



August 25, 2020  
**2020-602**

The Governor of California  
President pro Tempore of the Senate  
Speaker of the Assembly  
State Capitol  
Sacramento, California 95814

Dear Governor and Legislative Leaders:

As authorized by state law, my office presents this letter report designating the State's management of federal funds related to Coronavirus Disease 2019 (federal COVID-19 funds) as a high-risk statewide issue in California. Congress enacted legislation in March and April 2020 that included funding for states to help mitigate the effects of COVID-19. We reviewed available information about this funding that California departments received, or expect to receive, and we made our determination based on our evaluation of several factors including, but not limited to, the following:

- The significant amount of funding granted to the State.
- The expansion of or changes to programs' eligibility requirements.
- Program changes that could necessitate additional outreach by departments to ensure awareness of and access to available funds.
- Past audit findings on management of federal funds by state departments that will receive or expect to receive these funds.
- The rapid nature of the allocation and the urgent need of the funding.

This letter report identifies 18 state agencies that will each be responsible for managing a portion of the federal COVID-19 funds. Before finalizing our determination to add this issue to the state high risk list, we notified the 18 responsible state agencies about our preliminary determination and invited them to provide their perspective on the issue. We received responses from 12 of the 18 state agencies, and we summarize those responses at the end of this letter. Our analysis herein is up to date generally as of June 30, 2020, and as part of our State High-Risk program, we will continue to monitor California's receipt of federal COVID-19 funds, including any future enacted federal legislation or allocations to California agencies.

### **The State High-Risk Government Agency Audit Program**

California Government Code, section 8546.5 authorizes the California State Auditor (State Auditor) to develop a state high-risk government agency audit program for the purpose of identifying, auditing, and issuing reports on any agency of the State or statewide issue that my office identifies as being at high risk. Specifically, my office may determine that a state agency or statewide issue is high risk if, in our professional judgement, the agency or issue is at risk of suffering or producing waste, fraud, abuse, and mismanagement or major challenges associated with economy, efficiency, or effectiveness. In accordance with statutory authority, my office adopted regulations in 2016 that provide the criteria

and procedures we use to determine high-risk agencies and statewide issues. These regulations allow us to amend the state high risk list, last published in January 2020 (*State High Risk: The California State Auditor's Updated Assessment of High-Risk Issues Faced by the State and Select State Agencies*, Report 2019-601, January 2020), to add a statewide issue that is in urgent need of attention because of its increased risk of fraud, waste, abuse, or mismanagement. We provide the amended list as an attachment to this letter.

### **California Is Receiving Substantial Federal Funding to Assist Its Response to COVID-19**

The unprecedented public health emergency caused by COVID-19 spurred the federal government to enact legislation that has provided assistance to individuals, businesses, and state and local governments to deal with the effects of the pandemic. Specifically, the federal legislation for COVID-19 response includes, but is not limited to, the following four acts:

- The Coronavirus Preparedness and Response Supplemental Appropriations Act, 2020.
- The Families First Coronavirus Response Act.
- The Coronavirus Aid, Relief, and Economic Security Act (CARES Act).
- The Paycheck Protection Program and Health Care Enhancement Act.

For states, these federal laws generally provide authority for federal agencies to allocate funding for new programs and provide additional funding for existing programs. For example, the CARES Act provides more than \$2 trillion in emergency assistance and health care response, including \$150 billion for the Coronavirus Relief Fund, of which California received \$15.3 billion—\$5.8 billion paid directly to eligible local governments and \$9.5 billion paid to the State. Additionally, the President issued an emergency declaration in March 2020 that allows state and local governments to apply to the Federal Emergency Management Agency (FEMA) for partial reimbursement of certain emergency protective measures they may take in response to COVID-19.

According to the Governor's Budget for fiscal year 2020–21, the COVID-19 pandemic has affected every sector of California's economy and has caused record-high unemployment. Our analysis identified 18 state departments that have received or expect to receive a total of more than \$71 billion in federal COVID-19 funding to operate more than 35 federal programs. We identify the departments listed in Table 1 as the state agencies responsible for a portion of the high-risk statewide issue. Several programs will receive or have received an amount of federal funding that exceeds their recent annual expenditures. Notably, the Employment Development Department (EDD) expects to spend more than \$40 billion related to the unemployment insurance program, which is nearly seven times the amount it spent in fiscal year 2018–19 on the program. Other departments expect to receive federal COVID-19 funding for new programs; for example, the California Department of Education expects to receive roughly \$2 billion from the Education Stabilization Fund, to, among other objectives, provide emergency relief funds to local educational agencies to address the effects of COVID-19. Because new programs require departments to quickly establish new management controls, the significant influx of federal funding creates risks for the State as it establishes and manages the associated programs.

**Table 1**  
**Responsible State Agencies Expect to Receive More Than \$71 Billion in Federal Funding Related to COVID-19**

RESPONSIBLE STATE AGENCY	FEDERAL CATALOG NUMBER - PROGRAM NAME	AMOUNT (IN MILLIONS)
Aging, California Department of	93.045 - Special Programs for the Aging, Title III, Part C, Nutrition Services	75
	93.044 - Special Programs for the Aging, Title III, Part B, Grants for Supportive Services and Senior Centers	21
	93.052 - National Family Caregiver Support, Title III, Part E	10
	93.048 - Special Programs for the Aging, Title IV, and Title II, Discretionary Projects	3
	93.042 - Special Programs for the Aging, Title VII, Chapter 2, Long-Term Care Ombudsman Services for Older Individuals	2
Arts Council, California	45.025 - Promotion of the Arts Partnership Agreements	1
California Community Colleges	84.425 - Education Stabilization Fund	586
California State University	84.425 - Education Stabilization Fund	525
Community Services and Development, Department of	93.569 - Community Services Block Grant	89
	93.568 - Low-Income Home Energy Assistance Program	50
Education, California Department of	84.425 - Education Stabilization Fund	2,000
	93.575 - Child Care and Development Block Grant	350
	10.553, 10.555, 10.556, and 10.559 - Child Nutrition Cluster	Unknown*
Emergency Services, California Governor's Office of	97.036 - Disaster Grants-Public Assistance (Presidentially Declared Disasters)	5,300†
	97.042 - Emergency Management Performance Grants	8
	93.671 - Family Violence Prevention and Services/Domestic Violence Shelter and Supportive Services	4
Employment Development Department	17.225 - Unemployment Insurance	\$40,000‡
	17.277 - Workforce Innovation and Opportunity Act National Dislocated Worker Grants/ Workforce Investment Act National Emergency Grants	24
Finance, Department of	21.019 - Coronavirus Relief Fund	9,500
Health Care Services, Department of	93.778 - Medical Assistance Program (Medi-Cal)§	10,200
	93.301 - Small Rural Hospital Improvement Grant Program	4
	93.665 - Emergency Grants to Address Mental and Substance Use Disorders During COVID-19	2
Housing and Community Development, Department of	14.231 - Emergency Solutions Grant Program	316
	14.228 - Community Development Block Grants	133
Public Health, California Department of	93.323 - Epidemiology and Laboratory Capacity for Infectious Diseases	546
	93.354 - Public Health Emergency Response	60
	93.268 - Immunization Cooperative Agreements	20
	93.889 - National Bioterrorism Hospital Preparedness Program	9
	93.317 - Emerging Infections Programs	3
	93.917 - Human Immunodeficiency Virus Care Formula Grants	2
	14.241 - Housing Opportunities for Persons with AIDS	1
	10.557 - Special Supplemental Nutrition Program for Women, Infants, and Children	Unknown*
Secretary of State's Office	90.404 - Help America Vote Again Election Security Grants	36
Social Services, California Department of	10.561 and 10.551 - Supplemental Nutrition Assistance Program Cluster	1,400‡
	10.568 and 10.569 - Emergency Food Assistance Program	102
	93.645 - Stephanie Tubbs Jones Child Welfare Services Program	5
State and Community Corrections, Board of	16.034 - Coronavirus Emergency Supplemental Funding Program	59
State Library, California	45.310 - Grants to States	4

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RESPONSIBLE STATE AGENCY	FEDERAL CATALOG NUMBER - PROGRAM NAME	AMOUNT (IN MILLIONS)
Transportation, Department of	20.509 - Formula Grants for Rural Areas and Tribal Transit Program	95
University of California	84.425 - Education Stabilization Fund	260
<b>Totals</b>		<b>\$71,805</b>

Source: Analysis of federal legislation; guidance issued by federal agencies; state departments' websites; and federal assistance award listings. We identified the programs and amounts based on the sources listed, but acknowledge that there may be other programs we have not yet identified or that the amounts may change.

\* The federal legislation provides additional funding for the Child Nutrition Cluster programs and the Special Supplemental Nutrition Program for Women, Infants, and Children—\$8.8 billion and \$500 million, respectively—both administered by the U.S. Department of Agriculture. As of the date of this letter, the portion allocated to California is not yet known.

† Based on estimated disaster-related costs, which assumes 75 percent Federal Emergency Management Agency reimbursement.

‡ The State believes the amount could be higher, depending on the number of people participating in the program.

§ Also includes Medi-Cal funding for programs operated by the California Department of Social Services.

## Departments That Poorly Manage Federal COVID-19 Funding May Negatively Affect Californians

Because of the pandemic, a record number of Californians are now eligible for federally funded programs that help individuals maintain their health and pay for food and shelter. According to the Governor's Budget for fiscal year 2020–21, almost one in five California workers who were employed in February 2020 were out of work in May 2020. From March 2020 through May 2020, EDD received more than 5 million initial claims for unemployment insurance, which is more than twice the number of initial unemployment claims it received in all of calendar year 2019. Various news articles have reported that EDD has been unable to handle the surge in unemployment claims, therefore raising questions about EDD's capacity to promptly provide the unemployment insurance assistance to those in the most need.

A significant amount of the federal COVID-19 funding provided to California was directed at federal programs—including unemployment insurance and Medicaid (referred to as *Medi-Cal* in California)—that provide assistance to individuals who are not working or have low incomes. Given the financial impact that the pandemic has had on workers, California departments must engage in outreach efforts to ensure that newly eligible individuals understand the new or enhanced benefits available to them, as well as how to apply for the benefits. Failure to adequately do so could leave people without medical care or money to pay for housing and food for themselves and their families.

The CARES Act expanded the unemployment insurance program in several ways, including temporarily extending benefits to contract workers and the self-employed, providing out-of-work individuals with an additional 13 weeks of benefits, and increasing the weekly benefit amount paid to them. The federal government also temporarily increased the percentage it will reimburse the State for eligible Medi-Cal expenses, as long as the State does not terminate coverage for those who fail to pay premiums. The program changes resulting in temporary expansions of eligibility increase the risk that departments will inappropriately deny or delay benefits to eligible beneficiaries.

The federal government also allocated a significant amount of supplemental funding to the State for public health activities. Specifically, the Centers for Disease Control and Prevention (CDC) awarded \$546 million to California as part of the Epidemiology and Laboratory Capacity for Infectious Diseases program to, among other objectives, expand and oversee testing for COVID-19; conduct contact tracing; and monitor the number and availability of critical care staff, necessary personal protective equipment, and potentially life-saving medical equipment. In federal fiscal year 2019,

the CDC awarded California \$10 million under this program, which the California Department of Public Health operates through a third-party. If the State uses these federal funds effectively, it can help protect Californians' health. On the other hand, delays in their use or mismanagement of these funds could further harm public health if the State is not able to take quick and effective action to slow the disease's spread.

Some of California's youth and students also depend on federal assistance to avoid going hungry or to pay for housing or other expenses that allows them to remain enrolled in higher education. For example, the State estimated that 3.8 million children—more than half of the children enrolled in the State's public schools—qualified for free or reduced-price school meals when schools closed in spring 2020. To ensure that these children continued to receive these meal services, the federal government approved the State's plan to use about \$1.4 billion of federal funds for the California Department of Social Services (Social Services) to provide free breakfast and lunch to these children through the Supplemental Nutrition Assistance Program. At the same time, many of the 2.9 million students enrolled at the campuses of the University of California, California State University, and California Community Colleges need assistance to cope with the disruptions to campus operations, including possible changes to their housing circumstances. To help these students, the federal government provided these institutions of higher education with a total of nearly \$1.4 billion, of which at least half must be allocated to students. If Social Services and these institutions of higher education fail to effectively distribute the federal funding they receive to mitigate the effects of the pandemic, youth and students throughout the State may go hungry or without housing.

### **Departments Face Significant Hurdles in Managing Federal COVID-19 Funding, Which Create a High Risk for Inefficiencies and Waste**

Multiple factors create potential for inefficiencies and waste that may impair the effective and timely delivery of crucial government services supported by federal COVID-19 funds. For example, departments sometimes rely on subrecipients and vendors to provide services and must monitor these third parties to ensure that they use federal funds appropriately. However, recent audits of departments administering federal programs identified deficiencies in their management controls and monitoring activities that could cause departments to mismanage federal COVID-19 funding. In fact, nine of the programs that have received or expect to receive federal COVID-19 funds were audited in one of the two most recently completed federal compliance audits and six had findings concerning the management of those programs' funds. For example, we identified that both Social Services and the California Department of Education did not properly monitor subrecipients to ensure they are not wrongfully denying benefits to program participants or inaccurately determining benefits. Our office also identified that the Department of Health Care Services (Health Care Services) did not properly document determinations of eligibility for Medi-Cal. Moreover, in October 2018 our office reported that Health Care Services made \$4 billion in questionable Medi-Cal payments because of pervasive discrepancies between State and county determinations of beneficiaries' eligibilities for these services (*Department of Health Care Services: It Paid Billions in Questionable Medi-Cal Premiums and Claims Because It Failed to Follow Up on Eligibility Discrepancies*, Report 2018-603, October 2018). These past audit findings highlight issues with departments' abilities to manage federal funds appropriately even before the significant influx of federal COVID-19 funding. Some departments will also need to reconfigure their processes for evaluating applications for program benefits in order to manage considerable increases in the number of program applicants.

The urgency with which Congress passed legislation to provide funding related to COVID-19 should spur the State to distribute this funding as quickly as possible. Specifically, three of the four laws Congress passed to provide funding to states in response to COVID-19 became law before the end of March 2020—just two months after the director-general of the World Health Organization declared COVID-19 a public health emergency of international concern. This short time frame demonstrates the urgency of the federal legislation, and that the State should strive to distribute the federal COVID-19 funds as quickly as possible to provide assistance to individuals and local governments. However, some departments have not yet announced the availability of federal COVID-19 funds. For example, the federal government allocated \$133 million from the CARES Act to the California Department of Housing and Community Development (HCD) in April and May 2020. Although HCD announced in early June 2020 the availability of \$19 million for activities to prevent, prepare for, and respond to COVID-19, as of early August 2020, HCD had not announced the availability of the remaining funds. More concerning, recent media reports have highlighted EDD's struggle to process unemployment insurance claims, resulting in delays in getting critical funds to those in need. Specifically, EDD has asserted that it paid 4.8 million claims between March 2020 and mid-July 2020, but is still working to process more than 1.1 million claims. Further, in early August 2020, EDD acknowledged a four- to six-week delay in helping Californians through its call center. Likely as a result of these delays, many Californians have turned to their state representatives in the Legislature to ask for help with their claims. EDD must quickly provide the assistance to those in need, but it must also take care to protect Californians against identity theft amid a spike nationally in fraudulent unemployment insurance claims as reported by the Federal Bureau of Investigation in July 2020. Delays in distributing federal COVID-19 funding represent an impairment of the delivery of important government services, and may damage public confidence in government.

State departments could also face difficulty in accurately and consistently tracking spending related to COVID-19. Since early March 2020, the Department of Finance (Finance) has required state departments to report their costs related to COVID-19 to Finance every month. In June 2020, Finance then directed departments to categorize expenditures related to COVID-19 and to track those expenditures using the State's new financial system, the Financial Information System for California (FI\$Cal). However, problems with the functionality of that system led my office to recently identify the State's financial reporting and accountability as a high-risk issue to the State. Specifically, we added this issue to our state high risk list in January 2020 (*State High Risk: The California State Auditor's Updated Assessment of High-Risk Issues Faced by the State and Select State Agencies*, Report 2019-601, January 2020) because, among other issues, some departments using FI\$Cal were only able to prepare estimated financial reports, which threatens the State's ability to accurately report financial information, including expenditures related to COVID-19.

The financial reporting relative to federal COVID-19 funding is crucial for the State to be able to take full advantage of federal assistance. As a condition of receiving the federal funds, the federal law requires recipients, such as the State, to properly account for and report on the use of the funds. In a more specific example, the State must effectively track and justify the costs of its COVID-19-related emergency protective measures to ensure that it maximizes the reimbursement that FEMA will provide. Additionally, the State must be able to demonstrate that it is complying with the requirement imposed by some federal programs that California provide some amount of matching state funds with federal COVID-19 funds.

Federal legislation that provides additional funds to state departments to address the continuing effects of COVID-19 may further exacerbate these potential challenges, including monitoring COVID-19 expenditures. As of August 2020, media reports indicated that Congress considered

federal legislation to provide additional COVID-19-related relief funds to states and that the California Legislature has considered enacting state legislation to provide state stimulus funds to assist small businesses, among others. As of the date of this letter, neither federal nor state legislation has been enacted, but additional funding could magnify the challenges associated with state departments' management of such funding. Specifically, state departments may experience additional challenges monitoring any subrecipients or vendors that provide services with the funding or tracking accurately and consistently their spending related to COVID-19. The likelihood of state agencies receiving additional funding further indicates that the State's management of federal COVID-19 funding constitutes a high risk for California because the State or its residents may experience significant harm if departments mismanage this funding.

The challenges described above support our determination that the State's management of federal funding related to COVID-19 is a high-risk issue for California. The likelihood of mismanagement of these funds is great enough to create a substantial risk of serious detriment to the State and its residents, including a reduction in residents' overall health or safety, widespread damage to public confidence in California government, and impairment of the delivery of important government services. Moreover, the swift appropriation of federal COVID-19 funds, along with the prior audit findings, raise the possibility that responsible state agencies do not have adequate processes in place to address these risks. These risks may be reduced significantly by an audit of the responsible state agencies.

### **Perspective From Responsible State Agencies**

Of the 18 responsible state agencies we identified, 12 provided responses to the notice we sent that preliminarily identified them as responsible state agencies for the proposed new state high-risk issue. Most of the responding state agencies did acknowledge that they were the agencies responsible for managing a portion of federal COVID-19 funds the State will receive or has received. However, most of the state agencies believe that the management of those funds is not high risk for various reasons, such as their existing monitoring, tracking, and reporting mechanisms for federal funds. Several state agencies also cited existing oversight or audit requirements or a readiness review that Finance recently conducted as reasons this issue is not high risk. However, we note on page 5 that prior audits identified issues with departments' management of federal funds, including departments not properly monitoring subrecipients of similar kinds of funding. Further, we believe that additional and independent oversight of state departments' management of federal COVID-19 funds as part of the state high-risk program would increase transparency and may identify potential problems earlier. Thus, we stand by our determination and reasoning that the State's management of federal COVID-19 funding is a high-risk issue for California.

In its response to our notice, Finance indicated that it believes that the State's management of federal COVID-19 funds does not meet the regulatory criteria, nor does adding the issue to the high risk list serve the purpose of the state high-risk program. Among its arguments, Finance asserted that the State's management of federal COVID-19 funds does not present a substantial risk of serious detriment to the State or its residents. Although we appreciate its perspective, we note that a substantial risk of serious detriment may result from a change of circumstances that challenges existing state management controls. In this case, the change of circumstances is the significant influx of federal COVID-19 funds, the mismanagement of which could result in serious detriment to the

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State and its residents. Given that the purpose of federal COVID-19 funds is to help Californians through a life-threatening pandemic that has upended the economy, we assess the level of serious detriment as high if state departments do not properly manage these funds.

Finance additionally asserted in its response to our notice that because the State has only recently received federal COVID-19 funds, we cannot show that responsible state agencies have not taken adequate corrective actions to prevent the risk of serious detriment to the State and its residents. We disagree. The fact that the federal government only recently provided these funds, along with our descriptions of state departments' past and potential challenges with managing these funds, demonstrates the urgent need for attention to this issue particularly with so many Californians needing help now. Furthermore, conducting audits at this early stage will allow us to identify problems and make recommendations while departments are still able to effectively use the federal COVID-19 funds.

In conclusion, adding this issue to the state high risk list aligns with the purpose of the state high-risk program—to improve the operation of state government—and we therefore stand by our assessment and conclusion to add the State's management of federal COVID-19 funds as an issue on the state high risk list.

We prepared this report under the authority vested in the California State Auditor by Government Code section 8546.5.

Respectfully submitted,



ELAINE M. HOWLE, CPA  
California State Auditor

August 25, 2020

**Attachment**  
**Current State High Risk List**

HIGH-RISK ISSUE OR HIGH-RISK AGENCY	MOST RECENT DESCRIPTION OF ISSUE	FIRST ADDED TO HIGH-RISK LIST
State Management of Federal COVID-19 Funds (New High-Risk Issue)	The challenges of managing federal COVID-19 funds may negatively affect the State's ability to mitigate the impact of the pandemic on Californians.	2020
State Financial Reporting and Accountability	The transition to FISCal has diminished the State's financial reporting and accountability and could lead to increased borrowing costs.	2020
Water Infrastructure	Efforts to improve emergency planning for dams are ongoing and the State's long-term water supply remains uncertain.	2018
Information Security	Continued deficiencies in information system controls remain a concern.	2013
Kindergarten Through 12 <sup>th</sup> Grade Education	The State has not ensured that local educational agencies spend local control formula funds appropriately.	2013
Higher Education	Affordability issues persist within the University of California and California State University systems.	2013
California State Teachers' Retirement System	Significant time necessary to reduce its unfunded liability remains a concern.	2011
Transportation Infrastructure	The Transportation Commission and Caltrans have made progress improving the State's transportation infrastructure, but high risk monitoring should continue.	2007
Information Technology Oversight	Concerns about implementation of the State's information systems and continued reliance on legacy systems.	2007
California Department of Corrections and Rehabilitation	Significant deficiencies remain in its inmate health care system.	2007
Department of Health Care Services (Health Care Services)	Health Care Services has not corrected discrepancies in its Medi-Cal eligibility system or provided adequate oversight of funding for mental health services.	2007
California Department of Public Health (Public Health)	Public Health has not addressed certain concerns that could affect the health and safety of patients and the public.	2007
Other Postemployment Benefits	Significantly underfunded liability and future investment volatility remain concerns.	2007

Source: The California State Auditor's State High Risk Reports.