

## State Mandates

### Operational and Structural Changes Have Yielded Limited Improvements in Expediting Processes and in Controlling Costs and Liabilities

REPORT NUMBER 2009-501, OCTOBER 2009

*Responses from the Commission on State Mandates and State Controller's Office as of October 2010; Department of Finance's response as of November 2009*

The California Constitution requires that whenever the Legislature or any state agency mandates a new program or higher level of service for a local entity, the State is required to provide funding to reimburse the associated costs, with certain exceptions. The Commission on State Mandates (Commission), the State Controller's Office (Controller), the Department of Finance (Finance), and local entities are the key participants in California's state mandate process. The Bureau of State Audits (bureau) examined the state mandates process under its authority to conduct both follow-up audits and those addressing areas of high risk. To follow up on our prior audits, we reviewed the status of the Commission's work backlogs and assessed how processing times had changed over the years. We also reviewed the Controller's efforts for using audits to identify and resolve problems in state mandate claims. Further, we evaluated how the State's mandate liability had changed from June 2004 to June 2008. Finally, we assessed the effect of recent structural changes on the state mandate process and summarized possible ways to accomplish the process more effectively.

#### **Finding #1: The Commission still has lengthy processing times and large backlogs.**

A test claim from a local entity begins the process for the Commission to determine whether a mandate exists. Although the Commission's test claim backlog dropped from 132 in December 2003 to 81 in June 2009, 61 test claims filed before December 2003 are still pending. In addition, between fiscal years 2003–04 and 2008–09, the Commission did not complete the entire process for any test claims within the time frame established in state law and regulations. In fact, during this period, the Commission's average elapsed time for completing the process was more than six years, and between fiscal years 2006–07 and 2008–09, the average time increased to more than eight years. Both the test claim backlog and the delays in processing create significant burdens on the State and on local entities. At the state level, these conditions keep the Legislature from knowing the true costs of mandates for years; as a result, the Legislature does not have the information it needs to take any necessary action. Additionally, as the years pass, claims build, adding to the State's growing liability.

In addition, the Commission has not addressed many incorrect reduction claims, which local entities file if they believe the Controller has improperly reduced their claims through a desk review or field audit. The Commission has only completed a limited number of these claims, and consequently its backlog grew from 77 in December 2003 to 146 in June 2009. The Commission's inability to resolve these claims

#### **Audit Highlights . . .**

*Our review of state mandate determination and payment processes found that:*

- » *The Commission on State Mandates (Commission) still has a large backlog of test claims, including many claims from 2003 or earlier.*
- » *The Commission's backlog of incorrect reduction claims has significantly increased and creates uncertainty about what constitutes a proper claim.*
- » *The high level of audit adjustments for some mandates indicates that the State could save money if the State Controller's Office filled 10 vacant audit positions.*
- » *The State's liability for state mandates has grown to \$2.6 billion in June 2008, largely because of insufficient funding.*
- » *Recent reforms that could relieve the Commission of some of its workload have rarely been used.*
- » *A number of state and local entities have proposed mandate reforms that merit further discussion.*

leaves local entities uncertain about what qualifies as reimbursable costs. Conversely, the Commission has processed most requests for amendments to state mandate guidelines, completing 61 of 70 requested amendments between January 2004 and June 2009. Nevertheless, it did not address an amendment submitted by the Controller in April 2006 that requests the incorporation of standardized language into the guidelines for 49 mandates determined before 2003. Commission staff said that pending litigation caused them to suspend work on the boilerplate request. Although the court's February 2009 decision is on appeal, Commission staff have scheduled 24 mandates for review in 2009 and 25 for review in early 2010.

We recommended that the Commission work with Finance to seek additional resources to reduce its backlog, including test claims and incorrect reduction claims. We also recommended that the Commission implement its work plan to address the Controller's amendment.

***Commission's Action: Partial corrective action taken.***

The Commission said that it did not file a budget change proposal seeking additional resources because Budget Letter 10-23 required departments to provide monetary reductions when submitting budget change proposals for fiscal year 2011–12. Related to the Controller's amendment request, the Commission says it has completed amendments for all 49 mandates, determined before 2003, that were included in the request.

**Finding #2: The Controller appropriately oversees mandate claims, but vacant audit positions, if filled, could further ensure that mandate reimbursements are appropriate.**

The Controller uses a risk-based system for selecting the state mandate claims for reimbursement that it will audit, has improved its process by auditing claims earlier than in the past, has sought guideline amendments to resolve identified claims issues, and has undertaken outreach activities to inform local entities about audit issues. Nevertheless, continuing high reduction rates, reflecting large audit adjustments for some mandates, indicate that filling vacant audit positions and giving a high priority to mandate audits could save money for the State. The Controller has reduced 47 percent of the cumulative dollars it has field-audited for all mandate audits initiated since fiscal year 2003–04, cutting about \$334 million in claims. Audit efforts were greatly aided by a 175 percent increase in audit staff positions in the Controller's Mandated Cost Audits Bureau (from 12 to 33) in fiscal year 2003–04. However, the Controller was not able to take as much advantage of an additional increase of 10 staff positions two years later, and has had 10 or more authorized field-audit positions unfilled since fiscal year 2005–06. Given the substantial amounts involved, filling these positions to maximize audits of mandate claims is important to better ensure that the State makes only appropriate reimbursements.

We recommended that to ensure it can meet its responsibilities, including a heightened focus on audits of state mandates, the Controller work with Finance to obtain sufficient resources and increase its efforts to fill vacant positions in its Mandated Cost Audits Bureau.

***Controller's Action: Partial corrective action taken.***

The Controller said it lost 11 positions and related spending authority effective June 30, 2010, but worked closely with Finance to restore 10 positions in the fiscal year 2010–11 budget. The Controller also stated that it is working on allocating General Fund resources to fill vacant positions.

**Finding #3: New mandate processes have been rarely used, and the State has done little to publicize these alternative processes.**

New processes intended to relieve the Commission of some of its work have rarely been used. One of these options allows Finance and the local entity that submitted the test claim to notify the Commission of their intent to pursue the jointly developed reasonable reimbursement methodology process (joint process), within 30 days of the Commission's recognition of a new mandate. In this process, Finance

and the local entity join to create a formula for reimbursement rather than basing it on detailed actual costs. Although Commission participation is not eliminated, the joint process greatly reduces the Commission's workload related to establishing a mandate's guidelines and adopting a statewide cost estimate. As of August 2009, the joint process had only been implemented once, and the legislatively determined mandate process, another new process, had not generated any new mandates. Additionally, the Commission can work with Finance, local entities, and others to develop a reimbursement formula for a mandate (Commission process) instead of adopting guidelines for claiming actual costs in the traditional way. Between 2005 and 2008, the Commission had to assure that reimbursement formulas following the Commission process considered the costs of 50 percent of all potential local entities, a standard Commission staff said was difficult to meet. Since the elimination of the 50 percent criterion, the Commission process has been used twice as of August 2009. One factor that may be contributing to the lack of success of the new and revised processes is the State's limited efforts to communicate them to local entities. In particular, we noted that as of July 2009 neither Finance nor the Commission had provided information on their Web sites publicizing the existence of the alternative processes.

We recommended that the Commission add additional information in its semiannual report to inform the Legislature about the status of mandates being developed under joint and Commission processes, including delays that may be occurring. We also recommended that the Commission and Finance inform local entities about alternative processes by making information about them readily available on their Web sites.

***Commission's Action: Corrective action taken.***

In September 2010 the governor approved Chapter 699, Statutes of 2010, requiring that the Commission's semiannual report to the Legislature include information on the status of mandates being developed under joint and Commission processes, and any related delays in their development. The Commission also added information about alternative processes to its Web site.

***Finance's Action: Corrective action taken.***

To provide information regarding reimbursable state mandates, including the processes for seeking a mandate determination, Finance added links on its Web site to the Commission's and Controller's Web sites.

**Finding #4: A recent court case overturned revised test claim decisions.**

In March 2009 a state court of appeal held that the Legislature's direction to the Commission to reconsider cases that were already final violates the separation of powers doctrine. The court stated that it did not imply that there is no way to obtain reconsideration of a Commission decision when the law has changed, but that the process for declaring reconsideration was beyond the scope of its opinion. In April 2009 an Assembly Budget Subcommittee recognized the importance of reforming the reconsideration process and, according to Commission staff, directed Finance, the Legislative Analyst, and Commission and legislative staff to form a working group to develop legislation to establish a mandate reconsideration process consistent with the court decision. Until a new reconsideration process is established, mandate guidelines may not reflect statutory or other relevant changes. Thus, the State could pay for mandate activities that are no longer required.

We recommended that the Commission continue its efforts to work with the legislative subcommittee and other relevant parties to establish a reconsideration process that will allow mandates to undergo revision when appropriate.

***Commission's Action: Corrective action taken.***

In October 2010 the governor approved Chapter 719, Statutes of 2010, authorizing the Commission to adopt new test claim decisions upon a showing that the State's Liability for a previously adopted decision has been modified on a subsequent change in law.

