AGENDA

ASSEMBLY BUDGET SUBCOMMITTEE NO. 4 ON STATE ADMINISTRATION

Assemblymember Rudy Bermudez, Chair

TUESDAY, APRIL 26, 2005
1:30 PM, ROOM 447

ITEMS TO BE HEARD

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ITEM 0840 STATE CONTROLLER

The State Controller is the Chief Financial Officer of the state. The primary functions of the State Controller (SCO) are to provide sound fiscal control over both receipts and disbursements of public funds; to report periodically on the financial operations and condition of both state and local government; to make certain that money due the state is collected through fair, equitable, and effective tax administration; to provide fiscal guidance to local governments; to serve as a member of numerous policy-making state boards and commissions; and to administer the Unclaimed Property and Property Tax Postponement Programs. Total proposed budget expenditures are $124.7 million (an increase of $9.6 million or 8.3 percent from 2004-05), of which $72.7 million is from the General Fund (an increase of $1.7 million or 2.4 percent). Proposed staffing increases from 1,119.1 personnel-years (PYs) in the current year to 1,137.9 PYs in 2005-06, an increase of 1.7 percent.

Most of the overall funding increase relates to the Human Resource Management System (known as the "21st Century Project"). The Governor's Budget proposes to add $10.4 million ($7.9 million in special funds, $2.5 million in reimbursements) and 29.7 positions in the budget year to continue activities associated with the replacement of the existing employment history, payroll, leave accounting, and position control systems.

The following tables show funding and staffing by program for the State Controller's Office for the three years 2003-04 through 2005-06 (as proposed in the Governor's Budget).

State Controller
EXPENDITURES BY PROGRAM
(in thousands)

Program	Actual 2003-04*	Estimated 2004-05*	Proposed 2005-06*
Accounting and Reporting	$11,434	$12,680	$14,266
Audits	22,035	22,908	24,232
Personnel/Payroll Services	21,229	26,338	32,559
Information Systems	13,154	14,080	14,227
Collections	14,775	15,825	15,455
Disbursements and Support	36,068	35,513	35,666
Distributed to Other Programs	-9,724	-9,645	-9,661
Loan Repayment Programs	-1,259	-2,140	-2,054
Unallocated Reduction per Section 33.50	-	-449	-
Total Expenditures (All Programs)	**$107,712**	**$115,110**	**$124,690**
General Fund	**$69,330**	**$70,969**	**$72,695**

POSITIONS BY PROGRAM

Program	Actual 2003-04	Estimated 2004-05	Proposed 2005-06
Accounting and Reporting	134.3	138.2	138.0
Audits	260.5	272.0	271.5
Personnel/Payroll Services	210.8	235.7	254.0
Information Systems	129.2	134.8	134.5
Collections	203.5	217.2	218.8
Disbursements and Support	95.2	121.2	121.1
Distributed to Other Programs	-	-	-
Loan Repayment Programs	-	-	-
Unallocated Reduction per Section 33.50	-	-	-
Total Positions (All Programs)	**1,033.5**	**1,119.1**	**1,137.9**

ISSUE 1: JANUARY BUDGET CHANGE PROPOSALS

In addition to the 21st Century Project, the Governor's Budget includes the following budget change proposals:

1. $955,000 (GF) to continue and make permanent 14 existing limited-term positions for ongoing workload in the Unclaimed Property Program, under which the state receives unclaimed property and attempts to notify the owners. The property reverts to the state GF if there is no valid ownership claim. The program returns almost $200 million annually to property owners and yields larger amounts of annual GF revenue from property that remains unclaimed and reverts to the state.

2. $350,000 (GF) for additional legal costs to defend lawsuits against the Unclaimed Property Program.

3. Redirection of $575,000 (GF) from Operating Expenses and Equipment (OE&E) to Personal Services to recognize existing higher personnel costs and reduced OE&E costs, primarily for rent.

4. $202,000 (GF) for two 2-year limited term position to review online high school classroom programs as required by Chapter 429, Statutes of 2003 (AB 294, Daucher) beginning July 1, 2005.

5. $174,000 (GF) for 2 positions to collect and account for debts owed to the state under programs operated by the former Technology, Trade and Commerce Agency.

6. $1.685 million (special funds) for the second year of a project to replace the obsolete Apportionment Payment System. Project completion is scheduled for 2006-07, with a cost in that year of $661,000, and ongoing annual costs of $136,000 thereafter. Funding is derived from the various special funds that

the Controller apportions to local governments—for example, the Local Revenue Fund (Realignment, the Motor Vehicle License Fee Account (MVLF), and Trial Court Trust Fund). Control Section 25.50 provides the appropriation authority for this project and establishes the contribution of each fund for 2005-06.

7. $731,000 (special funds and reimbursements) and 4.3 positions (2 permanent redirections and 2.3 one-year limited-term redirections) to continue the implementation of the California Automated Travel Expense Reimbursement System (CalATERS). The Controller's Office estimates that this automated travel claim system for state employees will generate annual savings of $9 million.

8. $167,000 redirection from OE&E to fund 2 positions to monitor, evaluate, and participate in the California Child Support Automation System in order to fulfill the Controller's constitutional duties to oversee state disbursements.

COMMENTS

1. **Salary Savings Should Be Increased.** Salary savings is the amount of salary expense that a department saves when a position is vacant or filled at a lower salary level than the budgeted level. Generally, for established departments and programs, a 5-percent salary savings rate is normal. New positions may have even larger salary savings rates due to the time required to fill them. The Budget Change Proposals (BCPs) and Finance Letters provided by the SCO reflect a 2.4 percent salary savings rate. While recent budget reductions, lower than expected retirements, and other offsetting factors may have caused the department's overall recent salary savings rate to drop below five percent, this does not justify a lower salary savings rate *on a prospective basis*. The SCO should identify the amount of additional savings that would result from increasing the salary savings rate budgeted in BCPs to 5 percent.

2. **Control Section 25.50 May Need Revision.** As noted above, Control Section 25.50 provides funding for the Apportionment Payment System from various special funds that the Controller apportions to local governments. However, it appears that the allocation of almost one-third ($501,000) of the total $1.685 million from the MVLF does not recognize the changes in local government finance that were adopted last year in legislation and by the voters in Proposition 1A. These changes replaced most of the MVLF with property tax revenues allocated by counties. The Department of Finance should address whether revisions are needed to Control Section 25.50 to properly reflect current funding streams.

ISSUE 2: AUGMENTATION FOR THE PROPERTY TAX DEFERRAL PROGRAM

The Governor's Budget includes an augmentation of $4.7 million (GF) to the Senior Citizen's Property Tax Deferral Program, in conjunction with a savings of $40 million from the proposed elimination of the Senior Citizens' Property Tax Assistance Program, These changes are budgeted in Tax Relief--Item 9100—discussed later in this agenda. The SCO administers the deferral program, and the Governor's Budget includes an augmentation of two positions and $100,000 to process 5,000 additional deferral applications. Workload calculations, however, show a need for 5 positions if 5,000 applications are reviewed. The Legislative Analyst's Office (LAO) has not concurred with the DOF/SCO 5,000 applications estimate and has suggested the number of applications will be higher. Responding to this uncertainty, an April Department of Finance Letter requests the adoption of Budget Bill language to allow staffing and funding augmentations in the Property Tax Deferral Program with legislative notification.

Regarding the language request, the LAO recommends (*if* the program expansion is approved) against adoption and instead the Department of Finance should refine the workload request in the May Revision.

COMMENTS

Defer Action to Item 9100. The basic issue of expanding the property tax deferral program will be taken up in Item 9100 later in this agenda. The issue here in the SCO budget essentially is conforming.

ISSUE 3: APRIL FINANCE LETTER REQUEST—LOCAL MANDATE REIMBURSEMENT E-CLAIMS PROJECT

The Department of Finance has made the following augmentation request in an April 1 letter:

> It is requested that Item 0840-001-0001 be increased by $1,215,000 General Fund and 2.0 permanent and 1.0 one-year limited term positions be provided to install a web-based system that enables local governments to enter mandated cost claims directly into the Controller's database via the Internet, using electronic forms and digital signatures. This funding includes $505,000 for ongoing costs and $710,000 for one-time costs. This project will increase the accuracy of mandated cost claims and is expected to result in significant savings and cost avoidances for the state beginning in 2006-07.

According to the BCP submitted by the SCO, the new claims system should result in at least $14.7 million of annual GF (non-Proposition 98) savings due to the disqualification of claims for activities outside of the scope of approved mandates. There also would be an equal additional amount of annual savings within Proposition 98 for K-14 education mandate reimbursements. Furthermore, the new web-based claims system will ensure more accurate and consistent filing of claims, enable the SCO to absorb increasing workload as new mandates are identified each year and simplify the claiming process for local governments. The LAO recommends approval of this request.

ISSUE 4: ADDITIONAL MANDATE CLAIMS AUDITORS COULD YIELD SAVINGS

Background

The State Controller receives nearly 75,000 mandate reimbursement claim forms from local agencies and schools. The SCO conducts "desk" audits to detect costs that are outside the scope of the mandate on approximately 5 percent of the 75,000. This five percent is made up of large dollar and new claims. Existing mandates of moderate or low cost are not desk audited, but do receive a quick arithmetic check and scan for obvious flaws.

The SCO's Division of Audits conducts field audits on a tiny fraction of the 75,000 mandates claims received. Even so, these audits generally identify a large number of errors or over-claims. In 2002-03, SCO's auditors performed 27 audits on $77.5 million of claimed costs, resulting in $54.0 million in audit findings (a 70 percent error rate). In 2003-04, 34 audits were conducted on $50.9 million of claimed costs, resulting in $25.7 million in audit findings (a 51 percent error rate). In the current year, 58 audits have been conducted to date on $176.1 million in claimed costs, with $75.3 million disallowed (a 43 percent error rate).

Additional Auditors Could Be Very Cost-Effective. The Division of Audits currently utilizes 32 positions to conduct mandates audits. Information received from the SCO indicates that additional auditors would result in the identification of more flawed or fraudulent claims. From a cost-benefit perspective, the SCO estimates that 10 additional auditor positions (at a cost of $996,000) will identify unallowable costs at a rate of 45 times the cost of the positions (about $45 million of savings for $1 million of cost). Those disallowed claims will reduce the backlog of mandate claims—now estimated by the LAO to exceed $2.6 billion by 2005-06.

COMMENTS

Savings Should Offset Cost of Auditors and E-Claims Project. The LAO estimates that $62 million will need to be appropriated in the 2005-06 Budget to reimburse local government claims for 2004-05 costs for those mandates that the Governor does not propose to suspend in 2005-06 and that do not pertain to employee rights (The $2.6 billion backlog includes this amount). Under Proposition 1A, valid costs for 2004-05 must be paid for these mandates or the Legislature must suspend or repeal them. However, the $62 million estimate is based on claims and estimates as filed by local governments. The additional auditors would reduce this amount along with reductions to the other portions of the claims backlog.

The total cost of the additional auditors and the April E-Claims Project augmentation is $2.211 million. This would represent an audit recovery of only 3.6 percent against the $62 million that will need to be budgeted for 2004-05 claims. Given that past audits have recovered more than 40 percent, this would seem like an extremely conservative savings assumption for additional auditors (and it recognizes that most of the $45 million of additional audit savings would apply to backlog claims from prior years). Accordingly, it would seem reasonable to add the additional 10 auditors and budget savings of $2.211 million to offset their cost and the E-Claims augmentation discussed in Issue 3.

ISSUE 5: UPDATE ON THE "21ST CENTURY PROJECT"

The Governor's Budget proposes to add $10.4 million ($7.9 million in special funds, $2.5 million in reimbursements) and 29.7 positions in the budget year to continue activities associated with the replacement of the existing employment history, payroll, leave accounting, and position control systems. Appropriation authority for the special fund portion of this amount is provided by Control Section 25.25.

The 21st Century Project will replace the existing legacy systems used for payroll and Human Resources processing and information management. The project uses a Request for Proposal (RFP) procurement approach. The project has a two-phased procurement, the first for the selection of software and the second for a system integrator. The selecting of software independent of a system integrator will ensure competition between contracting software companies and will provide the best product and integration choices with the most value for the State.

A commercial off-the-shelf Human Resources Management System (HRMS) product suite will be selected. It will provide a modern, full featured, integrated administrative function for employment, payroll, position management, benefits administration, timekeeping, leave accounting and management reporting. The HRMS is intended to replace the existing State Controller’s Office HR/Payroll systems. A new statewide HRMS will potentially negate the need for redundant purchases of software packages and maintenance of department specific HR systems in state agencies. The System Integrator will be the prime contractor responsible for integration, coordination, customization, training, installation, conversion, and implementation of the selected software.

Funding Plan. Total 10-year project cost from 2003-04 through 2012-13 is estimated to be $132.2 million. Of this amount, $51.6 million will come from the GF and $22.6 million from redirection within the SCO budget. Because of the state's current budget problems, the GF contribution is back loaded and will not begin until 2006-07. In 2006-07, annual project costs will increase to $20.9 million (excluding redirection, but including $7.4 million from the GF) and will remain at roughly that level for about 3 years and then decline to $7.4 million annually by 2011-12.

Background—Why is a new system needed ?

The SCO is responsible for issuing pay to employees of the State Civil Service, California State University, Judicial Council and judges, and elected officials. To meet its responsibilities, the SCO operates large, complex legacy systems. While there are interfaces between the various systems, they were designed as separate stovepipe applications and thus are not integrated. The problems with existing systems can be summarized as follows:

Current systems lack flexibility. As modifications continue to be made through patches to the systems, the estimates for changes become more complex and more costly.

The core systems are based on outdated technology that is in danger of failure. The existing systems were built in the early 1970s using now-obsolete technology and prior to the needs of collective bargaining.

Lack of needed functionality. California's current systems were designed to meet limited objectives at a time when the State had a much smaller workforce, labor and tax laws were not as complex, collective bargaining did not exist, and management information was not as critical. Some examples of the problems with existing functionality are:

- A bi-weekly payroll system does not exist that can be used for large groups of employees.

- A statewide automated position management system does not exist in state government. The current system requires collection and tracking to occur through manual processes or department-created systems. Position information continues to be submitted on hard copy.

- An automated time and attendance system does not exist to capture time at the employee level. Current functionality is limited to total time worked, and does not maintain daily or hourly time.

- Management information capabilities do not exist that deliver information to the operating managers, nor is there a user-friendly means to extract information for departments to manage their human resources or payroll expenditures.

- Employee self-service features, or virtual human resources, do not exist in the current systems. Such transactions as home address changes, Direct Deposit enrollment, tax changes, and benefit enrollments must be completed on a hard copy, and employees must ask their human resource office for information when it is needed.

- User-friendly functions do not exist in the current legacy systems. The general design of the systems is based on green screen technology, rather than a graphic user interface. The systems do not include any help features or ties to training pages. As a result, use of the systems requires extensive on-the-job and classroom training.

- An electronic workflow capability does not exist. Thus departments/campuses rely on paper to deliver the information needed to the workstations to enter into the SCO legacy systems.

Current Status

- The SCO has tentatively awarded the software contract to SAP. However, the other bidder (Lawson) has indicated that it will protest the award. The SCO should inform the subcommittee of the status of this protest.

- The award of the Independent Verification and Validation (IV&V) contract is currently underway.

- The Request for Proposals for the System Integrator is scheduled for release on June 15, 2005.

ITEM 0890 SECRETARY OF STATE

The Secretary of State (SOS), a constitutionally established office, has statutory responsibility for managing the filing of 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 archives.

The budget proposes total expenditures of $76.4 million for the SOS in 2005-06. The two primary ongoing sources of funding are the General Fund ($30.3 million) and the Business Fees Fund ($33.3 million). In addition, the current-year budget contains over $265 million in federal funds for the implementation of the Help America Vote Act of 2002 (HAVA).

ISSUE 1: ELECTION MANDATES

The Governor’s 2005-06 budget is proposing to suspend seven election related mandates for a total expected savings of $16.5 million dollars. While according to local county election officials the suspension of these mandate with create general fund savings, accrued liabilities from past-year claims from these mandates is nearly $41 million. Under the Governor's proposal (embodied in ACA 4x [Keene]), these accrued liabilities would be paid back over 15 years. The following are the seven mandates that are proposed for suspension:

- **Voter Registration Procedures (Chapter 704, Statutes of 1975 [AB 822, Keysor]).** This mandate reimburses counties for the net costs associated with a number of changes made to voter registration procedures in 1975.

- **Absentee Ballots (Chapter 77, Statutes of 1978 [AB 1699, Lehman]).** This mandate specifies that all voters are eligible to receive an absentee ballot. Under prior law, only those voters who met certain conditions (illness, disability, absence from precinct,etc.) were eligible to vote by absentee ballot.

- **Handicapped Voter Access Information (Chapter 494, Statutes of 1979 [AB 745, Moore]).** This mandate requires that disabled voters have access to all polling locations. Subsequent to mandate's passage, federal law has imposed more extensive requirements in this area. With the requirements of federal law in place, this mandate has been suspended in recent years.

- **Permanent Absentee Ballots (Chapter 1422, Statutes of 1982 [AB 350, Agnos]).** This mandate requires counties to allow disabled voters to request status as a permanent absentee voter, so that they do not need to apply for an absentee ballot for each election. Chapter 922, Statutes of 2001 (AB 1520, Shelley), extends this requirement to all absentee voters. In September 2003, a county filed with the CSM to begin the process of determining whether Chapter 922 is a reimbursable state mandate. (Legislative analyses at the time of Chapter 922's passage assumed the requirements would be a state reimbursable mandate.)

- **Brendon Maguire Act (Chapter 391, Statutes of 1988 [AB 2582, Duplissea]).** This mandate specifies the election procedures when a candidate dies within three months of the general election. In those rare instances when the provisions of Chapter 391 apply, the state is responsible for reimbursing local governments for the costs of a special election.

- **Presidential Primaries (Chapter 18, Statutes of 1999 [SB 100, Burton]).** Chapter 18 placed new reporting requirements on county election officials for the March 2000 statewide primary election. At that time, Proposition 198's open primary system was in effect—allowing voters from any party to vote in a party's primary. The by-laws of the major political parties, however, only allow registered party voters to determine delegates to their national conventions. In order to allow for the determination of party delegates consistent with these by-laws, Chapter 18 requires counties to report primary election results by voters' party affiliations. Since the passage of Chapter 18, Proposition 198's system was found unconstitutional by the U.S. Supreme Court. Consequently, the requirements of Chapter 18 will not mandate any reporting activities for future primary elections. The mandate's $1.5 million in costs to date are one-time in nature.

- **Absentee Ballots—Tabulation by Precinct (Chapter 697, Statutes of 1999 [AB 1530, Longville]).** Chapter 697 placed new reporting requirements on county election officials for the November 2000 statewide election. In order to assist the Legislature in making redistricting decisions, counties were required to report absentee voting returns by precinct. Typically, counties have been able to report absentee voting as a lump-sum total. Chapter 697 added this requirement for the November 2000 election only. In addition, under Chapter 697, counties are now required to maintain precinct information for each absentee voter on an ongoing basis. Of the $216,000 in reported costs to date, about $7,000 is estimated to be an annual ongoing expense (for counties to maintain their absentee voter precinct information).

Background. The election related mandates listed above are state requirements of county election officials related to election procedures that have been determined to be reimbursable state mandates. In recent budgets, most of these mandates have been "deferred"—meaning that the requirements have remained in effect and the state is still accruing liabilities for counties' compliance with the mandates, but no reimbursements to counties have been made. In addition, over the past year, the Commission on State Mandates (CSM) has determined that there are two additional election-related reimbursable mandates—related to presidential primaries and tabulating absentee ballot results by precinct.

Under the provisions of Proposition 1A passed by the voters in November 2004, the state is no longer able to defer the costs of mandates. Instead, for each mandate the state is either obligated to provide full funding in the budget or "suspend" its requirements during 2005-06. For each of the seven election-related mandates, the Governor's budget proposes to suspend their operation in the budget year.

LAO Comments. The LAO has expressed concern that aside from potential savings, the administration has not provided the Legislature any policy rationale for the suspension of the mandates. By suspending the mandates, the requirements under state law become optional for local governments. In the context of these mandates, the LAO argues for instance, that each county could decide whether to offer absentee ballots to voters who did not meet the pre-1978 criteria of being disabled or ill. Without a stated policy rationale, it is unknown whether the administration, through the suspensions, hopes to encourage election-related changes—such as a move away from uniform state laws to a more county-based system or a reduction in the use of absentee ballots.

In order to address the various concerns that have been raised, the LAO has recommended that the Legislature repeal two election mandates and fully fund the remaining five mandates. Along with funding, the LAO has also recommended that the Legislature initiate a process to review and reform specific mandates. The following are the LAO recommendations:

1. The Legislature should repeal the handicapped voter access information and presidential primaries mandates. As noted above, federal law now generally provides greater protections and rights for disabled voters than that of the handicapped voter access information mandate. For this reason, the mandate has been long been suspended. Likewise, for the presidential primary mandate,

since Proposition 198 is no longer in effect, the y mandate no longer places any meaningful requirements on counties. Repealing both mandates would not affect election procedures.

2. The Legislature should fully fund the Brendon Maguire Act and the absentee ballot—tabulation by precinct mandates. This recommendation would require a total appropriation of $8,000—$1,000 for the Brendon Maguire Act (since no costs are expected) and $7,000 for the tabulation mandate.

3. In order to maintain statewide uniformity in election procedures, the Legislature should reject the Governor's proposal to suspend three mandates - voter registration procedures, absentee ballots, and permanent absentee ballots.

   In their review of a sample of recent local government claims for absentee ballot mandates, the LAO found the following problems identified with claims: a wide variation of costs; high overhead charges; and some costs appear disallowable. In addition, the interaction of various state requirements makes it difficult to properly claim the appropriate amounts of reimbursements. Subsequently, the LAO also recommends that the legislature convene a working group with the SCO to determine a new reimbursement methodology.

ISSUE 2: ADDITIONAL BUDGET CHANGE PROPOSALS

The following are additional BCPs for the office of the Secretary of State. Staff had no issues with proposals and recommends approval.

Advance Health Care Directives: Registry Assembly Bill 2445, Chapter 882, Statutes of 2004. The SOS requests a budget augmentation from t he Business Fees Fund (BFF) for $37,000 and authorization to permanently establish a half time Program Technician II position beginning in Fiscal Year 2005-06 to meet statutory requirements set forth in Assembly Bill 2445.

Business Programs Administration. The SOS requests final funding of $2.4 million from the BFF to complete the development and implementation of the Business Programs Automations Project (BPA). BPA is a multi year project to develop and implement an integrated document management system and replace the legacy systems for Uniform Commercial Code transactions and Business Entities filings.

Special Items of Expense to Conduct Statewide Elections. SOS requests to augment the current appropriation for special items of expense by $3.0 million to provide funding for statewide election costs. In prior years, annual statewide election costs that were greater than appropriated funds were provided through the deficiency process, however with the deletion of Control Section 27.00, the deficiency process was eliminated.

ITEM 0650 OFFICE OF PLANNING AND RESEARCH

The Office of Planning and Research (OPR) assists the Governor and the Administration in planning, research, and liaison with local government. OPR also oversees programs for small business advocacy, rural policy, environmental justice, and helps implement decisions made within the Administration. In addition, the Office has responsibilities pertaining to state planning, California Environmental Quality Act (CEQA) assistance, environmental and federal project review procedures, and oversees the California Service Corps.

ISSUE 1: GUIDELINES FOR TRIBAL CONSULTATIONS

In the 2005-06 budget, the Governor proposed to increase OPR's budget by $390,000 to handle additional workload created by the passage of SB 18 (Burton, Chapter 905, Statutes of 2004) which requires OPR to develop and publish guidelines for local governments to consult with Native American tribes on land use planning matters. This proposal will allow OPR to comply with the new mandate by adding one senior level professional planner plus outside consultants.

April 1 Finance Letter. In an April 1 Finance letter, the funding levels for this proposal were reduced by $202,000. This revision in funding level is the result of lower than expected outside costs and OPR's ability to shift internal resources.

ISSUE 2 SMALL BUSINESS ADVOCATE POSITION

AB 505 (Wright, Chapter Statutes of 2000) established the Small Business Advocate Position within OPR to act as a conduit between California's small business community. Since its establishment in statute, the Small Business Advocate Position, except for a brief period in 2002, has remained vacant within OPR. Though the position was established in statue, no additional funding was ever provided to OPR. Instead, it was expected that the position be filled with OPR's existing resources.

Staff Comments: When the Small Business Advocate Position was established, it was intended to provide a valuable link between the small business community and administration. Originally it was this intent for "access" to the administration that placed the position in OPR. Since its inception however, it has been difficult for the legislature to track the progress of filling the position and how well the position is serving the small business community.

Since the dismantling of the Technology Trade and Commerce Agency, the Business Transportation and Housing Agency has taken the lead role in the running of our state's economic development programs. Upon its formation, the Small Business Advocate position was intended to coordinate with the state's diverse net of economic development programs and serve as a conduit between those programs, their recipients and the administration. However, because this position has not been filled consistently, the state has been unable to take advantage of these opportunities.

The subcommittee may wish to consider relocating this position to the Office of the Secretary of BTH to better take advantage of the agency's cumulative experience with economic development programs.

ITEM 1110-1111 DEPARTMENT OF CONSUMER AFFAIRS

The Department of Consumer Affairs is responsible for promoting and protecting the interests of millions of California consumers by serving as a guardian and advocate for their health, safety, privacy, and economic well-being and by promoting legal and ethical standards of professional conduct. The Department helps to promote good business practices and to ensure that California's consumers receive quality services by establishing minimal competency standards for more than 230 professions involving approximately 2.3 million professionals. The Department is also an important advocate on consumer and business issues.

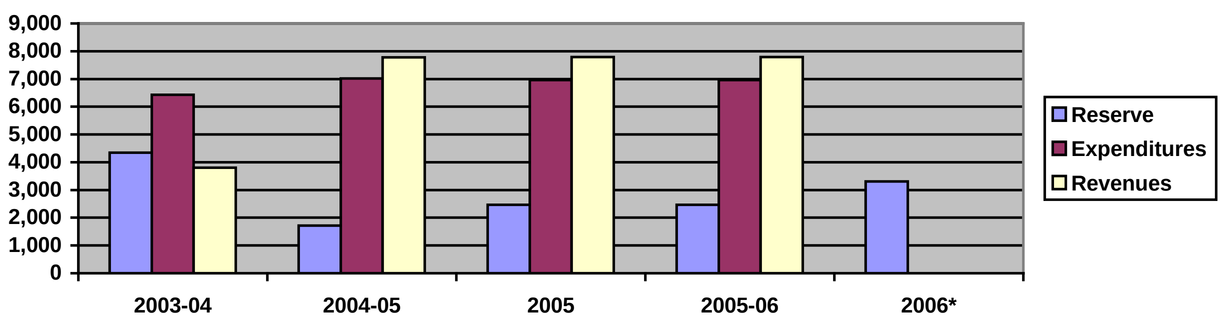
ISSUE 1: BUREAU OF SECURITY AND INVESTIGATIVE SERVICES

The Bureau of Security and Investigative Services ensures that only those who meet the prescribed qualifications to offer services as private investigators, repossessors, uniformed security guards, private patrol operators, alarm company operators, alarm agents, locksmiths, and firearm and baton training facilities be licensed and enforces the regulations established by legislation for such licenses.

Private Security Services Fund Balance

The Private Security Services Fund is the primary fund to support operations of the Bureau of Security and Investigative Services. Since 2004, reserves in the fund have been growing at a disproportionate rate to expenditures, resulting in an increase in reserves of $1.6 million. The graph below shows the expected growth of the reserve from 2004-2006.

Private Security Services Fund
Dollars in thousands



*expected reserve for 2006.

COMMENTS

Chapter 886 – Statutes of 2002 (AB 2880-Chavez) requires that registered security guards complete a total of, depending on their classification, 32-40 hours of training within 30 days of the day their registration card is issued by the bureau. In prior subcommittee hearings, concern has been raised that the Bureau is not devoting adequate resources to ensure that security companies and their security officers are meeting the new standards set forth in statute. The Bureau has responded that it has been able to accommodate the increased workload using additional staff and savings accrued through an increase in online registration processes.

Currently there is a $3.3 million reserve in the Private Security Services Fund and the subcommittee may wish to utilize the increasing reserve to address possible funding shortfalls currently present in the Bureau.

ITEM 8885 COMMISSION ON SATE MANDATES

The Commission on State Mandates (CSM) is a quasi-judicial body that makes the initial determination of state mandated costs. The Commission is tasked to fairly and impartially determine if local agencies and school districts are entitled to reimbursement for increased costs mandated by the state. The total proposed budget expenditures for the Commission on State Mandates are $1.6 million, all of which is state GF.

Governor's Budget
Commission on State Mandates
(dollars in thousands)

Program	Actual 2003-04*	Estimated 2004-05*	Proposed 2005-06*
Administration	$1,211	$1,218	$1,658
Unallocated Reduction	-	-	-29
Total Expenditures	**$1,211**	**$1,218**	**$1,629**
Positions	**9.7**	**9.7**	**13.6**

ISSUE 1: MANDATE IDENTIFICATION LANGUAGE

The Administration proposes trailer bill language to add an option to identify a suspended mandate by CSM test claim number, in addition to executive order or statute. This technical fix will reduce ambiguity regarding the actual suspended mandate. The language also has been introduced as AB 1467 (Laird).

ISSUE 2: STAFFING TO ADDRESS CLAIMS BACKLOG

The Commission on State Mandates has a backlog of mandate test claims that must be processed to determine whether the mandate requires State reimbursement. The Budget requests $427,000 GF and 4 positions (one permanent and three 3-year limited-term) to assist in processing this workload. The commission indicates that this augmentation will enable it to eliminate its backlog in three years.

No concerns have been raised regarding this request.

ITEM 9100 TAX RELIEF

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. These are distinct from "tax expenditures," such as tax deductions, exemptions, and credits, which reduce tax liability. Some of the tax relief expenditures in this item, however, are amounts paid to local governments to offset some or all of their revenue loss due to a tax expenditure. The budget proposes total 2005-06 tax relief expenditures to be $539.4 million, as shown in the table below:

Program	Actual 2003-04*	Estimated 2004-05	Proposed 2005-06
Senior Citizens' Property Tax Assistance	$39,062	$40,494	$-----
Senior Citizens' Property Tax Deferral Program	11,714	11,900	16,600
Senior Citizen Renters' Tax Assistance	143,702	142,636	42,507
Homeowners' Property Tax Relief	424,786	433,200	440,000
Subventions for Open Space	38,425	39,388	39,661
Substandard Housing	44	-	-
Motor Vehicle License Fee Relief	3,124,764	-	-
State-Mandated Local Programs	-	-	658
Total Expenditures (All Programs)	**$3,782,497**	**$667,618**	**$539,426**

Property Tax Swap Replaced Vehicle License Fee (VLF) Backfill. Prior to the current year, the State provided VLF "backfill" revenue to local governments. The backfill made local governments whole for their revenue loss due to the reduction in the VLF tax rate paid by vehicle owners. The Local Government Agreement adopted as part of the 2004-05 budget replaced the backfill with a shift of property tax revenues from K-14 education to cities and counties. The State, however, continues to bear the cost of the backfill (less $700 million in 2004-05 and in 2005-06) by offsetting the reduced property tax revenue to K-14 education with increased GF support.

Homeowners' Exemption. The largest tax relief program currently in the budget is the homeowners' exemption ($440 million proposed for 2005-06). This program, which was established 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. In order to accommodate the expected growth in the number of homeowners claiming the exemption, the Governor's budget proposes an increase of $6.8 million, or 1.6 percent, over the amount estimated for 2004-05.

Senior Citizens' and Disabled Persons' Tax Assistance and Deferral. This program provides once-a-year financial assistance to offset a portion of the property tax burden of low-income seniors and disabled persons who either own a home or rent a dwelling in California. In the deferral program, the state pays a homeowner's property tax and is repaid out of eventual sale proceeds. These programs are discussed in more detail in Issue 1.

Open-Space Subventions. The budget proposes a General Fund appropriation of $39.7 million for subventions that partially reimburse local governments (primarily counties) for property tax losses under Williamson Act Open Space contracts. The Williamson Act allows cities and counties to enter into contracts with landowners to restrict their property to open space and agricultural use. In return for the restriction, the property owner pays reduced property taxes because the land is assessed at lower than the maximum level. The amount of the state subvention to localities is based on the acreage and classification of land under contract, rather than the actual reduction in local property tax revenues.

The contracts entered into between local governments and property owners are rolling ten-year contracts (20 years in a Farmland Security Zone) that are typically renewed each year for an additional year. In the event the contract is not renewed, the tax on the property gradually returns over a ten-year period to the level at which comparable, but unrestricted, land is taxed.

Williamson Act contracts exist in 52 counties and seven cities and cover more than 16.3 million acres of land. Subventions range from $1 per acre for nonprime agricultural land outside of a Farmland Security Zone to $8 per acre for land within three miles of a city's sphere of influence in a Farmland Security Zone. The counties receiving the largest amount of subventions are Fresno and Kern (more than $5 million each). The state also spends an amount roughly equal to the subventions in order to backfill property tax losses to K-14 education due to the reduced assessments under open-space contracts.

Substandard Housing Subventions Ended. Existing state tax laws deny taxpayers deductions associated with rental income from substandard housing. Formerly, the revenue from the denied deductions was allocated to local governments for the enforcement of housing codes and rehabilitation. The amount allocated had been very small—only $44,000 in 2002-03 and 2003-04. The program was ended in the 2004-05 Budget.

ISSUE 1: SENIOR CITIZENS' PROPERTY TAX AND RENTERS' TAX ASSISTANCE

Background. These programs provide cash payments to low-income homeowners and renters who are either senior citizens (age 62 and older), disabled, or blind. The payments are intended to partially offset property taxes paid directly by qualifying homeowners or paid indirectly (in rent) by qualifying renters. The assistance provided is inversely related to the amount of total household income. The maximum assistance payments (for households with incomes less than $9,626) are $472.60 for homeowners and $347.50 for renters and the minimum payment is $20.40 for homeowners or $15.00 for renters at the current household income limit of $38,505. Households above the maximum income limit do not qualify for any assistance. The income limits are adjusted annually by the change in the California Consumer Price Index. The Franchise Tax Board (FTB) administers this program. Eligible seniors and disabled persons file claims annually with the board between July 1 and October 15.

According to the Legislative Analyst's Office, there were 156,000 claimants for property tax assistance and 494,000 claimants for renters' assistance in 2003-04. Data from the FTB indicate that about one-third of the renters' tax assistance is paid to disabled claimants. Senior claimants (who also may be disabled) comprise about 98 percent of the claimants for homeowners' tax assistance.

Annual General Fund budget appropriations finance this program. For 2005-06, the Governor's budget proposes to reduce funding by $140.6 million for the Senior Citizens' Property Tax and Renters' Tax Assistance, as shown below:

(in thousands)	**2003-04**	**2004-05**	**2005-06**	**Change in 2005-06**
Senior Homeowners' Property Tax Assistance	$39,062	$40,494	—	-$40,494
Senior Renters' Tax Assistance	143,702	142,636	42,507	-$100,129
Totals	$182,764	$183,130	$42,507	-$140,623

Property Tax Deferral Program. Under the deferral program, qualifying seniors (age 62 or older) or disabled homeowners may opt to have the state pay the property tax bill (including debt levies and special assessments) for their home. The state places a lien on the property for the deferred amounts plus interest and is repaid when the home is sold (after the owner's death, for example). To qualify for the deferral program, seniors or disabled persons must have a household income of no more than $24,000 ($34,000 for those who already were participants in 1983-84). Also, the homeowner must have at least 20 percent equity in the home. The State Controller administers this program.

Governor's Budget Proposals

Elimination of Senior Homeowners' Assistance. The Governor's budget proposes legislation to terminate the Senior Homeowners' Property Tax Assistance Program for a savings of $40.5 million in fiscal year 2005-06. This savings would be ongoing, but would be partly offset by an augmentation of $4.7 million for the Senior Citizens' Property Tax Deferral Program.

Expansion of Senior Property Tax Deferral Program. The augmentation reflects the Administration's proposal to expand income eligibility under the deferral program to the income level used by the homeowners' assistance program, so that all individuals who currently qualify for the assistance program would qualify for the deferral program. The budget states that for most individuals, the deferral program will provide more financial assistance than the property tax assistance program. This proposal implements one of the recommendations of the California Performance Review. The budget proposal would increase the household income limit for the deferral program to the same amount currently applicable to the assistance program ($38,505 in 2004, with annual adjustments for inflation).

Scale-Back of Senior Renters' Assistance Program. The Governor's budget proposes $100.1 million of savings by reducing the benefit and eligibility levels to what they were in 1998, when the income limit was $13,200 and the maximum amount of benefit was $240 (versus $347.50 in 2004). Unlike the homeowners' proposal, the budget does not include any other program expansion to offset any portion of this reduction. However, senior and disabled renters who have enough income to have a state income tax liability would continue to be eligible to claim the Renters' Credit on their income tax return. The Renters' Credit is $60 (single) or $120 (married) and is available to renters with incomes up to about $30,000 (single) or $60,000 (married). However, many low-income seniors and disabled persons have no state income tax liability or too little liability to obtain the full benefit of the Renters' Credit.

COMMENTS

Additional Hit to SSI/SSP Recipients. SSI/SSP beneficiaries generally qualify for the current senior renters' or homeowners' assistance payments. The budget proposes to eliminate both the state and federal cost-of-living adjustments (COLAs) to SSI/SSP grants. Consequently, the proposed reductions in homeowners and renters assistance will result in an overall reduction in total income to SSI/SSP beneficiaries who have no other sources of support.

Renters' Tax Credit Not Much Help to Recipients of Renters' Assistance. Senior and disabled renters who have enough income to have a state income tax liability would continue to be eligible to claim the Renters' Tax Credit on their income tax return. The Renters' Tax Credit is $60 (single) or $120 (married) and is available to renters with incomes up to about $30,000 (single) or $60,000 (married). However, the majority of low-income seniors and disabled persons who qualify for the assistance program have no state income tax liability or too little liability to obtain the full benefit of the Renters' Credit. An elderly married couple, for example, is not even required to file a California tax return until their adjusted gross income is at least $28,865. In any case, the budget proposes no offsetting expansion of the tax credit program.

Expansion of the Deferral Program is a Poor Trade-Off. Essentially, the budget proposes to trade off ending the homeowners' assistance program for an expansion of the property tax deferral program. This raises the following issues:

- **No help for the poorest**. Senior and disabled homeowners with incomes under $24,000 (or $34,000 in some cases) currently qualify for both the assistance and deferral programs (the assistance payments reduce the amount of the lien). For these homeowners, the budget proposal represents only a loss.

- **Larger immediate benefit for some.** The expanded deferral program may offer a larger amount of immediate financial assistance than the assistance program currently provides to recipients with incomes over $24,000. At that income level the assistance program provides only about $122 (equivalent to the 1-percent property tax on $12,200 of assessed value), and this amount declines further as income increases. For homes assessed at $19,200 ($12,200 plus the $7,000 homeowners' exemption) or more, the deferral program offers a larger immediate benefit (plus it covers debt levies and special assessments).

- **Loan versus grant.** The downside to the deferral program to the participants, of course, is that it is a loan rather than a grant. Deferrals reduce the amount that the homeowner can borrow with a mortgage and they reduce the value of the property to heirs. Furthermore, individuals who have less than 20 percent equity in their home do not qualify for the deferral program.

Homeowners' Assistance Savings Could Turn into A Cost. The LAO questions whether the $4.7 million budgeted for expansion of the deferral program includes the cost of greater participation in the deferral program if the assistance program is eliminated. According to LAO, costs would increase by $10 million if just 5 percent of the current recipients of homeowners' assistance decided to participate in the deferral program. In fact, since the up-front benefit of the deferral program often is significantly greater than the current amount of the assistance payment, any state savings over the immediate future depend on a low participation rate in the deferral program. If participation is high, the budgeted savings could turn into an additional cost.

ISSUE 2: COUNTY AUDITOR REDEVELOPMENT REPORT MANDATE

Background. State law requires redevelopment agencies to deposit 20 percent of their tax increment revenues into Low and Moderate Income Housing Funds and use these monies to develop affordable housing. In 1997, the Legislature's Task Force on Redevelopment Agencies' Affordable Housing Reports concluded that it was difficult for private and public agencies to monitor redevelopment agency compliance with this state law because data regarding tax increment revenues were not readily available. To address this problem, the Legislature enacted Chapter 39, Statutes of 1998 (SB 258, Kopp), requiring county auditors to prepare annual tax disbursement statements for each redevelopment agency project area.

In November 2002, the Commission on State Mandates determined that county auditor work to prepare these tax statements is a state-reimbursable mandate and estimated the statewide cost of this mandate to be $65,300 (for costs through 2004-05).

Budget Proposes Suspension. The Governor's Budget proposes to suspend this mandate in 2005-06 and to defer any funding for costs incurred through 2004-05.

LAO Recommends Repeal. The LAO points out that the SCO annually publishes detailed reports on the financial transactions of redevelopment agencies, including all information that Chapter 39 requires county auditors to report. In addition, state laws require redevelopment agencies to obtain independent annual audits that (1) detail all financial transactions and (2) include an auditor's opinion of the agency's compliance with applicable state laws and regulations. While this audit requirement existed in 1997, guidelines for preparing these audits have been clarified and expanded in recent years.

Because of the availability of these alternative sources of data, LAO finds that this mandate has become redundant. LAO notes, for example, that the state agency responsible for monitoring redevelopment agency housing law compliance (the Department of Housing and Community Development) does not use these county auditor reports. Accordingly, LAO recommends repeal of this mandate.

COMMENTS

Both the Department of Finance and LAO agree that this mandate need not be in effect in 2005-06. The difference is repeal versus a one-year suspension (that might be extended annually). In the event that the mandate is not suspended in a future year, county auditors would have to reinstate the production of these reports as well as cost-tracking for eventual reimbursement. Also, suspension leaves the report requirement in statute causing potential confusion. Repeal may be preferable.

The state's obligation to pay costs incurred through 2004-05 will remain in either case.

ITEM 9210 LOCAL GOVERNMENT FINANCING

This item includes a number of subvention and grant programs for local governments. The state also provides other funding to local governments, primarily counties, through other items in the budget. For example, many Health and Human Services programs provide substantial funding to counties. State funding is also included in Public Safety for such issues as local crime labs and suppression of high intensity drug trafficking areas. The Local Government Financing item presented here proposes $157.4 million of spending in 2005-06, all of which is from the General Fund.

Governor's Budget
Proposed Expenditures by Program
Local Government Financing
(in thousands)

Program	Actual 2003-04*	Estimated 2004-05*	Proposed 2005-06*
Property Tax Administration Grant Program	$60,000	$60,000	$54,334
Booking Fee Subventions[a]	38,220	38,220	--
Small and Rural Sheriffs Grants	--	18,500	--
Disaster Property Tax Replacement[b]	--	1,451	--
Santa Barbara County Formation Loan[b]	--	400	--
Citizens' Option for Public Safety (COPS) and Juvenile Justice Grants (excluding 2005-06)	199,725	199,725	100,000
Special Supplemental Subventions	477	650	650
State-Mandated Local Programs	3	5	2,408
Total Expenditures (All Programs)	**$297,596**	**$318,946**	**$157,392**

[a] 2004-05 budget trailer legislation ends this subvention program after 2004-05.
[b] One-time expenditure.

Note: The COPS and Juvenile Justice programs will be heard at the next hearing on April 27th.

ISSUE 1: PROPERTY TAX ADMINISTRATION GRANT PROGRAM

The Governor's Budget proposes a reduction of $5.7 million in grants to counties for the Property Tax Administration Program (PTAP). This program had previously been funded at $60 million. These grants provide additional funding to assist county assessors to process reassessments of property due to sales or new construction, resulting in additional property tax revenue for local governments and K-14 Education (offsetting the state's Proposition 98 funding requirement). A key component of the program is a maintenance of effort requirement for counties to keep assessors funding and staffing at least at the 1994-95 level to be eligible to receive PTAP funds.

COMMENTS

The Governor's Budget assumes that there will be no reduction in property tax revenues (resulting in an increase in state school funding) due to the reduction in the grant program. Material submitted by local agencies suggests that the funding reduction is exceeded by the revenues generated for education funding. The Los Angeles County assessor, for example indicates the program yields $6.50 for schools for every $1 in PTAP funding. Last year's Local Government Agreement shifted some property tax revenue from education back to local governments, which may increase the financial incentives for counties to fund assessment activities. However, schools still receive a substantial portion of property tax revenues.

Anecdotal accounts indicate that the recent rapid increase in home prices and sales, as well as construction and remodeling activity, have left assessors with a backlog of reassessments.

- The Department of Finance and the LAO should comment on the impact of the proposed funding reduction on property tax revenues for K-14 Education.

MANDATES

The table on the next page, prepared by the LAO summarizes the budget's proposal for the nine mandates under this item. For 2005-06, the administration proposes to (1) fund three of the mandates ($2.4 million) and (2) "suspend" the six other mandates. (When the state suspends a mandate for a fiscal year, it incurs no reimbursement liability for that year, and local governments are not required to provide the mandated services.)

State Mandates Under Item 9210

(Dollars in Thousands)

Mandate	LAO Estimates[a] 2004-05[b]	LAO Estimates[a] 2005-06	Budgeted 2005-06	LAO Recommendation
Open Meetings Act/ Brown Act Reform	$15,447	$15,910	$2,000	Withhold, pending proposal from administration.
Health Benefits for Survivors of Peace Officers and Firefighters	347	357	221	Fully fund at $703. Make future benefits subject to collective bargaining.
Rape Victim Counseling Center Notices	281	289	187	Delete funding. Modify to make requirement statement of legislative intent.
Photographic Record of Evidence	505	523	Suspend	Repeal mandate. If necessary, expand court authority.
Mandate Reimbursement Process	—[c]	—[c]	Suspend	Withhold, pending proposal.
CPR Pocket Masks	—[c]	—[c]	Suspend	Modify to make requirement statement of legislative intent.
Domestic Violence Information	—[c]	—[c]	Suspend	Modify to make requirement statement of legislative intent.
Filipino Employee Surveys	—[c]	—[c]	Suspend	Modify to make requirement statement of legislative intent.
Lis Pendens[d]	—[c]	—[c]	Suspend	Modify to make requirement statement of legislative intent.

a Based on existing law and claiming practices.

b Proposition 1A specifies that funding for a mandate's 2004-05 costs must be appropriated to continue a mandate in 2005-06.

c Costs unknown because mandate has been suspended for more than a decade.

d The administration indicates it will propose adding this mandate to the budget bill.

ISSUE 2: OPEN MEETINGS ACT MANDATE

The Governor's Budget proposes to restructure the Open Meetings mandate and provide $2 million in 2005-06 funding, a funding level significantly below the $15 million expense expected in the current year. The Department of Finance indicates that it will propose a statutory change to narrow the scope of the mandate to printing costs and postage (approximately $2 million).

LAO Suggests Making Mandate Optional: In 1953, the Legislature enacted the Brown Act, declaring, "all meetings of the legislative body of a local agency shall be open and public, and all persons shall be permitted to attend any meeting of the legislative body." Because the Brown Act preceded the 1975 operative date of mandate law, its requirements are *not* a state-reimbursable mandate. Instead, the Open Meeting Act "mandate" pertains to certain post-1975 procedural amendments to the Brown Act, most notably the requirement that local agencies prepare and post agendas 72 hours before a hearing (Chapter 641, Statutes of 1986 [AB 2674, Connelly]).

California residents have shown longstanding interest in open hearings, and the state's voters recently enacted Proposition 59, amending the State Constitution to specify that meetings of public bodies and writings of public officials must be open to public scrutiny. Accordingly, legislative action to eliminate (or make optional) the *procedural elements* of the Open Meeting Act mandate would not likely reduce people's ability to monitor local agency actions.

Accordingly, when considering the Administration's Open Meeting Act mandate proposal, LAO recommends that the Legislature consider, as an alternative, making the Open Meeting Act mandate optional (the Brown Act would still be in force). This alternative would eliminate all future state reimbursable costs for this mandate, as well as the requirement that the Legislature include funding for the mandate's 2004-05 costs in the 2005-06 Budget.

COMMENTS

Proposition 1A Funding Requirement. Under Proposition 1A, the state must provide funding for processed 2004-05 reimbursement claims if the mandate is not suspended or repealed (or made optional). To keep the mandate in force, therefore would require increasing the appropriation to around $15 million. Proposition 1A does not require funding of budget-year costs in order to avoid suspension or repeal.

ISSUE 3: PHOTOGRAPHIC RECORDS OF EVIDENCE MANDATE

This mandate requires local law enforcement agencies to provide photographs, chemical analyses, and other substitutes for evidence that a court determines poses a health, safety, security, or storage problem. In their mandate claims, local agencies typically request reimbursement for purchases of high-tech digital imaging and printing equipment. The Administration proposes to suspend this mandate in the budget year.

LAO Concerns: The responsibility for managing evidence used in the courts should rest with law enforcement agencies. The Administration's proposal to suspend this mandate in the budget bill, however, raises two concerns. It could:

- **Suspension Adds Ambiguity to the Laws of Evidence.** As was discussed in *An Assessment: Governor's Local Government Proposal* (May 2004)**,** when a mandate is suspended, the suspension applies only to the sections of law (or laws) found to be a mandate by the Commission on State Mandates (CSM). All other provisions in the statute continue to have the force of law, but interpreting these remaining provisions (which may refer to the suspended provisions) can become very difficult. Because the Photographic Record of Evidence mandate pertains to an area of law where ambiguity could have serious consequences, LAO recommends that the Legislature carefully craft permanent changes to the mandate's underlying statute, rather than using the suspension process.

- **Suspension May Increase Court Costs.** In 1985, court concerns regarding evidence storage and handling costs prompted passage of the subject legislation. At the time this analysis was prepared, we were not able to determine whether courts currently have sufficient authority—independent of this mandate legislation—to require local agencies to submit substitute evidence. If this mandate's suspension were to result in local agencies submitting some evidence for which they currently provide substitutes, courts could experience increased storage and handling costs.

COMMENTS

It is unclear, at this point, that the Administration has evaluated the offsetting expenses to the savings posed by suspending the Photographic Records of Evidence mandate.

Given the uncertainties concerning the effect of this proposal, the subcommittee may wish to hold this issue open and provide the following direction:

A. Direct the Department of Finance and LAO to report back at the next hearing on the potential cost savings relative to additional burdens on the court system from suspending or repealing this mandate.

B. Direct LAO to work with Legislative Counsel and the CSM to prepare trailer bill language to repeal the Photographic Records of Evidence mandate and, if necessary, enact provisions clarifying or expanding courts' authority to require substitute evidence.

ISSUE 4: MANDATE REIMBURSEMENT PROCESS

This mandate reimburses local agencies for their administrative costs to file mandate test claims and reimbursement claims. The reimbursement claims for this mandate totaled $17 million in 2002-03, of which $6.7 million was from local governments and the remainder from schools and community colleges. Most of the local government costs are for submitting ongoing mandate claims (as opposed to initial test claims).

LAO Comments: Typically, local agencies request reimbursement for their costs to (1) contract with mandate consulting firms and (2) oversee their consultants' contracts. The administration proposes to suspend this mandate in 2005-06. As a result, local agency actions to file test claims or reimbursement claims would be "optional." That is, local agencies would not be required to follow the mandate reimbursement process. However, by not following the process, local agencies would not receive state reimbursements of mandated local costs (as promised under the State Constitution).

Problems with the current reimbursement process mandate:

It's expensive. Many local agencies' claims for their administrative filing costs equal or exceed 15 percent of their total claims. In large part, local agencies face little incentive to minimize mandate claim preparation or test claim filing costs. Instead, local agencies hire firms that specialize in the arcane mandate process and advertise that they can "maximize" local revenues from state reimbursements.

No Incentive to Find Efficiencies. The existence of this reimbursable mandate reduces local agencies' (and their consultants') incentive to work with the state to develop an alternative, simpler mandate claiming system.

LAO Recommendation. Despite these shortcomings, LAO does not concur with the administration's proposal to suspend this mandate because LAO views suspension as unfair and possibly unconstitutional. Instead, LAO suggests that the administration suggest an alternative method of addressing these costs. The Legislature could assist in this by directing the administration, local agencies, and legislative staff to work together this spring to develop a new and simpler system for reviewing test claims and providing mandate reimbursements.

COMMENTS

A suspension would suspend the operation of all current mandate filing requirements during 2005-06. This would create a chaotic situation in which there might be no rules for mandate claims. The DOF should explain how local agencies will be able to submit claims under this suspension and how statutes requiring filings within one year will be affected by the proposed suspension.

Is This Really a Mandate? Under the California Constitution, local governments have a right to state reimbursement for the cost of "new program or higher level of service" required by the state. However, there is no requirement that local governments file reimbursement claims. That is a discretionary decision on the part of each local government. Furthermore, filing a claim for such reimbursement would not seem, in itself, to be a new program or higher level of service. Of course, an argument might be made that obtaining reimbursement is necessary to carrying out the actual mandates themselves in order to provide a source of funding. Nevertheless, the decision to file a claim remains discretionary.

Furthermore, staff is unaware of any other category of payment or claim for which government reimburses the claimant for their application costs. Taxpayers, for example, are not reimbursed for their tax preparation costs (although they may be deductible) even if they are owed a refund. Counties do not reimburse homeowners for filing a homeowners' property tax exemption claim even though that exemption is provided for in the state constitution.

While the same argument can be made that initial test claims are discretionary and not mandated, there is perhaps more of a basis for providing some reimbursement in these cases. This is because the cost of filing an initial test claim can be large and the benefit will accrue to all local governments affected by the mandate, not just the filing entity.

ISSUE 5: SO LONG TO LONG-SUSPENDED MANDATES?

LAO Recommends Changing Mandate to Statement of Intent. The budget proposes to suspend the last four mandates shown in the mandate summary table. These four mandates impose minor local government requirements, such as a duty to report on the number of Filipino employees. Over the last decade, no funding has been proposed for these mandates by an administration or a legislative budget committee. Instead, these mandates have been routinely suspended. To clarify the requirements of state law, we recommend the Legislature enact trailer bill language recasting these provisions as statements of legislative intent.

COMMENTS

The LAO recommendation would clarify existing law and it would be consistent with the ongoing practice of the Legislature and the current and past administrations.

ITEM 9840/9850 AUGMENTATION FOR CONTINGENCIES OR EMERGENCIES

In prior budgets, the administration was authorized to “spend at a rate that would result in a deficiency” by the authority provided under the former Budget Act language and Government Code Section 11006. Beginning with the 2004 Budget Act, the Administration no longer has this authority. Instead, a new process governing augmentations for contingencies and emergencies is in place to address departments' unanticipated expenses. The primary intent in making this change was to provide the Legislature the opportunity to exercise its control over appropriations by being notified of any unanticipated expenses *prior* to them being incurred. This framework is intended to rely on “pay as you go” budgeting.

How Unanticipated Expenses Are Funded. Under this process, the Administration is required to notify the Legislature of any departmental requests to fund unanticipated expenses. Approved unanticipated expenses are funded with either a transfer of funds from Item 9840 or a supplemental appropriation sought through legislation.

- **Transfer of Funds.** The Administration’s use of the funds appropriated in Item 9840 ($50 million General Fund and $15 million for special funds) are governed by the provisions of the item. The provisions prohibit the use of these funds in certain circumstances, including (1) any prior-year expenditure, (2) startup costs not yet authorized by the Legislature, (3) costs that the administration had knowledge of in time to include in the May Revision, and (4) costs that the administration has the discretion to incur or not to incur.

- **Supplemental Appropriations Bills.** Instead of a transfer of funds from Item 9840, the Administration may pursue an increase in an appropriation through a supplemental appropriation bill approved by the Legislature. The budget bill, however, does not specifically provide for such a process. Consequently, supplemental appropriations bills are not subject to restrictions that apply to 9840 fund transfers.

ISSUE 1: SUPPLEMENTAL APPROPRIATION PROCESS

Should There Be A Formalized Supplemental Appropriation Process? The lack of a formalized process for supplemental appropriations has allowed the Administration to pursue supplemental appropriations for activities ultimately determined inappropriate by the Legislature. For example, the Administration informed the Legislature of its intent to pursue a supplemental appropriations bill for the Gambling Control Commission to fund workload resulting from the passage of legislation ratifying several new gaming compacts. This legislation, however, was adopted without an appropriation. Such a funding proposal is not allowed under the restrictions governing 9840 funding transfers.

The Administration, of course, may propose any legislation it deems necessary or desirable. However, in those cases when proposed contingency or emergency appropriations meet the requirements specified in Item 9840, the Legislature could provide a supplemental appropriation bill process to identify those requests in order to simplify and expedite their passage (and inversely, to clarify when proposed augmentations do not meet those requirements). By requiring that these augmentation proposals be reported to the Legislature like those funded through Item 9840 fund transfers; the Legislature would be provided advance notice of these funding proposals. Advance notice would provide the Legislature an opportunity to review and have any of their concerns addressed prior to the introduction of the legislation. Given the advance review of these funding proposals, bills submitted under the supplemental appropriation process should move through the legislative process with less difficulty than other forms of legislation.

Under a “pay as you go” budgeting model, timely approval of funding proposals is necessary to effectively tie departmental spending to the Legislature’s appropriation authority. Also, establishing the supplemental appropriations bill process could strengthen the Legislature’s position when enforcing Control Section 32.00, which holds departmental staff who create an unauthorized excess expenditure personally liable.

COMMENTS

A supplemental appropriation process could be established by the adoption of suitable trailer bill language to require that the submittal of supplemental appropriation bills be governed by the restrictions similar to those that apply to Item 9840 funding transfers. This would make it more likely that the Administration would submit supplemental appropriations bills for unanticipated expenses consistent with Legislative intent.

The subcommittee may wish to request that the LAO work with staff to draft language that addresses these concerns.