement levels and avoid budgetary shortfalls.

Department of Financial Institutions

- F-90 ■ **Request to Relocate Sacramento Office Is Premature. Reduce Item 2150-001-0240 by \$24,000, Item 2150-001-0298 by \$315,000, and Item 2150-001-0299 by \$73,000.** Recommend that the Legislature delete \$412,000 for increased rent expenses associated with the proposed relocation of the Department of Financial Institutions' Sacramento office because the department's request is premature.

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Department of Corporations

- F-92 ■ **State Corporations Fund Balance Very High.** Recommend that the Department of Corporations report prior to budget hearings on (1) its fees and assessments, (2) proposed options for reducing or eliminating some of them, and (3) State Corporations Fund condition projections based on each option. Further recommend that upon evaluating this information, the Legislature enact legislation to change the fees and/or assessments.

Housing and Community Development

- F-99 ■ **Incentive Payments Unlikely to Change Behavior. Delete Item 2240-114-0001 and Item 2240-114-3006.** Recommend redirecting the proposed \$200 million augmentation for incentive payments to local governments to a more effective approach to addressing the state's lack of housing development.
- F-103 ■ **Infrastructure Program Not Targeted to Problem. Reduce Item 2240-001-0001 by \$200,000 and Item 2240-101-0001 by \$20 Million.** Recommend deleting the proposed \$20.2 million in funding for a new Central Valley Infrastructure Grant Program. The program would not address the underlying problem, other infrastructure programs already exist, and the funding would not make a significant impact.
- F-105 ■ **Employee Housing Costs Should Not Be Paid Twice. Amend the Employee Housing Act and Reduce Item 2240-001-0001 by \$50,000.** Recommend deleting a \$50,000 request for performing employee housing plan checks. Instead, the department should collect the necessary funding from the local governments which already received the payment of permit fees for the work.

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California Housing Finance Agency

- F-108 ■ **Eliminate Future Appropriations to School Facility Fee Housing Programs.** Amend state law to eliminate \$60 million in appropriations scheduled for 2001-02 and 2002-03. Given the limited use of the programs and concerns raised, previously appropriated funds should be sufficient to fund the programs through their conclusion at the end of calendar year 2002.

Department of Managed Health Care

- F-115 ■ **Financial Examinations Proposal Not Cost-Effective. Reduce Item 2400-001-0933 by \$300,000.** Recommend that the Legislature delete the \$300,000 request for consultant funds to increase the number of financial examinations of health plans performed annually because it does not provide sufficient resources to substantively increase the frequency of exams.

Stephen P. Teale Data Center

- F-117 ■ **Permanent Position Needed to Support Data Center Activities. Reduce 2780-001-0683 by \$116,000.** Recommend five additional positions rather than the use of overtime to support Teale Data Center's security and procurement advisement activities.

Technology, Trade, and Commerce Agency

- F-119 ■ **Consultant Funds for Military Base Retention and Reuse. Reduce Item 2920-001-0001 by \$100,000.** Recommend that the Legislature (1) delete \$100,000 of the proposed contract funds proposed for lobbying activities and (2) approve the remaining \$400,000 request for contract funds for one year only because the agency has not provided a more definite plan for the funds.

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- F-121 ■ **Augmentation Proposal for the California Technology Investment Partnership (CalTIP) Program Lacks Specifics. Reduce Item 2920-001-0001 by \$6.2 Million.** Recommend that the Legislature delete the \$6.2 million request to augment the CalTIP program because the proposal lacks necessary specifics to keep the Legislature informed of proposed program activities.

Energy Resources Conservation and Development Commission

- F-124 ■ **Additional Resources for Siting Program.** Withhold recommendation on the \$3.1 million General Fund request for 19 three-year limited-term positions (16 continuing and 3 new positions) and consulting funds for anticipated workload in the Energy Facilities Siting program until the commission provides an updated schedule of expected application filing dates and corresponding workload projections prior to budget hearings. Further recommend that if the Legislature approves an augmentation, it should be funded from the Energy Resources Programs Account (ERPA) rather than the General Fund.
- F-125 ■ **Long Term Energy Baseload Reduction Initiative. Augment Item 3360-001-0001 by \$3.5 Million and reduce Item 3360-001-0465 by \$3.5 Million.** Recommend that the Legislature approve the \$2.8 million General Fund request proposed for electricity demand analysis on a one-time basis as the Energy Commission has not made the case that General Fund support is needed on an ongoing basis. Further recommend that the Legislature approve \$3.5 million for one-time energy efficiency proposals and solar and distributed generation grant programs from the General Fund instead of ERPA.

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Energy Initiatives

- F-128 ■ **General Fund Monies Set Aside For Energy-Related Programs.** Withhold recommendation on the \$1 billion General Fund request for energy-related projects pending receipt and review of proposals for allocating these funds.

Health and Human Services Agency Data Center (HHSDC)

- F-130 ■ **Additional Department of Information Technology Oversight. Reduce Item 4130-001-0632 by \$524,000.** Recommend that the Legislature reduce the HHSDC's expenditure authority by \$524,000 because expenditure authority has never been needed nor is DOIT able to specify activities that this authority would provide.
- F-131 ■ **Project Management Software. Reduce Item 4130-001-0632 by \$78,000.** Recommend that the Legislature reduce the HHSDC expenditure authority by \$78,000 because current overhead charge should absorb the cost of software.
- F-131 ■ **Child Welfare Services/Case Management System (CWS/CMS) Maintenance and Operations. Reduce Item 4130-001-0632 by \$411,000 and authorize three additional positions.** Recommend that the Legislature reduce the proposed expenditure authority by \$411,000 and authorize three permanent positions for support of local area network. Adopt budget control language requiring HHSDC to amend CWS/CMS five-year maintenance and operation plan prior to increasing expenditure authority.
- F-133 ■ **The CWS/CMS Server Replacement.** Recommend that the Legislature adopt budget control language requiring the HHSDC to prepare risk mitigation plan prior to increasing expenditure authority.

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- F-136 ■ **Statewide Automated Welfare System (SAWS) Strategic Plan.** Recommend that the Legislature adopt supplemental report language requiring the Health and Human Services Agency and Department of Social Services (DSS) to develop a strategic plan describing SAWS program objectives.
- F-136 ■ **Los Angeles Eligibility Automated Determination, Evaluation and Report (LEADER).** Recommend that the Legislature require the HHSDC and DSS to report at budget hearings on the status of LEADER implementation.
- F-137 ■ **Interim Statewide Automated Welfare System (ISAWS).** Recommend that the HHSDC and the ISAWS consortium develop a five-year maintenance and operation plan to support the ISAWS system.
- F-138 ■ **Electronic Benefits Transfer.** Recommend that the Legislature take no action on the proposed expenditure authority increase and instead direct the HHSDC to submit a revised budget proposal consistent with contract negotiations.

California Arts Council

- F-140 ■ **Cultural Infrastructure Development Fund.** Withhold recommendation because program significantly expands the department's current mission and the proposal does not consider statewide capital outlay needs. Recommend the council report to the Legislature prior to budget hearings on (1) the policy and fiscal significance of formally expanding the council's mission, (2) provisions for incorporating the proposal into the state's five-year capital outlay plan, and (3) priorities and procedures for choosing grant recipients.

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- F-142 ■ **Museum Exhibit. Reduce Item 8260-103-0001 by \$3 million.** Delete funding for museum exhibit because request has not been justified.

Department of Industrial Relations

- F-144 ■ **Budget Realignment. Reduce Item 8350-001-0001 by \$1.3 Million and Item 8350-001-0223 by \$320,000.** Recommend deletion of \$1.3 millions from the General Fund and \$320,000 from special funds because the department has not justified the need for additional resources to fund existing salaries.
- F-145 ■ **Staff Redirected From Garment Manufacturing Program. Reduce Item 8350-001-0001 and Increase Item 8350-0001-3004 by \$565,000.** Recommend the Legislature not redirect 11 positions from the garment industry wage claim resolution program because (1) insufficient workload information is available to justify the redirection, (2) the impact on the garment industry regulatory process has not been identified, and (3) the shift is inconsistent with previous Legislative actions.
- F-146 ■ **Workers' Safety Training Grant Program. Delete \$2.5 Million Under Item 8350-001-0001.** Recommend deletion of \$2.5 million and three positions from the General Fund to administer a new workers' safety training grant program because of insufficient information on how the program will be administered.
- F-146 ■ **Increased Employer Education. Delete \$1.7 Million Under Item 8350-001-0001.** Recommend deletion of \$1.7 million from the General Fund for increased public information because the department (1) currently has sufficient resources for printing additional materials, (2) has Information Technology staff authorized to develop Internet-based information, and (3) has not prepared a Feasibility Study Report.

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- F-147 ■ **Amusement Ride Regulatory Process.** Recommend the department report to the Legislature at the time of budget hearings regarding the status of the new amusement ride regulatory process established by Chapter 585, Statutes of 1999 (AB 850, Torlakson).

Department of Personnel Administration

- F-150 ■ **One-Time Current-Year Funds for Collective Bargaining Consultant Should Be Deleted.** Reduce Item 8380-001-0001 by \$50,000. Recommend that the Legislature delete \$50,000 from the department's General Fund appropriation to remove one-time, current-year consultant funds related to collective bargaining from the department's budget.
- F-150 ■ **New Collective Bargaining Agreements To Be Negotiated.** The Department of Personnel Administration should report to the Legislature during budget hearings on the administration's collective bargaining proposals and the status of negotiations.

Department of Food and Agriculture

- F-152 ■ **Comprehensive Statewide Strategic Plan Not Yet Available.** Withhold recommendation on the \$112.7 million (\$71.5 million General Fund) for the Department of Food and Agriculture (DFA) Plant Pest Prevention, Detection, and Eradication programs pending receipt and review of the department's comprehensive statewide strategic plan that is to be sent to the Legislature by March 1, 2001.
- F-154 ■ **Glassy-Winged Sharpshooter (GWSS) Program.** Recommend the department to report to the Legislature, prior to budget hearings, on the development of clear goals and

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measurable outcome criteria for the Pierce's Disease/GWSS program.

- F-159 ■ **Headquarters Relocation Not Justified. Reduce Item 8570-001-0001 by \$566,000 Item 8570-001-0191 by \$66,000, and Item 8570-001-0111 by \$97,000.** Recommend the Legislature delete the \$729,000 augmentation request to move DFA from state-owned buildings into leased facilities because it is both costly and unnecessary to move the department.

Public Utilities Commission

- F-165 ■ **Universal Service Telephone Programs.** To improve legislative oversight, recommend that the Legislature adopt supplemental report language that requires the Public Utilities Commission (PUC) to submit to the Legislature an annual report that includes detailed programmatic information for each of the universal service programs.
- F-166 ■ **Compliance With Recent Legislation.** Recommend that the Legislature amend PUC's appropriation in the budget act to include funding, on a line-item basis, for each of the universal service programs. Further recommend that prior to budget hearings, PUC report on the plan for and progress of the required investigation of the universal service programs, issues PUC expects to address, and the schedule for completing the report.
- F-167 ■ **Monitoring of San Diego Gas and Electric Electricity Purchases.** Recommend that the Legislature approve \$682,000 and four positions for monitoring of electricity purchases on a two-year limited-term basis because of the uncertainty surrounding the electricity industry.
- F-168 ■ **Consultant Funds for Office of Ratepayer Advocates (ORA).** Reduce Item 8660-001-0462 by \$456,000.

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Recommend that the Legislature delete the \$456,000 request for additional consultant funds because (1) the complaint trend monitoring duplicates work performed by the Consumer Services Division and (2) the proposed commission proceedings workload should be prioritized within ORA's existing budget for consultants.

Electricity Oversight Board

- F-170 ■ **Consultant Funds for Electricity Market Analysis.** Withhold recommendation on the \$500,000 requested to contract with the University of California Energy Institute for electricity market analysis until the board reports to the Legislature prior to budget hearings on specific proposals to allocate the requested funds.

Department of Finance

- F-172 ■ **Information Technology Innovation Fund.** Recommend that the Legislature direct the Department of Finance (DOF) to report on Information Technology Innovation Fund activities.
- F-173 ■ **Vacancy and Underfunding Problems.** Recommend the DOF to report at budget hearings on the extent to which the proposed 2001-02 budget has reduced the need for departments to hold positions vacant to cover unbudgeted costs.

Military Department

- F-177 ■ **Cadet Corps Administrative Positions.** Recommend that positions remain limited term until the department submits evaluation of the program.
- F-178 ■ **Oakland Military Institute. Reduce Item 8940-001-0001 by \$1.3 Million.** Recommend reappropriation of unex-

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pending current-year funding and deletion of budget year funds because the program will not be operational in current year.

- F-179 ■ **Turning Point Academy.** Withhold recommendation pending revised proposal with better estimate of eligible population.

Department of Veterans Affairs and Veterans' Homes of California

- F-182 ■ **Serious Problems in Management and Operation of the Veterans' Home in Barstow.** We recommend that the Legislature not approve funding for the Barstow Veterans' Home (Item 8965-001-0001), until such time as the department reports to the Legislature on the progress and timetable for obtaining recertification of the facility.

Tax Relief

- F-187 ■ **Accelerate Transition for Vehicle License Fee (VLF) Offsets.** Begin the scheduled 67.5 percent VLF reduction on vehicle owners' registration bills a year early, resulting in one-time administrative savings of \$17 million from reduced rebate processing costs.

Local Government Financing

- F-189 ■ **Provide Long-Term Improvements to Property Tax System.** Replace the property tax administration loan program due to sunset with a long-term structural improvement to the property tax system.

- F-192 ■ **Use Funds Strategically for Reform.** Use the \$250 million in proposed local government fiscal relief strategically to achieve a specific reform goal.

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Health and Dental Benefits for Annuitants

- F-195 ■ **Budget-Year Costs Are Uncertain.** Withhold recommendation on the \$430.7 million General Fund request for annuitant benefits pending final determination of health insurance premium rates for calendar year 2002.

Augmentation for Employee Compensation

- F-198 ■ **Legislature Needs to Strengthen Its Collective Bargaining Oversight.** Recommend that the Legislature require a minimum 30-day review period for collective bargaining proposals and review proposals at budget hearings for adoption in the budget act. Further, the Department of Personnel Administration should report to the budget committees during budget hearings on the administration's collective bargaining proposals and the status of negotiations.

Janitorial/Contract Services

- F-201 ■ **Janitorial/Contract Services.** Withhold recommendation on \$6 million for employee benefits related to Janitorial/Service contracts pending receipt, prior to budget hearings, of a report from the Department of Finance on the method used in the current year to allocate funds for this purpose, the amount allocated to contractors, the balance of the current-year appropriation, and the basis for the budget-year request.

Utilities Costs

- F-203 ■ **Department Costs For Natural Gas and Electricity. Delete Provision 3 From Item 9911-001-0001 (with conforming changes in Item 9911-001-0494 and Item 9911-001-0988).** Withhold recommendation on the \$50 million proposal to fund departments' increased

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natural gas and electricity costs, pending receipt and review of documentation justifying the requested amount. Further, recommend the Legislature approve any funding on a one-time basis, instead of annually as requested, and delete proposed budget bill language that would authorize the Department of Finance to augment the \$50 million.

Control Section 3.60

- F-204 ■ **State Contribution Rates to PERS Expected to Increase.** Withhold recommendation on 2001-02 state contribution rates for retirement benefits pending (1) final determination of the actual rates to be applied in the budget year and (2) receipt and review of information regarding the actuarial assumptions underlying the rates.

