A REVIEW OF THE EMPLOYMENT TRAINING PANEL PROGRAM

(PURSUANT TO CH 1074/82)

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INTRODUCTION

Chapter 1074, Statutes of 1982 (AB 3461), established the Employment Training Panel (ETP) program to provide training and jobs to individuals who are covered under the Unemployment Insurance (UI) system. Chapter 1074 also required the Legislative Analyst to prepare a report on the performance and cost-effectiveness of the ETP program and to recommend "any appropriate improvements." This report was prepared in response to Chapter 1074's directive.

In Chapter I, we describe the ETP program and the way in which training opportunities are created.

Chapter II examines how well the program has operated to date. In this chapter, we examine planned and actual program performance, and we compare ETP performance to training provided under the Job Training Partnership Act, Displaced Worker program.

Chapter III discusses the extent to which the ETP program is accomplishing its statutory goals of job training, reducing employer UI costs, and stimulating economic growth.

Chapter IV reviews panel administrative procedures with an eye toward ensuring that the panel's regulations are clear, consistent, and fiscally sound.

This report was prepared by Paul Warren under the supervision of Hadley Johnson. Invaluable assistance was rendered by Dan Alvarez, who provided research assistance, and Tanya Elkins, who typed the report.

EXECUTIVE SUMMARY

The Employment Training Panel (ETP) administers training programs for individuals covered by the Unemployment Insurance (UI) program. Existing law requires the panel to enter into "fixed-fee performance contracts" with employers or training agencies under which training is provided to eligible individuals. The "performance" feature of these contracts results from the fact that the employer or training agency is not paid for training a client unless the person is placed in an unsubsidized job for at least 90 days.

The panel's training programs are supported with funds raised by the Employment Training Tax (ETT). The ETT is a 0.1 percent payroll tax that is levied on specified employers. State law limits to $55 million the amount that can be deposited into the panel's account. Any ETT collections exceeding $55 million revert to the UI Fund.

ETP Experiences Major Administrative Deficiencies

Overall, the administration of the ETP program teeters on the brink of failure. In general, the deficiencies that we identified during our review (conducted in the fall of 1985) do not reflect flaws in ETP's basic programmatic design. Instead, we believe that ETP's problems stem from a $55 million annual appropriation that is simply too large for the panel's staff to distribute effectively each year. The panel tries hard to commit these funds. To facilitate this effort, however, the panel employs a number of questionable administrative practices:

- Large Amounts of Funds Are Committed For Projects; Relatively Small Amounts are Spent. The ETP program spent approximately 41 percent of the funds set aside for completed projects. In part, this low expenditure rate was caused by a placement rate for ETP training projects that was significantly below what was projected by the panel--59 percent rather than 90 percent. By committing a large amount of funds for each project, however, the program is able to encumber more of its annual appropriation--thereby giving the impression that it is able to spend its entire budget allotment.
- Subsidizing Inappropriate Training Projects. Our review indicates that ETP subsidizes normal, ongoing employer training costs by funding training targeted to a firm's existing workers, under the rationale that the workers were "potentially displaced." In this case, ETP goes beyond the intent of the law. Some of the firms we talked to admitted that ETP-funded training merely substituted for employer-paid training--in other words, the trainees were not in danger of being laid off. By supporting this type of training project, ETP is able to fund many otherwise-ineligible training activities, and thus commit a larger proportion of its funding.
- No Minimum Standards for Training Proposals. The panel has never adopted minimum standards for evaluating training proposals, as state law requires it to do. Indeed, our review indicates that ETP has virtually no official rules and regulations guiding program operations. Without program rules, ETP has the ability

to fund virtually any project it chooses, thereby making it easier to spend appropriated funds. We believe that the lack of regulations results in inconsistent administration and increased program costs.

Despite the panel's attempts to spend all of its funds, the panel has not been successful. We calculate that as of the fall of 1985, as much as $100 million of the $142 million in ETP funds appropriated to the program from 1982-83 through 1984-85 remained unspent for the purpose for which it was originally encumbered.

We continue to believe that ETP can be a successful component of the state's job training strategy. Our recommendations in this report are designed to help the program realize its potential by promoting compliance with the Legislature's intent and improving internal administrative procedures.

Program Performance Does Not Meet the Legislature's Expectations

The ETP program was slow in getting started. During its first two full years of operation (1983-84 to 1984-85), the panel contracted to train 44,462 individuals. Only 11,139 of these persons, or 25 percent, actually began training by June 30, 1985. Moreover, as of that date, the program had achieved only 8.6 percent of planned placements lasting 90 days.

A more serious problem with the ETP program is that projects have not operated as successfully as the panel anticipated. Program data show that for the 56 contracts completed as of June 30, 1985, the number of trainees enrolled in training projects was only 59 percent of what had been planned. The placement rate for completed projects--the percent of total trainees employed for 90 days after training--was substantially below what was projected: 59 percent, rather than 90 percent.

Since the panel only reimburses contractors after a trainee is placed in a job for 90 days, the low success rate of ETP programs translates into a low spending rate as well. Completed ETP projects spent only 41 percent of the funds originally reserved for them.

The Results From ETP and JTPA Title III Are Similar. While ETP's actual performance is disappointing relative to its expected performance, the program's results have been similar to those achieved by displaced worker training programs operated under the federal JTPA. These two programs, however, are not strictly comparable. The panel can screen potential trainees and select the most qualified individuals, while JTPA programs generally cannot choose who is trained. The ability of ETP to "cream" increases the programs' chances of successfully placing trainees in jobs, relative to the JTPA program.

Despite the ETP's ability to "cream," its programs have not yielded significantly better results than JTPA Displaced Worker programs. While the panel programs achieved higher placement rates (85 percent, compared to 71 percent for JTPA), the displaced worker programs, on average, helped trainees find jobs with higher wages ($7.44 per hour for JTPA versus $6.84 for ETP) and at a lower cost per trainee placed ($3,641 per placement for JTPA, compared to $4,545 for ETP).

ETP Administrative Costs are High. The panel does not track the administrative costs associated with successful placements. We estimate that the administrative cost for the period from 1983-84 through 1984-85 averaged between $499 and $2,228 per placement. Our analysis suggests that the true administrative cost for this time period probably was closer to the larger figure. Generally, an administrative cost approaching $2,000 per trainee is considered very high.

We believe that the panel's administrative costs are high for three reasons:

1. ETP administrative costs include the cost of collecting the ETT, which supports the operation of the panel and its training projects.

2. Due to the relatively small number of trainees who were successfully placed during 1983-84 and 1984-85, administrative costs were spread over relatively few successful placements.

3. The panel's use of master contractors--agencies paid to develop training projects--is a costly mode of administration.

ETP Subsidizes Normal Employer Training Costs

State law permits the panel to train UI recipients, unemployed individuals who have exhausted their eligibility for UI, and currently employed workers who the panel determines are "likely to be displaced." As of June 30, 1985, 40 percent of the planned trainees under approved ETP projects were considered potentially displaced employees.

The panel has never defined what "likely to be displaced" means. Nor does it require employers to document their assertions that workers would be displaced from their current jobs without ETP training. Furthermore, the panel does not ask employers to certify that the proposed training would not take place without ETP assistance. Because the panel has not defined potentially displaced, the panel and its staff have enormous discretion over which training proposals to support.

Our review of ETP projects indicates that ETP funds are being used to supplant employer-paid training efforts. We find that a number of employers would have paid for the training of their workers if ETP-subsidized training had not been available. In fact, some of the employers we interviewed admitted that ETP-funded training merely substituted for employer-paid training--a strong indication that the affected employees were not at risk of being laid off, making the training project ineligible for funding by the panel.

Panel staff acknowledged that some ETP-funded training would have occurred without the training subsidies. The staff believe, however, that the subsidies yield other benefits--increased productivity and additional economic growth--which justify state support for ongoing employer training costs. The panel staff, however, could not document that these additional benefits result from ETP activities. This is not surprising since the staff's arguments are not analytically sound.

In order to ensure that the panel trains only those workers who truly are "likely to be displaced," we recommend the panel adopt written standards defining this key term.

Impact of ETP on Economic Development Could Be Increased

One of the major goals that the Legislature established for the ETP program is to increase economic development. Unfortunately, there is no accurate way to measure the program's effect on the economy.

Even though we cannot measure the absolute impact of ETP subsidies on economic growth, our analysis suggests that ETP funds could have a greater impact on the state's economy if the program focused more resources on smaller, more marginal firms. This is because the subsidies will have a larger proportional impact on a small firm's cash flow and profits than they will on a large firm's operating results. By helping small firms become more productive, the ETP will increase the chances that they can survive, thereby promoting economic growth.

At the present time, the panel does not have good ways to market its program to small firms. Although the panel contracts with three agencies to inform business that ETP funding is available, these agencies generally do not reach small firms. The California Manufacturers Association, which is paid to market the program to manufacturing firms, tends to focus on the training needs of larger manufacturing firms. The Department of Commerce and the California Association for Local Economic Development are paid to market the program to local economic development agencies. These agencies tend to focus on the needs of new business, not the needs of existing firms.

In order to maximize the potential for ETP funds to increase economic growth in the state, we recommend that the panel devise a written plan identifying how it proposes to increase the participation of small firms in the program.

ETP Needs to Adopt Regulations

Our review of ETP procedures indicates that a wide variety of policies, procedures, and standards remain to be determined by the panel. For example, the panel has never officially adopted minimum standards for evaluating training proposals, even though state law specifically requires the panel to establish these standards. Moreover, the panel has not developed other rules and regulations that would allow the program to operate in a predictable fashion.

We have identified three general areas where regulations are needed:

- Program Standards and Definitions. The ETP statutes require that the panel support training in jobs with "definite career potential and long-term job security." These terms have never been defined. Consequently, the Legislature cannot determine whether ETP projects train individuals in jobs with career potential.
- ETP Procedures. The panel often amends training contracts after it has given final approval to the contracts. The panel, however, has no written guidelines specifying the process contractors must go through to obtain amendments, the criteria used to evaluate proposed amendments, or the timelines for panel action on amendment proposals. As a result, amendments are granted at the panel's discretion, and the predictability of the system may be lost.
- Program Policies. The law exempts the program from the state's competitive bidding process, which means the panel has to determine the prices it will pay for training. The panel has no policies governing the price-setting process, causing the reimbursement rates paid to contractors for training to differ in ways that are not logical. In one case, the panel pays one agency more to provide 100 hours of training than it pays a second agency to provide 600 hours of training in the same occupation. We could find no analytical basis for such a significant difference in training rates.

In order to assure that the panel operates according to consistent rules and procedures, we recommend that the ETP adopt concise, comprehensive regulations in order to clarify the program's standards, policies, and procedures. These regulations should be adopted in accordance with the state Administrative Procedures Act.

Limits Needed on ETP Funding

State law limits the amount of funds collected by the ETT and credited to the ETP to $55 million annually. The ETT is a 0.1 percent payroll tax that supports the operation of the panel and its training projects. According to ETP records, the panel received $32.3 million, or 23 percent, more than it could spend or encumber during the period 1982-83 through 1984-85. These funds remain available to the panel for expenditure without regard to fiscal year.

Our analysis indicates that in the fall of 1985, the amount of uncommitted funds--funds not reserved for specific training projects--was significantly larger than the $32.3 million indicated by the panel. This is because some encumbered funds which were set aside for master contractors and other specified agencies had not been committed to a specific training project. The ETP records indicate that an additional $23.6 million in encumbered funds had not been committed to support training projects. When these funds are added to the $32.3 million in unencumbered funds, we find that a total of $55.9 million in ETP funds were not committed at the end of 1984-85.

In addition, our analysis suggests that a substantial portion of the panel funds which have been committed to specific training projects will not be spent. This is because ETP contractors to date have spent only 41 percent of the funds originally encumbered in support of their training projects. If future expenditure rates average 41 percent, an additional $46 million in training funds will be returned to the panel. Added to the $56 million in uncommitted funds remaining at the end of 1984-85, this would mean that $102 million, or 72 percent of the panel's total appropriations since 1982-83, had not been spent.

Given the program's past performance, it is unlikely that the panel will be able to spend such a large amount. Indeed, since the panel has not been able to spend its annual $55 million appropriation, we see no reason to believe that it can spend an additional $75 million to $100 million in the immediate future.

Therefore, until the program demonstrates the capacity to spend $55 million each year, we recommend that the Legislature enact legislation reverting to the UI Fund all uncommitted funds remaining in the ETF at the end of each fiscal year.

CHAPTER I

THE EMPLOYMENT TRAINING PANEL PROGRAM

The Employment Training Panel (ETP) program was established by Chapters 1074 and 1075, Statutes of 1982 (AB 3461 and AB 3154). The enabling legislation identifies who is eligible to receive training--primarily Unemployment Insurance (UI) recipients--and the types of services that are provided--skill training. This chapter describes the ETP program and provides a brief overview of its current operating procedures.

ETP Legislation

Goals of the Program. The ETP program is designed to accomplish a number of goals. A primary goal, of course, is to provide training to unemployed individuals so that they can find jobs. The program targets training services to workers who are covered under the UI program. Specifically, ETP may train UI recipients, unemployed individuals who have exhausted eligibility for UI benefits, and currently employed workers who are likely to be displaced and become UI recipients.

Another goal of ETP is to stimulate economic development by providing incentives to employers to locate or expand their businesses in California. These incentives include (1) subsidizing the training costs of firms within the state, (2) providing training so skilled workers are easily available to firms, and (3) training workers in occupations where there is an "acute need for skilled workers."

A third goal of ETP is to reduce employers' UI costs. Under the UI program, employers are required to pay a variable rate tax in order to support the costs of benefits provided to their former employees. The actual rate an employer pays is based on how often the employer lays off employees, thereby imposing costs on the UI Fund, which must pay benefits to the unemployed workers. Thus, if ETP training helps UI recipients find jobs more quickly, it may reduce the amount of UI benefits paid out of the UI Fund and, ultimately, reduce employer UI costs.

Functions of the Panel. Chapter 1074 created a seven-member panel responsible for overseeing the operation of the ETP program and providing direction to the staff that administers the program. The act requires that the panel members have experience in business management and employment relations.

The ETP legislation requires the panel to perform specific functions, as follows:

- Solicit training proposals and write contracts on the basis of proposals made directly to it and on the basis of recommendations made by local review panels.
- Establish minimum standards in order to evaluate proposals.
- Ensure adequate protection of program funds by establishing fiscal and accounting controls, as well as by monitoring and auditing ETP projects.
- Allocate funds to support training projects and the administrative expenses of the ETP staff.

The Employment Training Fund (ETF). The ETP program is supported by the Employment Training Tax (ETT), which is deposited in the ETF. The ETT is a 0.1 percent employer-paid payroll tax that is levied on those employers maintaining a positive UI account balance. That is, the tax is levied on most firms that have paid more into the UI Fund over time than their laid-off employees have collected in benefits. The law limits to $55 million the amount of ETT collections that may be deposited in the ETF. Collections in excess of $55 million revert to the UI Fund.

The law limits the administrative costs of the panel and its staff to 15 percent of ETT collections. It also requires that any expenditures for marketing of the ETP program that are called for by a training contract be counted as administrative expenses subject to the 15 percent cap.

<u>ETP is Different From Other Training Programs</u>. The ETP program differs from other training programs in two distinct ways. First, the act requires the panel to reimburse training providers using "fixed-fee performance contracts." Under these contracts, the panel reimburses training providers at a fixed amount per trainee, <u>provided</u> the trainee successfully completes the program. The ETP legislation defines successful completion as being employed by a single employer for 90 days. Thus, the design of ETP ensures that program funds will help workers find jobs since training costs are reimbursed only after a trainee holds a job for 90 days with an employer. Most other training programs pay providers regardless of whether trainees find jobs or not.

Second, ETP differs from other training programs in that it can pay employers to provide training to their own employees. Most training programs either provide training directly or through contracts with training agencies and community colleges. The law allows ETP to contract with a training agency if the agency can demonstrate that it can operate a successful program meeting the labor force needs of employers. Unlike other training programs, however, ETP can contract for training directly with employers.

How the ETP Program Operates

The panel has adopted a four-step process for developing and funding training projects. As part of this process, ETP staff:

1. Develops a preliminary outline of the proposed training project for the panel's review.

2. Develops a complete training and funding contract for the panel's approval.

3. Monitors and reviews the project as it is implemented.

4. Verifies the outcome of the completed program.

The panel staff learns of potential training projects from three primary sources: employers, training agencies, and master contractors (master contractors are paid by ETP to develop training projects). The panel staff reviews initial proposals to determine whether the training qualifies for ETP subsidies. If a project qualifies, the staff begins negotiations to determine the basic parameters of the project, including the number of trainees, the type of training that would be provided, the approximate cost of the training, and the wage that trainees can expect to earn once training is completed. This information is presented to the panel for its review. Generally, the panel approves or rejects the proposal depending on whether the proposal meets ETP policy requirements. For example, the panel usually will not fund projects that offer a starting wage below $5 per hour, or projects that cost more than $5,000 per trainee. The panel, however, sometimes departs from these guidelines.

Once the panel approves the outline for a training project, a number of wheels are set in motion. First, the outline is sent to various state and local agencies for review and comment. Among the agencies receiving approved outlines are local private industry councils (PICs) and service delivery areas (SDAs), as well as the state Departments of Employment Development and Commerce. Second, the staff (or a master contractor) develops a formal contract stipulating the terms of the training agreement between the ETP and the contractor. This contract is presented to the panel for its approval. The proposed contract also must be approved by any union whose members might be affected by the training.

Panel staff monitor the projects continuously. The ETP feels that monitoring helps ensure that the contractor will comply with the terms of the contract and uncover trouble spots early in the life of the training project. The ETP staff monitor projects either by telephoning the contractor or by visiting the training site. Panel rules require a site visit within 45 days of when training begins.

Once training is completed, ETP staff telephone contractors to determine the extent to which trainees were placed in a job as required by the contract. The ETP staff also telephone contractors at the end of the 90-day employment period to verify that the trainee was employed during that time period. In addition, the panel staff sometimes verifies the employment status of the trainee using UI files from the Employment Development Department (EDD).

<u>Master Contractors</u>. Many of the administrative activities discussed above are often carried out by master contractors, or by entities that are provided a "letter of intent" by the panel. In essence, these agencies are

paid by the panel to provide a range of administrative services to the panel. The ETP defines master contractors as qualified training agencies or groups of employers that have the expertise to help employers design and implement training programs. At the time this report was prepared, master contractors included the California Manufacturers Association (a trade organization representing manufacturing firms in California), the Los Angeles Community College District, and the Northern California Higher Education Council (a collection of community colleges located in rural counties in the northern part of the state).

Agencies that do not qualify as a master contractor may receive a letter of intent from the panel, which states the panel's willingness to fund projects developed by these agencies. Among the agencies that have received a letter of intent are the state Department of Commerce, the Office of the Chancellor of the Community Colleges, and the San Diego Regional Employment and Training Consortium.

Typically, the services provided by master contractors and agencies granted letters of intent are the same--primarily marketing and outreach services. In this way, ETP takes advantage of existing relationships to inform firms of ETP subsidies and establish credibility in the eyes of employers. It might take the panel much longer to establish this credibility on its own. For example, the California Manufacturers Association (CMA), which represents many manufacturing firms in California, has access to decision makers in manufacturing that a new state program could not hope to match. By using the association as a master contractor, ETP can take advantage of CMA's access to businesses.

Many master contractors also assist employers in designing and, in some cases, operating training programs. The ETP reimburses master contract agencies based on the number of trainees the agencies help place in a job for 90 days. Currently, ETP pays master contractors up to $800 per successful placement. For example, if a master contractor develops a training project that places 50 trainees, the contractor could earn up to $40,000 for its efforts (50 x $800 = $40,000).

CHAPTER II

WHAT ARE ETP's ACCOMPLISHMENTS TO DATE?

In this chapter, we review the performance of the ETP's training programs after two years of operation. Specifically, we examine ETP's success in placing trainees in jobs, and compare the program's performance with its planned objectives. We also discuss the cost of ETP training, as well as the ability of the panel to spend the funds that the Legislature makes available for training.

The performance data reviewed in this chapter indicate that the panel's programs have not been particularly successful in achieving planned objectives. Nor has the ETP been noticeably more cost-effective than federal Job Training Partnership Act (JTPA) programs. Finally, the data indicate that while the panel has obligated large sums of money to date, relatively few trainees have been successfully placed. As a consequence, a relatively small portion of these funds has actually been spent.

Performance Data for All ETP Projects

The ETP maintains extensive performance data on its training projects. Table 1 compares the planned and actual performance for all panel projects approved as of July 1, 1985. Not all of the projects covered by this table are completed. As a result, the performance figures tend to understate program accomplishments. Nevertheless, we believe that the data provide useful information on the progress of ETP projects after two years of operation.

Table 1

Employment Training Panel Projects
All Approved Projects
As of June 30, 1985

Performance Indicator	Planned Performance	Actual Performance	Actual as a Percent of Planned Performance
Number of trainees	44,462	11,139	25.1%
Number of trainees hired in a job	39,897	5,538	13.9
Number of trainees placed for 90 days	39,897	3,450	8.6
Dropout rate	10.3%	18.1%	175.7
Funds expended	$94,955,342	$9,330,707	9.8

ETP Experiences a Slow Start-Up. The data in Table 1 indicate that ETP projects have been slow in getting started. During the first two years of operation, the panel approved plans to provide training to 44,462 individuals. As of June 30, 1985, however, only 25 percent of these individuals had actually begun training. Moreover, the number of individuals that had actually completed training and remained employed for 90 days was only 8.6 percent of what was planned.

According to panel staff, this slow start-up reflects a variety of factors including the following:

- Employers often need a significant period of time to prepare for training. During this period, employers arrange in-house training programs or contract for needed training from an outside firm or agency. This delay is one cause of ETP's start-up problems.
- Many employers train new employees in small groups as they are needed even though their contracts call for a larger number of

trainees. For example, although a contract may call for training 100 employees, an employer may choose to train only 10 individuals at a time. As a result, while the employer may train 100 workers during the life of the contract (up to 2 years), it may appear that fewer people are being trained at any one time.

Completed Projects Have Not Achieved Program Objectives

A second factor explaining the difference between planned and actual performance is that completed ETP projects have not produced the results originally anticipated. Table 2 provides performance data for the 56 projects that were completed as of June 30, 1985. It shows that under these contracts, 1,669 workers were trained and placed in a job for at least 90 days. In general, these projects ran the full length of the period specified in the contracts, although a few contracts were terminated early.

Low Enrollment Rates. As Table 2 demonstrates, project performance has been somewhat disappointing in several respects. First, ETP projects did not enroll as many trainees as planned. On average, panel projects enrolled only 59 percent of the planned number of trainees. According to ETP staff, enrollments were below expectations for three reasons.

- First, training projects experienced difficulty in recruiting trainees. In some low unemployment areas, trainees were particularly hard to find.
- Second, panel staff believe that some employers had unrealistic training plans that did not accurately reflect the needs of the company. These plans called for more trainees than the companies would need and the type of training planned was not appropriate

for the skills needed by the firm. As a result, these projects were not successful.

- Third, some firms' hiring needs changed during the life of a contract, thereby reducing the number of trainees enrolled in a project.

Table 2

Employment Training Panel Projects
All Completed Projects
As of June 30, 1985

Performance Indicator	Planned Performance	Actual Performance	Actual as a Percent of Planned Performance
Number of trainees	4,822	2,848	59.1%
Number of trainees hired in a job	4,094	1,886	46.1
Number of trainees placed for 90 days	4,094	1,669	40.8
Placement rate	84.9%	58.6%	69.0
Dropout rate	15.1%	33.8%	223.8
Funds expended	$10,361,426	$4,262,622	41.1

Low Placement Rates. Even when the lower enrollments are taken into account, the ETP placement rate is significantly below the rate forecasted by the contractors. Table 2 shows that 59 percent of the trainees were employed for 90 days, as compared to the 85 percent rate projected for these projects.

The ETP staff gave two reasons for the lower rate. First, the dropout rate in ETP projects (the percentage of enrollees that do not complete training) was significantly higher than anticipated. Table 2 indicates that while the panel expected a 15 percent dropout rate, the actual dropout rate averaged 34 percent. Second, not all trainees who completed training found jobs that qualified as a placement under the terms of the contract. For example, a computer programmer trainee is not counted as a successful placement if he or she finds a job in an unrelated occupation, such as accounting. The panel staff believe that training agencies--which generally do not train individuals for jobs with specific firms--experience difficulty placing trainees in jobs related to the training. The staff offered no data to support this theory, however.

Low Expenditure Rate. Table 2 also shows that completed ETP projects spent only 41 percent of the funds obligated for them. The low expenditure rate is due to the fact that the number of trainees employed 90 days was well below the planned level. Table 2 shows that completed projects achieved only 41 percent of the planned placements. Since the ETP pays for training costs only when a trainee is employed in a job for at least 90 days, a low placement rate translates automatically into a low expenditure rate.

Success With the "Potentially Displaced" is Comparable to Success with Unemployed Persons

The ETP program trains two types of workers: (1) unemployed individuals who are collecting UI benefits or have exhausted eligibility for such benefits and (2) currently employed workers who are "likely to be displaced" and, therefore, are likely to collect UI benefits in the future. Table 3 shows ETP performance data for completed projects based on whether the project provided training to unemployed individuals or to workers who were likely to be displaced.

Table 3

Performance Data for Completed Employment Training Panel Projects By Target Group

Performance Indicator	Projects Training the: Unemployed	Projects Training the: Potentially Displaced	Difference Amount	Difference Percent
Number of trainees	1,979	869	1,100	--
Percent completing training	71.8%	67.5%	--	4.3%
Percent employed for 90 days	60.7%	53.9%	--	6.8
Dropout rate	24.7%	30.5%	--	-5.8
Hourly wage	$6.84	$8.27	-$1.43	--
Cost per trainee[a]	$3,157	$2,284	$873	--

a. Does not include administrative costs.

Placement Rates. We would expect projects serving the potentially displaced to be much more successful than projects involving the unemployed. This is because most projects serving the potentially displaced retrain individuals for other jobs within the same firm. Thus, employers have a large advantage in working with their existing employees: they already know the trainees' work histories and abilities. We expected that this advantage would translate into more successful programs.

In view of these exceptions, the data in Table 3 is particularly surprising. It shows that projects training the unemployed were more successful than projects serving displaced workers. In fact, the percent of potentially displaced trainees that were successfully placed was 54 percent--6.8 percentage points below the placement rate for projects training unemployed individuals.

Cost Per Trainee. Table 3 shows that the costs per unemployed trainee were $873 higher than the costs for training the potentially displaced trainee. The difference reflects ETP's belief that training projects for unemployed persons would experience higher dropout rates.

According to panel staff, anticipated dropout rates are taken into consideration when developing the ETP reimbursement rate. For example, a project training 100 people that anticipates a 20 percent dropout rate received an ETP reimbursement rate which is 20 percent above average projected per-trainee costs. In this way, the contractor is able to cover all of his costs if he meets the agreed-upon placement target. Thus, higher expected dropout rates for unemployed individuals account for part of the $873 difference in the average cost of training the two types of workers.

As Table 3 indicates, however, the dropout rate is not significantly different for the two groups. This suggests that either employers cannot determine as accurately as we expect which employees will successfully complete training or employers are not as careful in screening trainees because ETP is underwriting most training costs. We have no data to indicate which factor plays the more important role in most projects.

Hourly Wage Per Trainee. The wage differential between the two groups of trainees--the unemployed and the potentially displaced--is significant. Unemployed ETP trainees received $6.84 per hour as a beginning wage, whereas the potentially displaced received $8.27. The potentially displaced trainees received a higher starting wage because the skill level required for their jobs was significantly higher than that required of newly employed persons (that is, the previously unemployed).

There are other forces affecting starting wages, such as unionization of the workforce and prevailing industry wages. Our analysis suggests, however, that these forces did not significantly increase the wages of the potentially displaced relative to the unemployed. Rather, our review suggests that the potentially displaced are more likely than unemployed trainees to be trained for high-skill occupations. For example, the potentially displaced are more likely to be trained as senior electronics technicians, microprocessor repairers, and precision instrument makers; the unemployed are likely to be trained as apprentice carpenters, tree trimmers, and restaurant managers.

ETP and JTPA Performance: A Comparison

While ETP's actual performance has been disappointing, particularly when compared with expected performance, the program's accomplishments, in some respects, are similar to those produced by displaced worker training programs operated under the federal JTPA program.

Table 4 compares the performance of the ETP program with that of the JTPA Title III Displaced Worker programs. In reviewing the findings in Table 4, one should recognize that these two programs are not strictly comparable, for a number of reasons. First, ETP provides services to a broader and more diverse population. The ETP can choose among all UI recipients, whereas JTPA serves those individuals who are unemployed due to a plant closure or mass layoff and whose industry or occupation is no longer in demand. Second, the Title III JTPA projects generally cannot choose which participants receive services; most programs make services available to all eligible participants at a plant. In contrast, ETP projects can screen potential trainees so that only the most qualified individuals receive services. This ability to "cream" increases ETP's chances, relative to the JTPA program's, of successfully placing its trainees in jobs. These differences between ETP and JTPA should be kept in mind while reviewing the findings in Table 4.

Table 4

Actual Performance Data for Completed Employment Training Panel (Unemployed Workers Only) and JTPA Displaced Worker Programs

Performance Indicator	Training Program: JTPA Title III	Training Program: ETP[a] (Unemployed Only)	Difference: Amount	Difference: Percent
Percent of completers who are employed	70.7%	84.5%	--	13.8%
Hourly wage	$7.44	$6.84	-$0.60	--
Cost per trainee	$3,641	$4,545	$847	--

a. ETP data were adjusted in order to allow comparisons with Title III Displaced Worker programs.

Table 4 shows that Title III projects resulted in higher wages at a lower cost per trainee. The average hourly wage of Title III participants was $0.60 per hour more than the average wage of ETP unemployed trainees. The JTPA cost per employed trainee was significantly lower than ETP's--$847, or 19 percent less.

The panel projects, however, achieved a much higher employment rate for those individuals who completed training. The panel projects had an average placement rate of 85 percent for those individuals who completed training, compared to 71 percent for Title III trainees. This large differential stems primarily from the ETP requirement that training be provided for occupations that are in demand by local employers. Title III programs seldom have training requirements as stringent as the panel's.

ETP Administrative Costs Are High

The panel does not track the administrative costs associated with a successful placement. As a result, we had to calculate that figure in order to derive estimates of administrative costs for 1983-84 and 1984-85.

In order to derive the average administrative cost under ETP, however, it is necessary to decide how these costs should be apportioned. Should the costs be spread over actual placement or potential placements which the panel is likely to achieve as a result of the contracts approved during the two fiscal years?

Table 5 shows two estimates of ETP administrative costs: the average administrative cost per potential placement and the average administrative cost per actual placement. Both figures were calculated using administrative costs from 1983-84 and 1984-85, as follows: total ETP operating costs (administration plus marketing and outreach) were added to the costs of collecting the Employment Training Tax (ETT) in order to derive the total administrative costs of the ETP program.

Table 5

ETP Administrative Costs
1983-84 and 1984-85

Cost Component	1983-84	1984-85	Total
Collection of the ETT	$1,430,000	$1,489,000	$2,919,000
ETP administration	1,675,000	2,539,000	4,214,000
Marketing and Outreach	--[a]	552,000[b]	552,000
Totals	$3,105,000	$4,580,000	$7,685,000
Actual placements 1983-84 and 1984-85:			3,450
Potential placements developed in 1983-84 and 1984-85:[c]			15,400
Administrative cost per actual placement:			$2,228
Administrative cost per potential placement:			$499

a. In 1983-84, most marketing and outreach expenses were included as part of training contracts and, therefore, do not appear as an administrative cost.

b. Administrative costs associated with Letters of Intention are included as part of training contracts and, therefore, do not appear as an administrative cost.

c. Potential placements were derived as follows: total planned enrollments in all ETP projects were multiplied by the fraction of enrollments in completed projects that resulted in actual placements (34.6 percent).

As Table 5 indicates, the two approaches result in very different estimates of administrative costs. If we calculate administrative costs using actual placements, then the administrative cost totals $2,228 per trainee. This estimate, however, overstates administrative costs because it reflects the cost of work done to develop contracts that have not yet resulted in successful placements.

On the other hand, if we calculate costs based on potential placements, the average administrative costs drops to $499 per trainee. This latter estimate is 8.4 percent below the average administrative cost of $545 experienced by JTPA Title III programs. The cost per potential placement, however, understates administrative costs because significant additional time and money must be spent to ensure that these potential placements actually occur.

Given the data currently available, we cannot determine the amount of ETP administrative costs that are associated with each successful placement. Our analysis indicates that, while the true administrative cost is somewhere between $499 and $2,228, it probably lies closer to $2,228 because the panel understated its estimate of administrative spending, as follows:

- Some ETP administrative costs are not counted as administrative costs. In 1983-84, most marketing and outreach expenditures paid to master contractors were not counted as an administrative expense. Similarly, administrative costs incurred by "letter of intent" agencies were not considered administrative costs during 1983-84 or 1984-85. As a result, our estimates of the panel's costs are too low.
- Some administrative expenses incurred during 1983-84 and 1984-85 will not be paid during those years. For example, the panel pays master contractors based on the number of placements the contractors are responsible for developing. As a result, while master contractors spent time and money developing contracts in 1983-84 and 1984-85, they may not be reimbursed until 1985-86 or

even 1986-87, after trainees under these contracts are employed for 90 days. If measurable, these hidden costs would further increase our estimate of ETP administrative costs for 1983-84 and 1984-85.

Why are ETP Administrative Costs So High? For these reasons, we conclude that actual ETP administrative costs are significantly higher than Title III administrative costs. There are a number of factors--not all which are within the power of the panel to change--which account for ETP's relatively high administrative costs. First, part of ETP's administrative costs are attributable to the cost of collecting the ETT. In contrast, there are no tax collection costs associated with the JTPA programs; thus, ETP and JTPA administrative costs are not strictly comparable. Nevertheless, it is appropriate to include the tax collection costs as part of ETP's administrative costs because without the program, there would be no need for the ETT and its associated costs. On the other hand, the federal government would incur the same tax collection costs, regardless of whether or not JTPA existed. If ETT collection costs are excluded, ETP administrative costs average $1,381 per placement, which is still more than twice the size of JTPA Title III administrative costs.

Second, low program output during the first two years of operation also contributed to the high average administrative cost of the panel. As Table 5 indicates ETP placed 3,450 trainees in jobs during 1983-84 and 1984-85. As this number grows in the future, average ETP administrative costs should diminish.

A third reason for the high administrative costs is the panel's use of master contractors to carry out a range of administrative activities.

The panel pays master contractors up to $800 per trainee placed in a job for 90 days. Thus, for a medium-sized project involving 50 trainees, a contractor could earn up to $40,000--an amount sufficient to hire one additional full-time state staff. The contractor's duties connected with this project, however, represent much less than one man-year worth of effort. This is because the contractors primarily are paid to (1) develop training projects and (2) monitor approved projects in order to insure that the project operates as planned. (Contractors cannot conduct certain types of administrative activities, such as ensuring that training is provided as specified in the ETP contract and verifying that trainees were employed for at least 90 days. The ETP staff must perform these duties.) On average, developing and monitoring a project does not require a man-year's worth of time. In fact, the workload associated with a typical project averages significantly less than half a man-year. Therefore, we conclude that master contractors are significantly more expensive to use for administrative purposes than state staff.

CHAPTER III

IS ETP ACCOMPLISHING ITS STATUTORY GOALS?

The laws establishing ETP identify three primary goals for the program: to help UI recipients find work, to minimize employers' UI costs, and to stimulate economic development. This chapter measures how well ETP is meeting its statutory goals.

In general, we conclude that the panel is not maximizing the use of ETP funds to attain legislative goals. Our review suggests that, due to vague program policies, ETP primarily trains employed individuals who probably do not qualify as employees "likely to be displaced." As a result, panel funds tend to supplant employer funding for employee training. For this reason, we believe that the actual benefits of the program to the unemployed are considerably less than what they would be otherwise.

In addition, the ETP program appears to actually increase UI benefit costs in the short run. This is because most ETP trainees collect these benefits while in training. Although it is possible that ETP will reduce UI costs in the long term, there is no way to determine if this will occur given only two years of program experience.

Finally, we find that ETP's contribution to the state's economic development probably is minimal, primarily because there are few opportunities for training to dramatically improve the future health of a firm. We believe, however, that the panel could increase ETP's potential impact on the economy by intensifying its focus on assisting small business.

ETP Trains the Employed

State law permits the ETP to train individuals who (1) are current UI recipients, (2) have exhausted their UI benefits and remain unemployed, or (3) are employed but are "likely to be displaced and therefore claiming UI benefits."

The ETP program was established in 1982, at a time of high unemployment. A number of manufacturing plants in California were in the process of closing or significantly reducing their workforce, leaving long-time employees with few prospects for future employment. Existing training programs, however, could not assist these individuals until they became unemployed. Thus, even though it was clear that these workers were going to be unemployed and would need training to become reemployed, no services were available to them. In order to fill this gap, the Legislature empowered the panel to provide training to employed workers who were likely to be displaced from their jobs.

In practice, the panel trains significant numbers of employed workers that it considers to be in the "likely to be displaced" category. As of June 30, 1985, 40 percent of all proposed trainees under approved ETP contracts were employed but, according to the panel, "potentially displaced." The panel, however, has never officially defined "potentially displaced." Instead, it decides on a case-by-case basis whether training proposals meet the intent of the legislation.

The panel staff provided us with the following working definition of "potentially displaced": potentially displaced means that a worker would lose his or her job within the next two or three years unless trained in a new skill. According to the ETP staff, employers must do the following in order for their workers to be considered "potentially displaced." First, employers must demonstrate that affected employees will experience a "change in the nature" of their jobs that necessitates training. Second, employers must show that the proposed training plan provides workers with the skills needed to successfully deal with the changing job requirements. Third, employers are required to certify to the panel that the employees in training are likely to be displaced. (The employer, however, is not required to certify that the workers will be laid off within a specified period of time in the future.)

"Potentially Displaced" Policy Is Too Vague. There are two problems with the panel's policy toward potentially displaced employees. First, it is almost impossible for the panel to determine whether a worker without ETP training is likely to be displaced two or three years in the future. The panel does not require that firms document their future plans for these employees. Indeed, the employers we interviewed indicated that corporate manpower policies rarely extend beyond one year into the future, and they could not document that specific employees were likely to be laid off if they did not receive training. As a result, the panel must rely on the employers' certifications that the employees are potentially displaced. Since potentially displaced has no definition, it is not evident what it is that employers are certifying.

Second, the panel does not ask employers to certify that the training proposed for ETP funding would not take place without ETP assistance. This is a critical defect of the policy, because if employers would have provided the same amount of training in the absence of ETP subsidies, then employees were not at risk of being laid off in the first place.

Because its policies are so vague, the panel maintains incredible discretion over which training proposals can be supported.

ETP Subsidizes Normal Employer Training Costs. Our review of ETP projects indicates that the panel's vague policies regarding potentially displaced workers cause the program to subsidize many employers' normal ongoing training costs. This is especially likely to occur when the "potentially displaced" project involves training workers to use automated machinery which replaces the firm's less automated equipment.

For example, one ETP contract trains machinists working in the aerospace industry in the use of computer-controlled machining equipment. According to the panel contract, these machinists would lose their jobs if they are not retrained. It is improbable, however, that a firm in the aerospace industry would lay off experienced machinists and attempt to hire new ones, given the fierce competition for machinists in the Los Angeles area. (Indeed, EDD's data indicate that competition for inexperienced machinists in the area is keen.) Thus, the demand for machinists suggests that those currently employed are not likely to be laid off in the foreseeable future. Furthermore, it is obvious that if a firm installing new equipment did not train its workers to use the new machines, the firm would not have adequate personnel to operate. Thus, we conclude that in this instance, ETP is paying for training that the firm ordinarily would have provided to its workers.

Our review found many other ETP contracts where it is highly doubtful that the target employees would be at risk of being laid off without ETP subsidies. Among these are projects providing for:

- Computer programming training. Currently, the panel is funding a project that is training 40 employees to become computer programmers for a firm that is automating its operations. At the time the contract was approved, the firm had a long-standing no-layoff policy; employees whose jobs were abolished typically were retrained for other assignments rather than let go. In fact, the firm apparently sought to conceal the basis for the project from its employees. The employees participating in the ETP training class did not know they were considered to be potentially displaced. Furthermore, the panel staff excused the firm from requiring trainees to indicate on ETP forms why they qualified for ETP subsidies. The employer has acknowledged that the computer training would have occurred regardless of whether the panel subsidies were available.
- Engineer computer training. A second project trains engineers in a new computer language that the federal government may require specified manufacturers to use. Currently, no one knows how to use this computer language because it is brand new. As a result, the firm could not replace its current employees with new hires because there are no engineers familiar with this language that the company could hire. The company advised us that this training would have occurred regardless of whether the panel subsidies were available.

Panel Admits That Some ETP-Funded Training Would Have Occurred. The panel staff has admitted that some training funded by ETP would have been provided by firms in the absence of training subsidies. The staff believes, however, that even under these circumstances the subsidies produce benefits to the state.

We Do Not Find the Staff's Arguments Convincing. The arguments themselves are not analytically sound, and panel staff have not offered any data to support them. In addition, some of the staff's reasoning is clearly contrary to state law. Indeed, the staff's explanation for why it subsidizes training that otherwise would have occurred strikes us as simply a rationale for activities that have no sound justification.

The ETP staff claims that by subsidizing normal business training activities, the program achieves the following benefits:

- ETP subsidies improve existing training efforts, thereby increasing worker productivity. This argument assumes that employer-funded training does not maximize worker productivity--but that ETP-supported training does. This seems unlikely. We doubt that the panel understands employer training needs better than the employers themselves. In addition, if the panel was concerned with improving existing training efforts, we would expect ETP staff to assess whether the cost of such training to ETP was justified in light of anticipated productivity improvements. The panel does not measure productivity improvements generated by ETP training.
- ETP subsidies encourage firms to retrain their employees. This argument also assumes that firms do not understand the value of retraining--but ETP does. In addition, the panel does not operate the program in a manner which would demonstrate the value of retraining. Specifically, it does not measure

productivity gains and other savings resulting from ETP-funded training.

- ETP subsidies help firms maintain their no-layoff policy. Firms with no-layoff policies already understand the value of retraining. Therefore, these employers do not need ETP subsidies to spur retraining. None of the employers we interviewed suggested that existing no-layoff policies would have been terminated without state subsidies.
- ETP subsidies enhance economic development within the state. We believe that a general subsidy of business operating costs--in this case training costs--does not achieve any specific development objective beyond increasing business profits. The panel offered no evidence demonstrating that general business subsidies stimulate business growth.

The ETP staff also maintains that since the program is supported by a tax on business, funding the ongoing training costs of some firms is merely returning the panel's money to its source--business. This argument, also, is invalid. Individual businesses do <u>not</u> have an automatic claim to ETP funds. While it is true that ETP is supported by employer-paid taxes, it does not follow that any particular firm deserves ETP support simply because the employer pays its taxes. State law clearly identifies the types of projects that qualify for ETP funding. Because statutes do not permit all employer training to be subsidized by the panel, the panel's claim that it is permissible to support the ongoing training needs of firms simply because the funds came from the employers themselves is not relevant to the issue at hand.

ETP Needs to Implement Written Standards for Potentially Displaced Worker Training Projects. In order to ensure that ETP-funded training does not merely supplant employer-paid training and that only those workers who truly are potentially displaced receive training under the program, the panel needs to adopt written standards defining the permissible types of potentially displaced projects. At a minimum, these standards should include the following:

- Employers should be required to certify that trainees would be laid off within one year if training is not provided. The panel would identify the type of information that firms need to provide in order to demonstrate that layoffs would, in fact, occur without training.
- Employers should be required to certify that they would not retrain their employees without ETP subsidies. In effect, this requirement would exclude firms maintaining no-layoff policies from participating in any potentially displaced projects. These firms, however, could participate in ETP projects that train the unemployed. The panel would define what information an employer must submit in order to demonstrate that the proposed training would not have occurred without ETP funds.

Accordingly, we recommend that ETP adopt written standards defining permissible types of potentially displaced projects that incorporate these standards.

Is ETP Reducing UI Benefit Costs?

A major goal of the ETP program is to reduce Unemployment Insurance (UI) costs.

In theory, the program can affect UI costs in both the short and long term. Short-term savings may result if ETP trainees find a job more quickly than they would have had they not received training. Long-term savings may result if ETP trainees collect fewer UI benefits over a longer period of time because training provided them with increased job security or stability.

Use of Control Groups. In order to measure the savings to the UI Fund--either long-term or short-term--one needs to compare the number of weeks that UI benefits are paid to ETP trainees as well as to a similar group of UI recipients. One way of making such a comparison is to randomly assign individuals at an ETP site to test and control groups. The test group would receive ETP training, while the control group would not receive training.

In 1983, we requested that the panel establish such groups at one or more ETP sites in order to provide the Legislature with the data needed to evaluate the impact of ETP training on UI benefit costs. The panel denied our request, citing as its reason potential employer dissatisfaction.

Computerized Data Needed. A second way of establishing test and control groups is to use readily available statistical data. The test and control groups would be created using statistical techniques that compare the personal attributes of ETP participants and nonparticipants. In making such a comparison, the trick is to eliminate any variation in the amount of UI benefits collected by ETP and non-ETP participants that result from differences in personal attributes (such as education, race, and age), so that only the differences resulting from ETP training are measured. The panel staff advise us, however, that none of the personal data collected from trainees appear in the trainee's computerized file; these data are only stored on paper.

In our judgment, the panel needs to maintain computer-ready data describing the characteristics of its trainees. Not only are such data needed in order to determine if the program reduces costs to the UI Fund, the data are needed in order to describe the types of individuals who receive ETP training. For these reasons, we recommend that the panel maintain computerized data on the characteristics of each ETP trainee.

ETP May Result In Higher Short-Term UI Costs. In the absence of a test and control experiment, it is difficult to determine the exact impact that the ETP program is having on the UI Fund. Nevertheless, our analysis leads us to conclude that, in the short term, ETP probably increases costs to the UI Fund.

The average ETP training course lasts 12 weeks, during which time trainees receive UI benefits. The average UI claimant receives benefits for 16 weeks. Thus, a direct comparison shows that ETP trainees receive 4 fewer weeks of UI benefits than the average UI recipient, thereby resulting in lower costs to the UI Fund.

Most unemployed ETP trainees, however, undoubtedly receive UI for a number of weeks before entering the program. We do not know how many weeks of UI benefits panel trainees received before entering training. If, however, the average ETP trainee received more than four weeks of UI benefits prior to training, the trainee would receive UI benefits during a greater number of weeks than the average UI recipient.

We believe that the average ETP recipient probably receives more weeks of UI benefits than the average UI recipient. This is because the unemployed probably are not likely to opt for training--and continuing unemployment--unless all reasonable employment opportunities have been exhausted. In most cases, we believe that individuals are likely to spend more than four weeks exploring available employment options. For this reason, we conclude that at least in the short run, ETP increases outlays from the UI Fund.

It should be pointed out that UI benefits are available to any eligible UI recipient who receives training under EDD-approved programs. Thus, to the extent that some ETP trainees would have received training from other sources had the panel program not been available, the marginal cost of ETP training to the UI Fund is correspondingly reduced. We have no data indicating how many program participants might have sought other training opportunities.

In the case of those who qualify for ETP training as potentially displaced workers, there is no increased costs to the UI Fund, since these trainees do not draw UI benefits during the training period. On the other hand, this training probably does not reduce UI Fund outlays, since many potentially displaced trainees were not in danger of losing their jobs. Thus, training these workers may not have any appreciable short-term impact--positive or negative--on the UI Fund.

Long-Term Impact a Matter of Speculation. Currently, there are not sufficient data available to evaluate the long-term impact of ETP on the UI Fund. To conduct such an evaluation, one would need two or three years of data on the post-program job experience for ETP trainees. These data would allow us to compare the trainees' job histories and income with that of non-ETP workers. Since most ETP trainees have graduated within the last six months, the data needed for this type of evaluation will not be available for quite a while.

It is difficult to construct even a theoretical model of how ETP training affects the UI Fund over time. Nor can we estimate the impact by reviewing other programs that are similar to the panel program. Unfortunately, there is almost no information on the long-term effect of providing skill training to the types of people served by ETP. In general, we know that increasing education translates into higher incomes and more job stability. Panel staff believe that ETP training will increase the employment stability of trainees, thereby making it less likely that they will collect UI benefits in the future.

We believe that the nature of a particular industry may have a greater impact on job stability than the skills possessed by workers in the industry. For example, it is not clear how the skills of manufacturing workers could prevent layoffs when additional training made available by ETP may not substantially reduce the incidence of unemployment in the future. At the current time, we do not know enough about the impact of ETP services to offer any assessment of ETP's long-term impact.

ETP's Contribution to Economic Development Could Be Increased

During our review, we were unable to determine to what extent the ETP program has stimulated economic development in California. In attempting to do so, we encountered the same kind of problems that we faced in trying to assess the program's impact on the UI Fund: the absence of a control group. In order to accurately measure the program's effect on the economy, we need to understand how ETP funds affect the success of firms receiving ETP subsidies. There is no accurate way to measure the program's impact without establishing test and control groups of firms (one group of firms receiving ETP funds, another group barred from receiving any program subsidies). Since no control group has been established, the impact of ETP subsidies on firms cannot be measured.

Based on our review, we believe it is unlikely that ETP subsidies can make the difference between financial survival and failure for most firms. Most of the firms receiving program subsidies are large and can afford the cost of training. Consequently, ETP subsidies probably do not dramatically affect the success of these firms. While the program also helps small, less successful businesses, these firms usually have more pressing problems than inadequately trained staff. For instance, additional training usually cannot dramatically improve the productivity of a firm that uses obsolete, inefficient equipment.

Under certain circumstances, however, ETP probably _can_ improve a firm's chances of surviving. Specifically, the panel can help ailing firms that are seeking to alter their production methods in order to stay competitive. To qualify for ETP funding, these firms would need to demonstrate that workers would be laid off without the change in production methods.

In these cases, it matters little that ETP subsidizes training, rather than some other cost of doing business. True, training must constitute part of a firm's strategy in order to qualify for ETP funding. The firm's dilemma, however, is that it cannot raise sufficient _capital_ to finance its improvement program. Thus, ETP's value to the firm, and therefore, to the state's economic development, is as a source of cash to business.

The panel spends significant resources to help ensure that the program is available as an economic development tool to ailing firms. For example, ETP pays the Department of Commerce and the California Association for Local Economic Development (CAL-ED) to make firms and local economic development agencies aware of ETP's potential value to endangered firms. We believe the panel should be commended for its efforts to make ETP a valuable economic development tool.

ETP Should Increase its Focus on Small Business. Even though the absolute impact of ETP on economic development cannot be measured, our analysis suggests that ETP funds could be used in a manner that would have a greater impact on the state's economy.

It is unlikely that ETP can help a firm survive when it otherwise would fail. On the other hand, ETP subsidies can help smaller, less well-capitalized firms grow. We would expect that government subsidies would have a greater positive impact on smaller firms than on larger, more stable firms, simply because the smaller the firm, the larger the proportional impact of subsidies on cash flow and profits. It seems unlikely that the expansion plans of large firms would depend on a relatively small government subsidy.

According to ETP, 61 percent of its projects involve large businesses (more than 50 employees); the remaining contracts are with firms that have 50 or fewer employees. We believe that the panel's definition of a "small" firm is too imprecise, since 50 employees may be a large or small number depending on what the firm produces. A 50-employee car manufacturing company, for instance, would certainly be considered a small firm. On the other hand, a car repair firm with the same number of employees would not be considered small. Because ETP does not incorporate such distinctions into its definition of small business, we believe that the panel's penetration into the small business sector of the economy is not as significant as its data indicate.

Moreover, the panel currently does not have good ways to serve small existing firms. On the one hand, ETP contracts with the California Manufacturers Association to market the program as well as develop specific training contracts with employers using panel subsidies. The association, however, primarily serves larger firms--not small businesses. On the other hand, ETP contracts with the state Department of Commerce and CAL-ED to market the panel program to economic development agencies. These entities tend to focus on the needs of new businesses in an area, not on the needs of existing small firms.

To increase small business access to ETP funds, we recommend that the panel prepare a written plan for increasing the participation of small firms in the program. As part of this plan, we recommend that the panel include (1) a more specific definition of "small" business, (2) a discussion of how small firms train employees in industries where small business expansion is a major factor for growth, (3) an analysis of how training could improve the growth potential of these small firms, and (4) how ETP can influence the training plans of these employers.

CHAPTER IV

ADMINISTRATIVE ISSUES

In this chapter, we review ETP's administrative procedures. This review was conducted during the fall of 1985. Our findings and recommendations are based on program operations at that time and do not reflect any subsequent changes that may have been made by the panel.

We find that the panel has officially adopted no regulations and few program guidelines or procedures. This gives the panel considerable flexibility in operating the program. On the other hand, the lack of written guidelines creates uncertainty as to what the panel expects of its contractors. In addition, the lack of policies governing contract reimbursement rates may cause program costs to be higher than necessary.

Our review also indicates that additional limits on ETP funds are needed in order to prevent the accumulation of large amounts of unspent funds. We find that ETP probably will not be able to spend more than half of the amounts appropriated during the program's first two years of operation. With this in mind, we recommend that the Legislature adopt fiscal controls that will enable the panel to spend its funds appropriately but not allow the panel to carry funds over from year to year.

ETP Needs to Adopt Regulations

Setting standards, establishing procedures, defining terms--all constitute a necessary precondition for a smooth-functioning program. Our review of the ETP, however, indicates that the panel still has not adopted all of the policies, procedures, and standards needed to guide the program.

For example, the panel has never officially adopted minimum standards for use in evaluating training proposals, even though the law requires it to do so. Employers and training agencies need such standards in order to know what types of training projects ETP will support. Without this information, employers are forced to guess what types of training projects the panel will fund.

Panel staff indicate that each training proposal is evaluated individually and that setting standards would reduce the panel's flexibility in meeting the training needs of business.

We believe that while some flexibility is desirable, regulations must be adopted if the panel is to achieve the Legislature's objectives. We have identified three general areas where regulations are needed: (1) program standards and definitions, (2) procedures for conducting business, and (3) program policies.

Program Standards and Definitions--What Constitutes a Job That Offers "Long-Term Job Security and Career Potential." Existing law requires that the panel support training in jobs with "definite career potential and long-term job security." These terms have never been defined. In other words, the panel has never determined how this requirement should influence the kinds of training projects that are funded under the program.

Our review indicates that the panel has subsidized training in occupations that exhibit questionable career potential. For example, the panel has approved a project to train auto parts counter persons. On the surface, this type of job would not appear to provide much career potential, in terms of entry into the middle and upper levels of a store's hierarchy. Without a working definition of "career potential," however, the Legislature is not in a position to evaluate the sales clerk project.

Other terms that are found in ETP authorizing legislation which still lack definition include "critical skill shortage," "areas targeted for economic development," and "qualified training agency." Because these concepts play a crucial role in the design of the panel program, the Legislature needs a precise definition of them in order to understand how the panel is implementing the program.

Procedures--Under What Circumstances Does ETP Allow Amendments to Contracts? The panel often amends training contracts after it has given final approval to the contracts. These amendments can alter any aspect of the contract, from the number of trainees to the cost of training. The panel has no written guidelines that specify the process which contractors must go through in order to obtain amendments. Nor does it limit the types of amendments that would be considered, the circumstances under which proposed amendments would be denied, and the timelines for panel action on proposed amendments. As a result, amendments are considered and granted without any apparent rationale or predictability.

In addition, the panel has not adopted (1) criteria for determining whether a placement is allowable under ETP, (2) timelines indicating when the panel will approve or deny project placements, and (3) an appeals process for solving disputes over placements. (Placements may not qualify for ETP payments for a number of reasons. For example, placement in an occupation that is "substantially different" than the one a person was trained in does not qualify for reimbursement.)

Our review indicates that almost all ETP administrative procedures must be clarified in order to rationalize the operation of the program.

Policies--How Much Should ETP Pay Its Contractors? The ETP legislation exempts the program from the state's competitive bidding process, thus allowing the panel to determine the price it pays for training. Obviously, therefore, a critical concern to the Legislature is the price that ETP pays for training.

According to panel staff, prices paid for training (as well as for marketing activities) result from a "bottom-up" budgeting process that reviews the appropriateness of proposed expenditures. Specifically, the panel requires firms to submit a line-item budget showing proposed expenditures for supplies, equipment, utilities, etc.

Our review of ETP's price determination process suggests that most prices are determined before detailed budgets are submitted to the panel and that no panel policies currently guide the price-setting process. Generally, prices are negotiated along with the proposed program outline--the employer or training agency proposes a price; the panel staff responds with a counteroffer. It is not clear how the panel staff determines the price of its counteroffer.

The lack of policies governing contract prices has resulted in an inconsistent pattern of reimbursement rates as illustrated by Table 6. The table shows the cost per trainee and the cost per trainee-hour for six projects training individuals to be "automated office specialists." As the table indicates, the cost per trainee-hour varies considerably, from a low of $2.22 to a high of $16.81.

Some price variation is unavoidable, due to differences in the cost of living, the length of training programs, and other factors. The different reimbursement rates shown in Table 6, however, are far larger than what can be explained by these factors. For instance, ETP pays Sawyer College almost twice the hourly rate paid to San Mateo College for almost the same total number of training hours. Table 6 also indicates that ETP pays Los Angeles Community College District 26 percent more for 100 hours of training than it pays San Mateo College for <u>600</u> hours of training. We know of no reason why costs in Los Angeles should be so much higher than costs in San Mateo.

Table 6

ETP Reimbursement Rates for Training Persons to Be Automated Office Specialists

Training Agency/ Employer	Hours of Training	Cost Per Placement	Cost Per Training Hour
San Mateo College	600	$1,334	$2.22
Sawyer College	620	2,715	4.38
Metro Enterprises	150	1,250	8.33
Glendale College	190	1,977	10.41
Lockheed	100	1,150	11.50
Los Angeles Community College District	100	1,681	16.81

<u>ETP Needs to Adopt Concise, Complete Regulations</u>. The panel's staff argues that many of the terms or standards that we believe have not been adequately defined are either established in law or through an ETP policy. Staff advise, for example, that a definition of "qualified training agency" exists in law. This definition, however, is incomplete. The panel still needs to adopt criteria for determining what constitutes a "qualified"

training agency under the ETP program. For instance, the law states that qualified agencies must demonstrate a "satisfactory record" of placement performance. The panel has never defined what placement history by a training agency is considered "satisfactory." State law also requires training agencies to demonstrate labor market demand for the proposed training. The panel has not established how these agencies should demonstrate labor market demand for its proposals.

In view of these limitations, we recommend that the ETP adopt concise, comprehensive regulations in order to clarify the program's standards, policies, and procedures. We further recommend that the panel adopt these regulations in accordance with the state Administrative Procedures Act.

Limits Needed on ETP Funding

State law limits the amount of funds collected by the ETT and deposited in the ETF to $55 million annually. Any collections which exceed $55 million revert to the UI Fund.

Table 7 shows the panel's revenues, expenditures, and encumbrances for the period from 1982-83 through 1984-85. The table shows both expenditures and encumbrances because most of the funds that are obligated for support of training projects have not actually been spent.

Table 7

Employment Training Panel
Revenues, Expenditures, and Encumbrances
1982-83 through 1984-85
(in thousands)

	1982-83	1983-84	1984-85	Total
Revenues				
ETF	$26,000	$50,850	$55,000	$131,850
Interest earnings	265	4,871	5,500	10,737
Carry-over from prior year	--	23,141	24,924	NA
Total revenues	$26,265	$78,862	$85,424	$142,486
Expenditures				
Administration	$1,675	$3,105	$4,580	$9,360
Encumbrances				
Training projects	$1,449	$50,833	$48,539	$100,821
Carry-over to next year	23,141	$24,924	$32,305	$32,305

As the table indicates, the panel has not spent or encumbered all of the funds available to it. Since the beginning of the program, the panel has received $32.3 million more than it could spend or encumber. These funds remain in the ETF and are available for expenditure without regard to fiscal year.

Our analysis indicates that as of the fall of 1985 the amount of uncommitted funds--funds not reserved for <u>specific training projects</u>--was significantly larger than $32.3 million. This is because some encumbered funds which were set aside for master contractors and letters of intent had not been committed to a <u>specific</u> training project. For example, under one master contract, the California Manufacturers Association (CMA) encumbered $4.87 million in ETP training funds, of which only $1.1 million had been

We believe this change would encourage the panel to obligate only the amount of funds needed for specific projects and help prevent situations in which the panel accumulates large amounts of uncommitted funds. Such a change in law would not jeopardize the panel's contracts with master contractors and letter of intention agencies. The panel could honor its obligations out of a subsequent year's appropriation. For instance, if a contractor committed $3 million out of $5 million by the end of 1985-86, the panel could fund contracts developed during 1986-87 out of the ETP's 1986-87 appropriation.